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Six Ways Outside Directors Benefit Business Growth

By John M. Collard

Benefits of Outside Directors

Action/Skill	Benefit
Independent Perspective	**Challenge Management, Sounding Board**
Strategic Thinking & Planning	**New Directions, Transitions, Incentive-Based Compensation**
Experience & Objectivity	**Been There, Done That, Oversee Performance & Risk**
Contacts	**Partners, Customers, Suppliers, Personnel, Lenders, Investors**
Capital Infusion	**Raise Money, Restructure, Create Offering Package**
Transactions	**Prepare Company For Sale, Negotiate The Deal**

An outside director is a member of the board of directors or advisors who is not part of the executive management team. These professionals are sometimes referred to as independent or non-executive directors. They are not employees of the company and are differentiated from inside directors, who do serve as executive managers and/or corporate officers.

Outside directors are advantageous because they rarely have conflict of interest and they often see the big picture differently than insiders. While corporate governance standards of public companies require a certain number or percentage of outside directors because they are more likely to provide unbiased opinions, private companies are normally left alone — but, I highly recommend that unbiased advice.

In today's business environment, smart organizations frequently seek outside expertise. Traditionally, companies invited advisors to join their board of directors. There is now, however, more risk to these directors based upon recent legislation (Sarbanes-Oxley). While there is formality (shareholder reporting, responsibility, risk, liability) and more expense (D&O insurance, etc.) to a board of directors, there is a budget friendly alternative in the form of a 'board of advisors' who is beholden to management. The main difference is in where the fiduciary duty lies: to shareholders or management. Regardless of which vehicle you use, there is great value to be obtained by hiring an outside director.

Why add outsiders to your board of directors or advisors?

1) Outside directors can be a low-risk, low-cost, but valuable resource. They bring a new set of skills produce benefit.

2) Outside directors are on your side. Unlike other outsiders to whom even a private company must answer, like banks, insurance companies, IRS, EPA, OSHA, these advisors answer to you.

3) Outside directors add credibility. When it comes time for a liquidity seeking event, like new financing, selling the company, or IPO, outside directors send the message that you are a professional serious organization with guidance.

With a board of directors, your company immediately gains legitimacy, and a panel with expertise that you probably don't have "in house." Selecting board members from the business community can also bring greater awareness of your company.

Create a culture and structure that will withstand third party accountability. Start thinking as a serious growing company and prepare for a potential future life as a public company.

Independent Perspective

The day-to-day events in a business often distract the CEO's time and energy. It is easy to get wrapped up in the ways and means of running the operation, while losing track of the bigger picture. The sounding board provided by an outside advisor can certainly help ground the CEO in real leadership duties. Typically, a board will focus on protecting the unique value of the company, but they often add much more.

The CEO needs advice from outside directors who care about the company's success, but who can view things from a distance and a different perspective. The CEO will be well served by adding board members who can challenge him or her and the decisions that they are about to make. When the CEO only listens to "yes" men they are essentially on their own, and new ideas don't enter the decision process. You want strong board members who are not afraid to offer advice, guidance, feedback, and argument on issues. Employee board members may be in fear of losing their job if they speak up.

Create the opportunity for people to disagree with you and confront your thinking. This is a must if you want to grow. Honest debate from knowledgeable people, who are on your side, will produce results that you can rely on. If you fear this approach, what are you hiding? Smart people learn from advisors who don't threaten their position, hence the need for outside independent thinkers.

Strategic Thinking & Planning

Outside directors should constructively challenge and contribute to strategy development, implementation, infrastructure. The board is the perfect way to help set aside tactical perspective, and force you to work on the strategic business issues.

Planning requires fresh thinking and business analysis, even if the result in some areas is to continue business as usual. The value is in the process, which requires all participants to think through and understand strategy. Put in place contingency plans for those events that we hope will never occur, but somehow always happen.

Once strategy is set you have defined where you want to go. Now communicate that message for all stakeholders to see and understand by using a mission or direction statement. There is nothing quite so effective as designing compensation and incentive plans that are paid out when goals are met, but don't pay for nonperformance. Incentive-based management is extremely effective, but be cautious that you have set the right goals, because if not, employees will take you in unplanned directions.

Experience & Objectivity

The very nature of growth implies that a company is going where it has not been before. It is refreshing to make that journey to new opportunities with the help of an advisor who has been there, and done that before. Their objectivity can help you through the obstacles.

When independent observers scrutinize performance of management in meeting goals and objectives, and monitoring results compared to long term valuation goals there is real value in their participation. Outside directors should satisfy themselves that financial information is accurate, financial controls are in place, internal reporting is at the right levels and prepared often, and that risk management systems are in place. Make sure that the company complies with laws and regulations.

While most companies follow a well understood life cycle, it is extremely helpful to distinguish between crises that are normal based upon their stage in that life cycle versus crises that are troublesome because they are unexpected. Look for business advice from experts who have experience in these situations.

When transitioning into new markets it helps to have someone on your team that has both gone through transitions before and understands the idiosyncrasies of the new market. For instance, doing business with the federal government is quite different than doing business in commercial and international markets. If you want to enter into new markets have team members with diverse experiences to help guide the way.

Contacts

Your contact book doesn't include everyone. Every company needs help when it wants to grow, prosper, or turn around. Outside directors can extend the company's reach by using their own contact network, colleagues that can get involved to provide guidance and resources.

Rely on these contact introductions to bring in new customers, which will drive revenue. New suppliers can favorably impact cost-cutting of materials, which drive a better bottom line. Strive for strategic teaming relationships to promote growth.

Contacts can be influential in bringing resources not previously available. They can attract new talent into the company at all levels, and provide a new set of eyes and ears during the interview process. Locate other independent directors. Improve the management team. Grow the sales force and distribution channels. Introduce and improve marketing, penetration, and Internet presence strategies. Entice operational experts to produce product and services. Lure innovative people who can embellish research and development.

Capital Infusion

Outside directors often have a database of contacts who can supply capital, in a form of debt (lenders) and/or equity (investors). This means that you can get in front of many financing resources quickly once an expression of interest or offering package is ready. The key is to document the plan describing where you want to go and why you will succeed, put that in summary and detail form, describe assumptions and risks, and present rate of return projections. In other words, present your opportunity in terms the investor or lender wants to see —you are the product. Investors are in this for returns on their investment. You will need financial history of operations and projections of future plans to satisfy the stringent criteria of financing sources. Begin this process early so that you are prepared when the time comes. I favor a 2 page (executive introduction), 10 page (present the deal opportunity), due diligence (details) approach, to step potential interested parties through the process.

If a turnaround is in process the task is more complex. While there is an overabundance of capital available, you will have to demonstrate that you have indeed made changes at the company. Changes in management, control systems, strategy, etcetera are a must. A board of directors demonstrates that you are up to the task of reporting to an outside financing entity.

Transactions

Like with raising capital, outside directors often have a database of contacts who both have deals for acquisition and who are looking for opportunities to buy. This means that you can get in front of M&A dealmaker resources quickly once an offering package is ready.

Prepare for that future liquidity event. The best time to sell a company is when a buyer wants to buy and has cash, which could come when you don't expect it. Be prepared and work toward ultimate valuation throughout the process of growth.

Outside directors are often adept at introductions and negotiating deals. They then elevate you (management and the board) to the decision-making role.

Hire that outside director.

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