Article # 1

Introduction to privately held company boards of advisors

As the owner of a private company you may at times feel it is “lonely at the top.” The use of a board of advisors is one way to overcome that sense of needing to fill gaps in experience or expertise. As an owner of a private company making a decision to form a board of advisors is an effective and efficient way to fill the voids or gaps in experience. A board of advisors is a resource for ideas, feedback and insight.

“If you are a student of the game, you understand what you want to get done strategically and the extent of your talent in that area”

“So surround yourself with a board of people who are as smart as you can possibly find. You don’t always have to agree with them but you had better listen to them.”

That is a quote from Jack Kahl, founder and retired chairman of Manco Inc. of Avon, Ohio. Jack built a successful business growing from less than $1 million dollars to more than $250 million dollars.

Jack’s company successfully served the largest and best retailers in the world and effectively competed with companies more than 10 times his company’s size. He created a seamless environment from his suppliers, through his company, out to his customers and on to his consumers.

As the company grew, circumstances changed, challenges became bigger and the stakes became larger. Jack searched for and found advisors who could be supportive, constructively critical, challenging and independent. His advisors were intelligent, experienced, articulate people who filled specific needs for his growing company.

Over a dramatic growth period of more than twenty years Jack gave full credit for success to his board of advisors. His board of advisors was one of his key competitive weapons.

This series of articles on forming and using a board of advisors for privately held companies will draw on my own experiences serving on boards and on the experiences of Jack Kahl and other executives who have used their boards to effectively achieve outstanding results. The articles will focus on when, what, how and why to form a board of advisors.

The benefits of forming and effectively using an outside board of advisors include improved management focus and performance. It facilitates effective decision making, better selection of options and it leads to a higher probability of success not only for the owner but also for the stakeholders.

There is no single model for a successful board of advisors. There are, however, principles and steps that will optimize the value for both the owner and for the paid professional managers in the business.

The steps described in this series of articles are presented below:

- Introduction to privately held company boards of advisors
- When should a company consider an outside board of advisors
- What is a board of advisors in a privately held company
- Factors to consider, resolve and formalize prior to forming a board of advisors
- How does the owner nurture the advisory board to keep it vital and valuable
- How to maintain value in your board of advisors
- Additional tips on effectively utilizing your board of advisors
- Board of advisors composition and compensation

You can take a number of actions in the process of forming and utilizing a board of advisors that will help you develop and gain the full potential from a successful and productive board. They include: detailed planning, benchmarking with successful owners who have experience with productive boards, and defining the specific benefits to the company.

Taking these actions will provide a good foundation for your own board of advisors.

Article # 2

<u>When should a company consider an outside board of advisors</u>?

The most direct answer to that question is now!

Take some time to look at the privately held companies in your area, both inside and outside your industry. You will see that most of the successful and recognizable companies not only have an outside board of advisors, they utilize them to benefit the company's decisions and results. The CEOS recognized as "outstanding entrepreneurs," and companies known as "growth" companies or "top fifty" companies to work for have outside boards of advisors.

A number of signs or conditions indicate clear signals it is to a company's advantage to form a board of advisors. They include:

<u>When it begins to feel lonely at the top!</u>

The owner feels isolated from the professional managers hired to run the business, or the decision process in the company directs all the decisions to the owner. An outside board can help the owner make timely, objective, informed decisions.

An effective board can assist the owner in productively engaging the paid managers of the business, making them more valuable, action oriented and accountable for results.

<u>When size and scope become weighty</u>!

While size and scope may be clear indications that outside, independent support may benefit a company, it is not necessary to wait until that time. Starting early when the company is small is even better for the long term growth of the company. Increased complexity and the need for sustainable growth are conditions that call for enlisting specific expertise from outside advisors.

<u>When the competitive curve steepens</u>!

Today's environment of industry consolidations means that competitors continue to get larger and have access to greater pools of resources. In most industries consolidation is a fact of life. Only the strong and the nimble will survive. An outside board of advisors can bring specific experiences and skill sets, help you deal with industry consolidation issues, and regain a competitive edge for your company.

<u>When outside objectivity and advice have the potential to add value</u>!

As companies grow and become more complex the gaps in a company's resources, skills and core competencies tend to widen. This makes the company more vulnerable to the market and success more problematic. Identifying and filling the gaps with outside advisors is a valuable and effective solution to this problem.

<u>When "globalization" becomes a factor</u>!

Technology and communication have made the business environment a "global village" for even the smallest businesses. Today a competitor can be any place in the world. Assuring success in this more complex and competitive world calls for the use of advisors with global experience and global vision.

<u>When the economy challenges results</u>!

Whether the economy is strengthening or weakening it presents unique challenges to a company. These externally driven circumstances are not directly controllable by the enterprise. Dealing with these complex issues opens another opportunity to look for solutions in the formation and effective use of an outside board of advisors.

<u>When the owner recognizes the low risk, high value potential</u>!

A surprising number of owners have a "fear" of losing control or admitting they need help. Remember, you don't have to agree, you only have to listen to your board of advisors. There is no loss of ownership, authority or financial control. An owner who uses a board of advisors has the opportunity to see his business through new eyes and find new solutions backed by experience.

When succession or mentoring the next generation is a looming issue.

As soon as an owner begins considering the issues surrounding passing the baton to the next generation or when it is recognized that the professional managers in the business can gain from mentoring it is time to turn to an outside board of advisors. A board can provide new eyes to evaluate the performance and potential of either designated or to- be-identified successors or key managers in the business.

When the inside becomes mentally and creatively isolated from the outside.

When the management of the business is in place for a long period of time or when the frequency of fresh thinking and the challenging of the old guard is infrequent it is time to bring in a board of advisors.

In today's competitive market delaying the decision to use an effective, outside board of advisors is not only a costly decision but also a missed opportunity for a competitive advantage and improved results.

No matter which reasons you choose from this article to bring in an outside board of advisors, remember the gains are a function of taking the appropriate steps to put a board in place and using the board effectively.

Article # 3

What is a board of advisors in a privately held company?

From a practical point of view a board of advisors in a privately held company is a resource for new thinking and fresh ideas. It is an opportunity to install added discipline into the workings and processes of the company. Outside advisors bring balance to the decision process and experience to the key issues at hand.

In order to address some of the typical fears heard from owners of private companies about creating a board, the following article describes the differences between a public company board of directors and a private company board of advisors.

In a public company a board of directors is a legal requirement. The board of directors represents the company's shareholders. It provides governance. It is the role of the board to hire, hold accountable and when necessary fire the CEO. A board oversees procedural and regulatory compliance and plays the central role in the statutory and fiduciary duties and responsibilities of the company on behalf of the shareholders.

In contrast, in privately held companies a board of advisors is serving at the option and pleasure of the owner or CEO. It is an outside resource that brings value-added perspective and constructive insight to the problems and opportunities of the company. A board of advisors brings fresh thinking and fills expertise gaps.

Another key role for a board of advisors is to provide objective and experienced evaluation of the professional, senior managers in the company. Using the board of advisors as mentors for the professional managers as well as for the next generation owners brings unique and valuable contributions to the company.

In companies where multiple family members are engaged in the management of the company the board of advisors can serve the role of helping to organize the experience and potential of family members. The board can play a role of not only mentoring but also evaluating the next generation to best serve the company. The advisors can play an important role in assuring the optimum long term results for the business. The board of advisors can shoulder the responsibility for the best succession decisions.

Another unique role of a board of advisors in a privately held company is to send a clear message of openness and fairness to employees, suppliers and customers. To each of these groups the use of an advisory board is a message that the owner is willing to listen and to be challenged in a constructive way for the benefit of all.

My friends in the legal profession do make a clear distinction between the definition of a board of directors and a board of advisors in a privately held company.

In my experience, serving on multiple private company boards, the success of the process is not in what it is called but in how it is organized. The successful use of a board of advisors is driven by setting clear direction and discipline for the involvement of the board.

There may be a benefit in choosing either description the owner decides to use for the board. Each of the choices communicates unique messages the owner may wish to send to employees, suppliers and customers.

The term “board of directors” may send a more formalized and serious message than the term “board of advisors.” The two terms may each have different impact on the talent attracted by the opportunity to serve the owner and the company.

In the end, however, the results of the use of outside talent to improve the performance of the company are decided by the discipline applied to the establishment and process of using a board of advisors.

So, when you as the owner reach the stage of deciding to form a board that includes members with experience from outside the company, remember, the benefits will come not from what you call the board but in how you constitute the board.

The important steps to remember when creating a board include establishing a clear mission and specific job responsibilities, identifying and filling real gaps in talent or experience, and formalizing job descriptions for board members.

Article # 4

<u>Factors to consider, resolve and formalize prior to forming a board</u>.

Making the decision to form an outside board of advisors is a difficult one for some owners. However, once the decision is made it is critical to take the time to properly prepare for the organization of the board. This article discusses the factors to consider, resolve and formalize before forming and convening a board.

The first step is to develop a clear mission statement for the board. A clear mission statement will give the owner, the company and the board members an explicit understanding of expectations.

Briefly describe the mission of the advisory board in specific terms relative to the mission of the overall company. An effective mission statement will include the following elements:

- to serve the owner by having experience, expertise in specific disciplines

- to provide the owner with independent advice and counsel
- to serve formally through quarterly meetings and informally through communications and meetings as key issues evolve
- to serve as coach or mentor to succession candidates and senior management

Important issues specific to your own company and circumstances can be added to your own list.

Write the mission statement to fit your company needs and your expectations for your board of advisors. The mission statement serves as a guidepost in both selecting appropriate participants and in the effective utilization of your board.

Next, develop a specific list of responsibilities for the members of the advisory board. The following list will provide some examples of appropriate responsibilities:

- bring specific experience and expertise to the board
- elicit superior management team performance
- provide balance and objectivity to the owner and management team
- assist with training and mentoring
- assist in the development of an exit strategy
- enhance intra-company discipline, management style and process
- serve on committees such as audit, compensation, etc.
- attend and prepare for quarterly meetings

- review financial and other critical data of the company
- be available for phone consultations and special meetings
- have company welfare and long term success in mind

Make the job responsibilities of the advisory board fit the needs and objectives of your specific company. By making responsibilities specific the advisory board will clearly understand their jobs and be better able to deliver the expectations of the owner.

The next step to consider and define prior to initiating a board of advisors is to identify specific gaps in experience or expertise that the board can deliver to the company.

Divide your thinking in this step into two categories. First, think of the company functions that might benefit most from broader experience or fresh thinking. Consider the following: manufacturing, marketing, finance, human resources, technical (research and development or information technology), engineering, legal, etc.

Second, think of the processes of the company that might benefit from improvement in performance, from redefining or reorganizing. Consider the following processes: strategic planning, organizational structure, industry processes, customer development, supplier development, market access, team building, communication, etc.

In both the functional areas and the processes of the company identify where the gaps are most apparent and where filling the gaps has the most potential for improving the performance and results of the company. Find advisors who can fill the three or four greatest potential gaps.

The next step is to formalize the job description for the board members. It is suggested that writing a job description for board members can be best developed by dividing the exercise into two components: the qualifying attributes or defined gaps the company most needs to have filled, and the duties expected of the board member.

Suggested qualifying attributes of board members include the following:

- expertise in one or more fields of value to the company
- adding to the chemistry of the board and the senior management team
- thinking and acting responsibly and with independence
- intelligence
- interest in the company and commitment to the company's goals
- respected reputation, personally and professionally

This list is important for board members to qualify for participation. You may want to customize or add to the list but make sure each of your board members deliver, at a minimum, the qualifiers you select.

A second component to consider is specific job duties. The duties can be divided into two parts. The first part is appropriate for all members of the board; the second is specific to individual board members, customized to the expertise brought to the company.

The duties include:

- attending quarterly meetings
- being available for between-meeting communications
- serving on a committee
- maintaining confidentiality
- mentoring a specific manager

Develop a list that both defines the duties and adds to the understanding of performance expectations for board members.

Spending time thinking through and developing clear job descriptions for your board will add to the quality and results delivered. Keep the exercise specific and brief. Write it out formally. Make it available for board candidates when you reach the interview stage of forming your board. And, when your board is operating, use it in evaluating the performance of your board.

Article # 5

How does the owner nurture the advisory board to keep it vital and valuable?

Nurturing your board of advisors is a little like fertilizing your vegetable garden. If you feed and nurture your vegetable garden you will reap a bountiful harvest. If you feed and nurture your board your company will reap the fruits of their participation and contributions.

It takes effort on your part to be sure you are nurturing your board to reap the harvest of their participation, but the returns are dramatic. The methods and steps you take must be customized to fit your company and the mission statement you developed for your board. The items discussed below are designed to get you started thinking about ways you might nurture your board.

Encourage involvement from your board members. You have appointed them to bring their new thinking and their unique wealth of experience to your company. Focus your relationship with each of the board members by drawing from their fresh ideas and perspective. Recruit for “type A” personalities who relish speaking up and taking an active role in the board process.

Open communication, in both directions - you to the board and the board to you- is important in order to extract the value of a board of advisors. Phone your board members between meetings and through informal discussions keep them up to date. Encourage your board members to call you with "between meeting" thoughts and ideas. The more you share the greater the return from your board. The idea of "open ongoing discussion" management is an important way to leverage the value of your board.

Expose management to your board. Your key professional, paid managers are important to the performance of the company. At each meeting select a manager to present a current project or problem to the board. Exposing your managers to the board gives the managers and their team's recognition and increases their pride of ownership in their work. It also gives your board the opportunity to assist you in the evaluation and development of your key managers.

Visit a customer along with one of your board members. Visiting a customer in either a formal or informal setting will give the board member a better understanding of the customer and market environment you are competing in every day. It will bring a new appreciation of the opportunities and problems your company is dealing with. The result may be that the board member may think differently about the business by gaining the perspective of the customer.

Visit a supplier with a board member. Suppliers are an important partner in the supply chain. It is critical for your board to understand the issues between your company and your important suppliers. In addition to encouraging a broader understanding of your company, a visit to a supplier will create an opportunity to bring new thinking and creative ideas to the negotiations between your company and your suppliers.

Give feedback to your board members on a regular basis. When a board member makes a significant contribution to the company in the way of new thinking or creative approaches to solving problems recognize the board member both privately and publicly. Giving credit encourages new levels of participation and contribution.

If a problem arises with a board member have a private feedback discussion and resolve the issue as soon as possible.

Share data openly with your board members. The more you are willing to manage and operate with an "open book" style the more you will get back from your board. Sharing performance data around productivity, market share, operating performance, financial results, customer surveys, and union contracts will enhance your board members understanding and increase their ability to contribute to better performance.

Read a book / share a book is a unique and valuable way to stimulate thinking and generate constructive conversation between you and your board. The best owners I have experienced are readers and students of the business process. When you and your board have read selected current business books and articles and discussed that information with each other you stimulate new thinking and raise the bar for expectations from the business. This is an easy and inexpensive way to nurture both your board and your managers.

In addition to the tips provided above develop your own ways to nurture your board. Time and effort spent on nurturing activities will return benefits to the company many times over.

Article # 6

<u>How do you maintain value in your board of advisors?</u>

Sustainability is always an issue when looking for ways to improve either the results of your business or its functional processes. Maintaining value in your board of advisors is equally important and takes consistent effort on your part as the owner.

The opportunity I have had of participating on a number of diverse private company boards has demonstrated the importance of maintaining a high level of performance and participation. Companies and owners who are up to the task of leveraging the contributions of their board of advisors get repayment many times over. It is one of the secrets of success for companies embarking on the establishment of an outside board of advisors.

The suggestions discussed here are provided as a stimulant to get you thinking about ways you can sustain the value of your board of advisors. Paying attention to these suggestions will assure sustainability in the contributions your board makes to you and your company.

<u>Being a good listener</u> is an important start to maintaining the value of your board. In the first article of this series a quote from the owner and retired CEO of Manco Inc., Jack Kahl said, “You don’t always have to agree with your board but you had better listen to them”. Your board is there to open your mind and your company to their expertise and experience. Your board is there to help you avoid pitfalls they may have experienced or can see from their own experiences.

<u>Have a plan of involvement</u> for your entire board as well as for each member you appoint to the board. If the appointees to your board fill the experience gaps, each one will bring specific strengths to the company. Together they bring you a broader vision. Individually they bring you specific opportunities for success.

<u>Avoid clones</u> on your board. Remember you formed a board to bring in new thinking and to fill gaps in experience. You don’t need more people just like you or just like your managers. Avoiding clones is an opportunity to reach beyond the collective experience of the company.

<u>Encourage new points of view and different thinking</u> from your board. That is why you formed the board. Avoid friends who always agree with you and bring neither new experiences nor new thinking to the company. They will do

you no favor and the company will miss the opportunity to grow to new levels of success.

Add diversity as a supplement to ability and experience gaps. Board members from completely different industries and experiences bring new points of view. All the new thinking is not in your own industry. Transferring knowledge or experience across industries often brings competitive advantage.

Avoid appointing professionals whom you already pay for advice. Appoint board members who bring new exposure, new experience and new thinking to the table. If the legal, accounting or other professionals you already are paying are bringing you the value you are paying for, then putting them on the board takes the place of someone new and unique to the identified gaps in the experience of the company.

Establish and stagger terms of service so you have the opportunity to gradually turn over your board as the needs of the company change. For example, if you have three outside board members, stagger their terms of service so you turn over only one board member each year. Be flexible. If an existing board member remains valuable extend the term of service. Opt for a size that is manageable. Be adaptable so you can thank and excuse a current board member or add a new board member as the situation demands. When considering board terms of service have a goal of maintaining balance and continuity that meets the needs of the company.

Compensate fairly when appointing a board member. Benchmark the experience of your peer company owners and discuss compensation openly with potential candidates. In most cases this is not a board member's livelihood and payment is generally proportionate to the size of the company, value of the input and expectation of involvement. Compensation may be in cash, in a form of equity or a combination of the two.

Maintaining value comes from paying attention to the suggestions discussed in this article. It is also a function of common sense and fairness from both the owner and the board appointees.

As you experience the development and contributions of your board you will find other powerful ways to leverage the return for the time and effort spent in appointing and using an outside board effectively.

Article # 7

Additional tips on effectively utilizing your board of advisors

Forming and maintaining a board of advisors that brings long term value to the owner and company takes detailed up front planning. It takes attention to details as well as a willingness to allow the process to grow and evolve to meet the needs of the company. It takes discipline to keep the process effective and valuable.

In situations where both the owner and the board perceive the value of an effective board the odds are both parties will work to continually improve the process. In these cases the business has a competitive edge. Not all advisory boards are effective. I can attest from personal experience the best ones are in companies with open minds, open books and a management team that thrives on new thinking and major challenges.

This article focuses on the procedures and disciplines found in effective boards of advisors. As you gain experience with your own board you will customize procedures that best fit your company, your management team, and the goals you set for your board of advisors.

Meet quarterly, or as appropriate, with your board of advisors. Most private companies find quarterly meetings sufficient. At times special meetings or conference calls may be necessary or valuable.

Have an agenda ahead of time in the hands of the board members and the company managers who will be attending the meeting. Providing lead time of a few business days to a week is usually sufficient. This allows for preparation and greater participation adding value to the meeting.

Send out data and results ahead of time to all participants. This allows everyone to be up to date and ready to discuss the real issues without time spent on background information. Material sent prior to the meeting should include financial data, as well as key business results such as productivity, status of major capital spending initiatives and progress on important projects.

Communicate important information between meetings to the outside board so they stay abreast of milestone activities. Keep the updates simple. Substituting visual graphics for narrative description can facilitate and highlight important information.

Present one major functional discipline at each meeting to give the board exposure to both key managers and key projects of the company. The company will gain valuable input while the board will gain valuable insight into the quality of both the managers and the projects.

Expose new thinking, new processes and new products early so the board has an opportunity for input at a time when additional outside thinking can add value.

Have a formal letter of engagement so outside board members have a clear statement of performance expectations, understanding of risks, terms of service and a commitment to compensation.

Consider one social event per year for your board members and your key managers to interact and develop a sense of team. This will also give your board an opportunity to further evaluate your manager's skills, attributes and attitudes.

Finding and implementing value-adding processes for your board of advisors most likely will be distinctive to your company needs and your management style.

In my experience the most productive and value-adding boards work for owners who recognize the benefits that accrue from the time and effort needed to create an effective outside board of advisors.

If you are like many business owners considering a board of advisors for the first time you likely have to overcome some level of the "fear of the unknown." Once the comfort level is there and the decision is made to proceed with a board of advisors, take the time to think through the issues discussed in these articles. Choose the right combination of options for your management style and your company's needs.

As your board evolves and your company grows, adjust and adapt your board make up and processes to meet the changing needs of the company and the demands of the market. Keep your commitment to the board and establish ways to both maintain continuity and consistency and to extract sustainable value from your board of advisors.

Article # 8

<u>Board of advisors composition and compensation</u>

This series of seven previous articles has provided insight and experience concerning the elements necessary to develop and maintain a value-adding board of advisors for private companies.

In this eighth and last article of the series the issues of board composition and board compensation will be discussed.

In private companies effectively using a board of advisors the composition is generally made up of two elements. The first group is outside directors. The second group includes selective, senior, functional managers from inside the company.

The outside board members are chosen using the tips and tools discussed in this series of articles. They fill specific gaps in the experience or expertise of the company, and will represent an opportunity for new perspectives and new thinking.

The number of outside directors should be proportionate to the size of the company and will represent important gaps in the company's experience or expertise. A good guide line for companies making their first commitment to using a board of advisors is to identify two to four outside directors who fill the highest priority gaps in the company's experience or expertise.

Board candidates should be smart, independent, and diverse in experience. They should be eager to bring new perspective and insight to the company and willing to soundly support their views. Board candidates must have both personal and professional integrity. One final attribute of importance for your outside board members is, when appropriate, to be willing to provide constructively opposing points of view contrary to the owner and inside managers.

As cautioned in earlier articles, avoid outside board candidates whose only qualification is that of a friend. In addition, generally avoid candidates who are already outside paid professionals for the company such as outside counsel or an outside auditor. They are already being paid for their independent advice. They can be invited to board meetings as needed to present information or to give their opinions directly to the board.

The inside members of your board of advisors will be made up of selected senior managers who are also employees of the company. As the owner and president or CEO you will serve as the chairman of the board.

Next, select functional area managers of your company who are most important to the company's success. If the company is manufacturing driven, the senior manufacturing manager would represent a likely candidate for a board position. If your company is marketing driven, the senior marketing manager is an appropriate candidate. Often the senior financial officer is an important part of the makeup of the inside board members.

Candidates from inside the company should fill seats that represent important functional disciplines of the company and / or senior managers who are clear succession candidates for the company.

The total number of board seats should reflect company size, the defined opportunity of having a board, diversified experience and expertise and a number that is comfortable and manageable for the owner. Additional board seats can be added after gaining experience with this management tool. Remember, keep your options open and be flexible. Make revisions as the company and market circumstances change.

Board compensation for outside directors is best addressed by considering a few key factors. Benchmark other companies similar in size to yours. Look at companies inside and outside of your own industry. Relate the range of appropriate compensation to the value you put on having a board of advisors. Consider various methods of payment including cash, equity or some combination of the two payment methods. Remember, most outside board members in private companies are not serving on the board as their primary means of support. Compensation should be related to the time provided and the value delivered by the board members.

As the size of the company increases other financial issues need to be considered. As the owner do you expect your board members to shoulder any fiduciary or regulatory risk? If so, what protection can be provided for the board members? If not, will a written release be provided to the board members from the company?

Compensation for inside board members also needs consideration during the planning stage of forming a board of advisors. If the inside manager's job description and reward system already takes into account board participation then additional compensation is not appropriate. If this activity is added to the manager's duties and responsibilities, then consideration of additional compensation is appropriate. Payment to inside board members should be related to compensation of the outside directors.

Board composition and compensation should reflect the mission and job descriptions you as the owner have developed for your board of advisors. Following the suggestions in this series of articles can be of value in the choices you make and in the way you operate and gain value from your board of advisors.

Successful owners who have utilized outside boards effectively have found that the message sent to employees, customers and suppliers is powerful. It says you are an owner who recognizes and uses a competitive advantage, is open to new thinking, and is likely to be on the top of your game.

From my experience on numerous boards I have no doubt that an owner effectively deploying an independent board of advisors is more likely to reach his or her goals for growth, reward, succession and at some future time a smooth transition or exit.

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