



ASPEN FAMILY BUSINESS GROUP, LLC

DEEP RELATIONSHIPS. ENDURING LEGACIES.

## Family Business Board Governance

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### Difference Between Governance And Management

“Governance usually refers to the ways in which a company organizes itself to do business within a legal framework of the society in which it operates and its own bylaws. In the context of public corporations, the concept is largely defined by the fiduciary responsibility of the board of directors to represent the interests of shareholders in overseeing the strategic direction and policies of the company as well as the decisions and performance of management....**Governance structures in family companies must be designed to safeguard the long-term interests of family shareholders by ensuring the growth and continuity of the enterprise and promoting the family’s harmony and welfare.** This definition implies that both the business and the family are in need of governance.” (Lansberg p. 280-281)

But family members need to understand the boundary between owning and governing a business and the day to day management of the business: the authority which has been delegated by the board to the management of the company (President, CEO/COO, on down).

### Purpose of Board of Directors in a Family Business

“The objective, confidential and caring counsel of an effective board can help the owners sustain wise and competent leadership.” (Ward)

The fundamental responsibility of directors is “to represent the interests of the shareholders as a group, as the owners of the enterprise, in directing the business and affairs of the corporation within the law.” Directors are also required to adopt or change corporate bylaws; approve amendments to the articles of incorporation; approve mergers, acquisitions, and changes in capital structure; declare dividends; and elect corporate officers.



In family businesses, the board becomes the *legitimate* forum for owners (or their representatives) to discuss their interests in the family business and provide clear and singular direction to management.

Individual directors also have important legal obligations regarding the quality of their service, including attention to the duties of care, loyalty, and attention. Directors are assigned broad responsibility for protecting the assets of the corporation, reviewing corporate objectives and policies, monitoring corporate performance, and ensuring competent management.

Overseeing the operation of the business:

- Reviewing corporate objectives
- Monitoring the performance of the enterprise
- Approving major acquisitions and divestitures of businesses
- Approving the strategic plan and operating budgets
- Advising the CEO and his/her management team
- Approving debt/equity ratios
- Guiding succession planning
- Assuring that the values, ethics and priorities of the family owners guide the operations of the business

## Legal Responsibilities

### Duty of Care

“Directors must act with the care that a reasonably prudent person in a similar position would use under similar circumstances.”

Show up regularly at meetings; pay attention; act in good faith

In the best interest of the organization

You are responsible for decisions made by the board whether you are in attendance at the meeting or not.

### Duty of Loyalty

Sole purpose doctrine (to assure good return to shareholders)

Avoidance of conflict of interest

The best interest of the corporation and shareholders must take precedence over the personal interests of the director



### Duty of Obedience

In accordance with applicable statutes and the company charter

### Duty of Oversight

Presence of reasonable controls in place in the organization

That the board has full and necessary information to be fully informed

The responsibility to be pro-active in seeking information and asking questions (why/why not something is done).

### The Business Judgement Rule

This is the guiding principle and protection for all directors.

This presumes that board decisions are made by

- disinterested directors
- acting on an informed basis
- in good faith and
- in the honest belief that their actions serve the corporations best interests.

E.g. if a board decision proves unwise, directors are free from liability as long as they acted in good faith.

## Board Operations

### Regular Tasks of the Board:

- Evaluate Company system of controls and measures
- Review financial policy and performance
- Assist in the creation of a vision for the future
- Develop a process for selection of successors
- Review short, mid-term and long-range strategies
- Evaluate human resource policies and practices
- Review the performance of key executive(s)

### Meetings:

- Typically Quarterly
- With clear agenda
- Information sent 2 weeks in advance
- Facilitated by the Chairman or his/her designee
- According to Roberts Rules of order or a similar system
- Documented with minutes capturing direction, decisions, material reviewed.



### Committees:

- Audit
- Compensation
- Governance/Nominating

### Board Evaluation

- Be clear about the talents you need on the board
- Matrix to assess competencies present, needed
- Evaluate individual contributions and overall effectiveness of the board

### Hazards to Watch Out for

- Conflict of Interest
- Apathy/Complacency
- Rubber stamp
- Confidentiality

### Some Guidelines

- Don't have a board unless you are going to use it.
- The board should focus on strategy and evaluation of the business not on week to week operations and decisions.
- Prepare members with agenda, reports or other reading beforehand to use time for discussion, recommendations and decision-making.
- Allow for enough time/meeting for substantial discussion-*at least* 2-3 hours.
- Have outside directors who can add value through objectivity and expertise.
- Remember that board members can represent the board only as one member of the board. He or she can not make decision as an individual member or give direction to the company individually.

## Family Business Board Competencies

### Introduction

Family Businesses are different than other businesses because of the engagement of family members who might not otherwise be involved in a business. As such there are family dynamics that must be considered and education that must be provided to “stakeholders” who can have an impact on the business.

The Board of Directors of a family business should still be operated with the best governance practices found in other businesses. Representation of family owners may serve on the board and education of the family through presentations by the board to family members (e.g. in a family council). Often, we prepare future family board representatives through educational programs and board “internships” (e.g. observing board meetings and reviewing the meetings with a mentor who is an independent board member). Representing the family is a special responsibility and brings with it an important and delicate communication role. One must be clear what can be shared and what can’t (in both directions). Managing confidentiality is an important skill.

Independent board members who serve on Family Business boards need to be prepared to interface with a more complicated system than a non-family business board and contribute to the process in several ways. First, getting to know the family and understand dynamics of the family that may impact decision making. Second, being available to coach, communicate with and educate family members is often requested. Finally, being prepared to address “sacred cows” that have impacted the business in the past and may constrain the effectiveness of the business is part of serving as an independent who can see the impact most clearly.

In addition to those specialized skills and perspectives, it is useful to see what a recent survey of board members has found about the competencies needed by effective board members

**Price Waterhouse Study Suggested:** (2015 Annual Corporate Directors Survey)

### What director attributes are most important?

Consistent with results from last year, the most desirable director attributes continue to be **financial expertise** (91% describe it as very important), followed by **industry expertise** (70%), operational expertise (66%), and **risk management expertise** (62%). These areas are crucial to board service as they provide the foundations for overseeing the business.

The percentage of directors who think board diversity is an important attribute increased; 39% now consider gender diversity very important compared to only 37% in 2014. And 30% now consider racial diversity very important – up from 28% last year.

### What makes a good Board member?

#### Financial skills

particularly being able to read financial reports and understand the industry-specific returns, be able to assess the performance of the company based on the financial information provided and to be able to ask relevant and insightful questions based on analysis of the financials.

#### Strategic Thinking

To review strategy by constructive questioning and suggestion; to apply business acumen and awareness of the unintended consequences of certain actions; to use analytical skills under pressure; to plan as well as ‘do’; to know when to change or innovate; to identify the tipping point. Directorships help fine-tune how to apply strategic thinking to strategic process and strategic choices; to articulate and link back to the core purpose.

#### Systems Thinking

good directors see the interconnections and unintended consequences of potential actions. The questions they ask discover the why behind the why. Systemic analysis gives clarity to customer and market impact within the life-cycle stage of the organization; and the critical nexus between the ‘what’ of the marketplace with the ‘how’ of organizational culture. This is especially important in family businesses: to understand the business as part of a larger system.



### **Oversight and Risk Management**

To oversee compliance and regulatory matters and develop a broader view of the areas of major risk to a business. In particular, good directors have learned how to ask the right questions, in the right way: to be supportive and to hold key executive accountable.

### **Effective, Collaborative Decision Making**

Corporate decisions for most operating executives are focused on operational needs, resource allocation or to solve short-term problems. At board level decisions are broader, more strategic, collective and require foresight. Underpinning this is an ability to influence or facilitate consensus on complex matters, through listening, respect and insight. Board business relies on collaboration cross functionally as well as cross culturally and across purposes. Boards draw on people from different backgrounds, skills, approaches, expectations and thinking styles. Skills such as empathy and emotional intelligence are needed to build the levels of trust for collaborative decision-making and accountability.

### **Time Commitment**

Board members must have sufficient time and commitment to serve effectively, including being prepared for meetings, accessible for dialogue in between the meetings.

### **Character and Values**

That create a level of trust among the board members, with the leadership team and with the shareholders are essential.

### **Knowledge of Industry and the Business**

The board should include someone who has deep industry experience and connections that are relevant. Other members should work to gain that knowledge and to commit to learning about the business and industry in which they are governing.

### **Other subject matter expertise**

The board should contain expertise in areas that are important to the development of the business as ascertained in organizational assessment, such as marketing, finance, law, technology, human resources, etc.



### Board Matrix: Sample

Rank in each area from one to five with five high. One is minimal. Five is outstanding.

	Current Directors							Prospects					Total
	1	2	3	4	5	6		1	2	3	4	5	
Financial Literacy													
Operations Experience													
Mechanical Contracting Industry Exp													
Knowledge of Local Business Environment													
Board Experience													
Family Business Experience													
Construction background													
Strategic Thinking/Planning													
Marketing/Sales													
Mergers & Acquisitions													
Finance													
Partnerships/Affiliations													
Management knowledge/experience													
<b>Qualities:</b>													
Ethical													
Intellect													
Visionary/Strategic													
Entrepreneurial													
Appreciation of human capital													
Leadership													
Team Player													
Cultural Fit													

## Role of The Chair

*The Chair of the Board serves as the Board's Agent for the proper execution of corporate governance functions retained by the Board. As such the Chair organizes and manages the functioning of the Board itself, such that the Company's total activities are aligned with Company values, mission, and strategic objectives as well as laws applying to the activities of the Corporation. Further, the Chair provides specified liaison, relationship enhancement and development activities between the board and various stakeholders, (i.e. shareholders, employees, lenders, etc.), which are strategic and supporting the long-term health and growth of the Corporation. (Pendergast)*

## Outline of A Board Evaluation Process

Board Assessment Systems include:

- 1. Clarity of purpose of the board**
  - a. Review of pertinent documents
    1. Articles of Incorporation
    2. Shareholder Agreements
    3. Voting Agreements
    4. Irrevocable Proxies
    5. Voting Trusts
  - b. Statement in Board Charter code of conduct (see 2)
- 2. Clarity of role and boundaries**
  - a. Expectation of board members
  - b. Ethics, confidentiality
  - c. Governance vs. management
  - d. Access to employees
- 3. Effectiveness of structure:**
  - a. Committees
  - b. Leadership
  - c. Terms
  - d. Board manual etc.



#### 4. Effectiveness of process:

- a. Information flow
- b. Clarity and relevance of objectives
- c. Effectiveness of meeting management
- d. Participation of board members
  - i. Active participation in meetings
  - ii. Thorough preparation for meetings
  - iii. Contributing to Company outside of meetings as an ambassador and advisor
- e. Education, Orientation and Development of board members
- f. Board Evaluation (individual and collective)

#### 5. Board Composition

- a. Selection based on need of organization
- b. Rotation of membership
- c. Diversity of perspective
- d. Independence
- e. Represents Stakeholder groups

#### Assessment of board: A “Grade”

Does it meet legal requirements?	C (70%)
Does it meet minimum standards for operations?	C+ (75%)
Does it add value to the business	B (85%)
Does it work effectively and efficiently?	A (90+)