

## Corporate Governance

# Processes and Practices of the Board of Directors

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### Overview

The Premier Board of Directors has long endorsed good governance practices and in recent years has taken significant steps to enhance its governance policies. In 2003 the board approved adoption of the recommendations of business ethicist Kirk Hanson, designed to lead the industry in the implementation of exemplary business practices and a transparency of purpose and practice not seen before in a healthcare alliance. The recommendations of Professor Hanson, together with adoption of governance best practices based on the Sarbanes-Oxley Act of 2002, formed the foundation for development and implementation of Premier's present governance principles and practices; they have been fine-tuned since then. These principles are reviewed annually by the Governance Committee and appropriate enhancements are recommended to the full board. It is significant to note that Premier was not required to adopt Professor Hanson's recommendations nor the requirements of Sarbanes-Oxley; rather it chose the stringent models of best practices and transparency on a voluntary basis as a measure of its commitment to governance leadership within the organization, its business segments, and the healthcare industry. A compliance program is in place, and the Ethics and Compliance Officer, who reports directly to the Audit Committee of the board, is responsible for the effective operation of the program. The adoption of these governance policies

and practices have placed additional responsibilities on management and clarified the oversight duties of board members.

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### **Role and Responsibilities of the Board**

Premier is owned by hospitals and health systems across the nation. The Board of Directors is elected by these Premier stockholders to oversee the management and conduct of Premier's business by its chief executive officer and management and to enhance the long term value of the company for the benefit of its stockholders within the context of its vision and purpose. The fundamental responsibility of a director is to exercise common sense business judgment. This requires skepticism, diligence, and a willingness to ask tough questions, while insisting the answers received are understandable. It requires a level of prudence in making sure the company does not take on an undue level of risk and a level of vigilance in making sure that any compliance criticism or identified audit or control deficiencies are quickly and appropriately addressed. The core responsibilities of the Board of Directors are:

- To select the chair of the board.
- To select, evaluate, and compensate the chief executive officer.
- To oversee management succession planning.
- To provide counsel and oversight in the selection and evaluation of senior management and to approve the compensation program for senior management.
- To review and approve management's strategic plans, annual, and long-term goals.
- To provide counsel and oversight with respect to corporate performance and to evaluate results compared with strategic plans, annual, and long-term goals.
- To review and monitor the company's financial controls and reporting systems.
- To review and approve the company's financial standards, policies, and plans including distributions to stockholders.
- To review and approve the independent auditors engaged to audit the company's financial statements and to oversee the internal audit function.
- To review the company's ethics standards and legal compliance.
- To provide counsel and oversight with respect to relations with stockholders, customers, employees, and the communities in which the company operates.
- To identify candidates for election to the board.

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### **Board Size, Qualifications of Directors, Chair**

The number of directors is currently fixed at 15. The board has adopted a set of Criteria for Nomination to the board as a guideline for the Committee on Directors in evaluating and nominating board candidates. The board recognizes that criteria change as the membership of the board changes and takes into account the current make-up and requirements of the board in its nomination process. Two additional stockholder representatives participate in the nominating process. As part of the company's governance review and best practices implementation in 2003, the positions of board chair and CEO were made separate offices.

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### **Board Meetings**

The board has 12 regularly scheduled meetings each year, three of which are in-person meetings. The first in-person meeting of the board is held in conjunction with the Annual Governance Education Conference in January. A multi-day strategic planning retreat is held in April and the Fall meeting is planned to coincide with the Annual Meeting of Stockholders. On the third Friday of each of the other nine months a conference-call meeting is scheduled, ordinarily lasting one hour. Committees generally schedule meetings during the in-person meetings and arrange phone conference or in-person meetings throughout the year as necessary.

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### **Director Evaluation and Tenure**

The board participates in an annual board assessment and quadrennial self-assessment designed and administered by outside consultants. The results are presented at the April in-person meeting. Follow-up is scheduled through designated committee agenda items. There are no term limits for outside directors or the chief executive officer directorship. Under current policy stockholder directors are limited to two full three-year terms. Recognizing the value of the Premier board experience in selecting a chair and in light of the separation of the chief executive officer and chair positions, the Premier By-Laws were amended to make available an exception to the stockholder director term limit provision which permits a stockholder director chosen as chair late in his or her tenure to serve a minimum two-year term as chair. This policy, as well as all board policies, continues to be reviewed as the impact of the best practices and policies on the effective operation of the company is evaluated.

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### **Committees**

Standing board committees are the Audit, Governance, Compensation, and Special Committee. Composed entirely of directors, these committees act in accord with their established charters and meet during in-person meetings of the board or as otherwise needed. Two other committees designated as *stockholder committees* are composed of executives of Premier stockholder

organizations that are not members of the board. They are the Group Purchasing and Member Relations Committee and the Quality Improvement Committee. Members are appointed to these committees by the board, act in accord with their established charters, and typically provide reports to the board at its in-person meetings.

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### **Composition and Independence of the Board and its Committees**

The board is divided into three classes with staggered terms of three years each. The term of one class expires at each Annual Meeting of Stockholders; thus, directors typically stand for election every three years, unless they are filling an unexpired term. When a director is appointed by the board to fill a vacancy in any class, the appointed director stands for election by the stockholders at the next Annual Meeting of Stockholders.

Given the nature of Premier's business, its structure, and its relationship to its stockholders, Premier looked to outside counsel to evaluate the issue of "independence" as it applies to board members, and to develop a definition of an independent director for the company. The definition recommended to the Premier Board by counsel at the Paul Hastings Janofsky & Walker, LLP law firm was incorporated into Premier's By-Laws. It states that a director is independent if he or she (i) does not accept directly or indirectly any consulting, advisory, or other compensatory fee from Premier and its related companies (other than as a board member), and (ii) is not an affiliate of Premier or its related companies. Affiliate means a person or entity that directly or indirectly controls, or is controlled by or under common control with the person or entity. Control means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person or entity, whether through the ownership of capital stock entitled to vote, by contract or otherwise.

The Paul Hastings law firm memo stated that a commercial relationship between Premier and a company whose CEO is on Premier's Board should not constitute an indirect payment by Premier to this CEO, and accordingly does not, in and of itself, destroy the CEO's independence. Counsel further pointed to the safe harbor contained in the Sarbanes-Oxley Act which provides that owners of less than 10 percent of the reporting company's stock are not deemed to be affiliates. Since no Premier stockholder owns 10 percent or more of Premier stock, a CEO Director would not run afoul of the independent definition under Sarbanes-Oxley, a definition that specifically applies to public companies. The charters of all committees provide that all committee members must be "independent" according to the definition set forth in the company's By-Laws. A Conflicts of Interest Policy and Process is in place to ensure that conflicts or relationships with the company do not compromise directors' independence on any particular issue or vote.

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## **Director Compensation**

The Governance Committee has the responsibility for reviewing and recommending to the board compensation and benefits for non-employee directors. Board members who are executives of stockholder hospitals or health systems are not compensated individually for their board service; rather, their stockholder hospital or health system receives the compensation credited to their chief executive officer for board service. Outside directors, that is, those that are not executives of a stockholder hospital or healthcare system, are compensated as individuals. Directors who are employees of Premier, Inc. or its affiliates receive no compensation for their board service. With the assistance of the Governance Committee, the board reviews Director compensation policies on an annual basis to ensure that Premier is in a competitive position to attract directors with the expertise, experience, and standing to provide Premier and the healthcare industry exemplary leadership.

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## **Evaluation of the Chief Executive Officer**

The performance of the chief executive officer is reviewed annually at the Fall in-person board meeting based on a formal CEO evaluation process adopted by the board. This process includes a CEO self-assessment, a multi-source feedback appraisal administered by an independent third-party vendor who collects confidential input from the board chair, committee chairs, and CEO direct reports, and it may include performance input from other board members, owners, and business partners. The evaluation includes an analysis of achievement measured against strategic annual and long-term corporate performance results. In addition, outside consultants provide a competitive compensation analysis to the Compensation Committee. The committee considers the market data, multi-source appraisal and goal performance results, in consultation with the board chair, to determine final CEO performance evaluation and compensation recommendations to present to the full board. The chair leads the evaluation of performance and achievements of the CEO in executive session of the board assisted by the Chair of the Compensation Committee. The recommendations are considered and acted upon by the board. Feedback is provided to the CEO.

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## **Review of Management and Succession Planning**

The Chief Executive Officer provides the board with background and development of each member of senior management at the April retreat. At that time the board reviews and updates the management succession plan.

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### **Executive Sessions**

Executive sessions of independent directors, held outside the presence of members of company management are scheduled at each of the three in-person board meetings and may be called at any other board or committee meeting.

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### **Board Process and Deliberation**

The CEO and chair work together to set the board agenda. Board members are invited to make agenda suggestions. To facilitate deliberations at board meetings, appropriate information and data important to the directors' understanding of the issues are provided to directors in writing before each meeting, unless sensitivity requires presentation at the meeting. Committees assist the board in reviewing detailed information and making recommendations to the full board and by completing assigned tasks.

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### **Director Access to Management**

Executive management members are invited to make presentations and reports related to their respective organizational units or company strategic issues at board meetings and to interact with board members on a regular basis. Management also staff board committees.

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### **Retention of External Advisors**

The board and its committees may retain external advisors as necessary in the discharge of their responsibilities. The Audit Committee regularly consults with Ernst & Young, the company external auditors and with KPMG, the internal audit service provider. The Compensation Committee utilizes Mercer to provide on-going analysis and advice in carrying out its responsibilities to the board related to executive compensation strategies, programs and plans. The Governance Committee engages Nygren Consulting to administer the board assessment program. The Governance Committee also consults with outside firms on various director policy matters and also has utilized Mercer in its review of director compensation.