



Lecture 11

Board
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- You've become a director of a venture capital backed company (VCBC), what level of board governance knowledge should you have?



Typically

- Privately held venture capital backed company VCBC boards have a very high percentage of inexperienced corporate directors.
- First-time entrepreneurs who become founding CEOs frequently become corporate directors even before they obtain their first institutional round of venture capital financing.

While taking venture capital (“VC”) is always a choice, there is no opting out of the legal responsibilities of corporate directors.



VC boards are unique

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- VCBC boards are unique because they face challenges that are particular to emerging companies in rapidly changing competitive markets.
- VCBC's develop through four distinct stages:
 - (1) seed funding and product/technology/service development;
 - (2) early commercialization;
 - (3) late stage expansion;
 - (4) liquidity through either an acquisition or an initial public offering ("IPO").
- As companies grow in size and invested capital, board sizes typically increase from 3 members to as many as 7.
 - The composition of the board also changes to include more independent directors, particularly if the company wishes to go public.

Through this evolution, business processes become more complex, and VCBC boards are naturally exposed to various situations that raise inherent conflicts of interest among board members.



Self-regulation

- While private companies are not subject to most aspects of Sarbanes Oxley (SOX) and other regulations that impose governance standards upon public companies, it is in the best interests of the venture capital industry to develop and proactively follow corporate governance best practices in the private company context.
- If we don't, it is likely that lawmakers, administrative agencies, or the courts will impose regulation on the venture capital industry from the outside without the benefit of deep knowledge of the nuances that make entrepreneurs and the eco-system that surrounds them unique.
- Moreover, the failure of the VC industry to respond to changing expectations and best practices regarding corporate governance could expose VCBC directors to personal liability.
- **Most important, the application of good governance practices will help us build better companies.**



How to Achieve an Aligned and Effective Board

- The legal fiduciary duties associated with board service are duties to all of the shareholders, not just to the shareholder class in which a VC director's firm has made an investment.
- At a minimum, the board must agree to common goals and basic tenets of behavior.
- Although all boards are made up of individuals with differing interests and responsibilities outside the boardroom, they must serve

common goals inside the boardroom.



Align expectations

- A key feature of effective boards is that they deliberately align expectations:
- The board is economically and strategically aligned among itself
- The board's expectations of the CEO and the CEO's expectations of the board are mutually well understood.



Four main areas

- **Exit Plans:** VCs should openly address their expectations regarding a liquidity event. Specific exit values (or ranges) should be discussed to ensure common expectations from the management team (which is most likely the final arbiter of any potential M&A activity).
 - For example, different investors even within the same round may have different exit valuations in mind; one investor may be happy selling the company for \$100M while another may need \$300M to even consider a deal.
- **Exit Timing:** The Board should openly discuss the timeframes for exit options. Some investors may want to wait longer than others for an exit.
 - This issue becomes even more important when investors join the board in different rounds, especially if one VC invests many years later than the earliest investors.
- **Investment Expectations:** VCs should candidly discuss the amount of money their funds have allocated for follow-on reserves to the company. Depending on the stage of investment, some investors may have reserved 1- 3X or more of their initial investment.
 - It is important for the entire board to understand the level of each investor's reserves and the conditions for follow-on investment.
- **Syndication Expectations:** The VC board should discuss its interest in syndication for follow-on rounds. Some VCs do deals based on a “fully funded syndicate” model which expects all the early investors to continue backing the company through liquidity. Others depend on syndication across rounds, expecting new investors to join them in subsequent rounds.
 - A transparent discussion is required for the VCBC to not pursue investment paths (like recruiting new investors) if the current investors are not interested in outside capital.

In order to ensure the board is aligned economically, there are four main areas surrounding investment strategy that should be considered.



Behavior of board

- One of the most important jobs of the board is to promote effective behavior in the boardroom so that management can focus on getting the operating job done and avoid distractions from boardroom intrigue and political maneuvering.
- This does not mean that the CEO should not be actively working with the board—on the contrary, it means that the substance of this activity should be geared toward building the business.
- Simply meeting legal governance requirements is an important, but not sufficient, part of an effective board.
- Directors need to be interested in getting the board to do the best job it can to promote the best interests of the company and maximize value for the shareholders.
- Peer review and self evaluations may lead to greater director accountability, better education, and the adoption of governance practices that are appropriate for private companies.



Governance process, and internal controls

- WHO OWNS THE GOVERNANCE EDUCATION PROCESS ON THE BOARD?
 - Someone on the board MUST take ownership of the process of educating directors about their service responsibilities and implementing the process of director evaluations.
 - Whether the “owner” of the implementation process is a VC, the CEO, or an independent director is secondary. At a minimum, the CEO initiate a board discussion to assign this responsibility.
 - Because VCBCs experience significant changes in board size and composition over their normal life cycles, not all of the processes are applicable to every VCBC, especially at the earlier stages of their development.



Audit Committee

- AUDIT COMMITTEE OVERSIGHT VARIES WITH DEVELOPMENT STAGE
 - Applying sound standards of corporate governance to an emerging company does not end in the boardroom.
 - The most critical board committee from a compliance standpoint is the audit committee, and the audit committee's duty of oversight falls squarely into the area of assessing the adequacy of the company's internal controls.
 - We overlay important questions about the internal controls that a company has in place and measure these against a company's stage of development—and therefore its operational complexity—in order to suggest appropriate levels of internal controls coincident with each company's governance processes and level of maturity.



Internal Controls

- INTERNAL CONTROLS AT THE SEED/R&D STAGE
 - Even a small company that is not selling products or services is likely to have activities in the following areas: purchasing and disbursements, payroll, treasury management, fixed assets, equity and stock administration, and financial reporting.
 - The risks associated with checks and balances around cash disbursements will in many cases depend on the volume of transactions and the type of transactions.
 - The board should establish thresholds for board approval, and approve management authorization levels.
 - The board is normally pretty close to financial metrics, such as spending levels, etc. which serve as effective monitoring controls.
 - An awareness of fraud risks (smaller companies typically have segregation of duties issues) and an understanding of the company's key financial processes, monitored appropriately, layered on top of the Board's review of financial metrics, should normally cover the typical risks.



Early Internal Controls

- INTERNAL CONTROLS DURING THE EARLY COMMERCIALIZATION STAGE
 - The transition from product development to generating revenues is one of the most difficult for emerging companies because priorities are reset and new personnel are brought on board in senior positions.
 - Typically these new senior team members have not lived through the "birthing" process of the development program, which can bring stress to the prior team.
 - As the operating business model is being established, this is the point where the company's applicable accounting policies begin to take shape (for example, how the product or service being sold is driving revenue recognition implications).
 - At this time, it is appropriate to assess what accounting expertise is required, and what is already in place. Accounting has become increasingly complex, and smaller organizations in particular are challenged in this area. Larger companies often have a "Chief Accounting Officer" or similar position.



Questions for Audit Committee

- What are the critical accounting policies (and what are the applicable pieces of technical literature)?
- What experience and expertise do we have in-house?
- Do we have enough depth in our finance team to have someone effectively review complex accounting judgments (or are we relying on the "preparer" to get it right)?
- If we don't have the technical expertise we need, can we train existing personnel to be responsible for certain areas of accounting complexity?
- As we look at building the finance team (typically, headcount increases as a company moves from early commercialization to expansion), what specific accounting expertise and skill sets should our next hire possess?
- What processes do we have in place to identify new accounting issues and determine if they apply to the company?
- How much ongoing training do finance personnel receive, and is it sufficient to maintain competence levels?
- Do we need to engage outside parties in specific areas to supplement our existing skill sets?

That is not practical for a smaller company with limited financial resources. The full board, or, at a minimum the audit committee, should have the questions at the left.



Late Stage Internal Control

- INTERNAL CONTROLS DURING LATE STAGE EXPANSION
 - As the growth rate of annual revenues begins to accelerate, it becomes appropriate for a company to adopt more formal risk assessment processes (relative to financial reporting risk). This risk assessment should enable discussion around questions such as:
 - What are the significant accounting processes
 - What are the areas of accounting complexity?
 - Where is my highest risk of material misstatement?



Other factors

Some factors to consider as management prepares and the board reviews process and account level risks are:

- Materiality to the financial statements;
- Level of accounting and reporting complexity;
- Account characteristics (transactional and routine, estimate and non-routine);
- Fraud risk inherent in account or process;
- Volume of activity;
- Volatility;
- Other reporting considerations inherent in account or process.

The risk assessment will guide more extensive monitoring activities, as appropriate. While designing appropriate monitoring activities, the audit committee and/or board should also consider items such as known weaknesses, especially any reported significant deficiencies or material weaknesses; and the maturity level of its financial reporting processes.



Liquidity

- ANTICIPATING A LIQUIDITY EVENT (IPO OR ACQUISITION)
 - Whether or not a company is expecting to go public, applying public company accounting and governance standards is important because of the likelihood that an acquisition by a public company will occur.
 - Organizations that lack proper internal controls may experience a lower acquisition valuation than those that have well defined risk controls and high governance standards.
 - Many companies start their SOX compliance effort as they approach an IPO, and this is often an early implementation of SOX compliance.
 - SOX compliance activities can be scaled depending on the risk assessments to date, the timing and probability of the liquidity event, and the type of exit (IPO or acquisition).
 - SOX compliance activities and milestones may vary depending upon factors such as:
 - Risk assessment process in place and level of risk tolerance;
 - Level of perceived process maturity;
 - Level of anticipated remediation, including known significant deficiencies and material weaknesses;
 - Level of existing control documentation;
 - Level of current control monitoring.
 - Board involvement/monitoring will likely flow from the agreed upon SOX compliance activities.

DEVELOPMENT STAGE MATRIX

Development Stage	Typical Total Number of Directors	Typical Mix	Governance Processes to be Considered	Internal Control Processes to be Considered	Typical Control Process Management Activities
Seed / Product / Technology / Service Development	3 - 4	Management 1 - 2 VC 1 - 2 Independent 0 - 1	<ul style="list-style-type: none"> Typically implemented by the board as a whole 	<ul style="list-style-type: none"> Understand and monitor relevant financial reporting and fraud risks Establish signing threshold levels for disbursements and legal agreements 	<ul style="list-style-type: none"> Establish financial reporting processes and controls, as needed
Early Commercialization	4 - 5	Management 1 - 2 VC 2 - 3 Independent 1 - 2	<ul style="list-style-type: none"> Either (a) formally designate specific board members with the responsibility to lead Audit and Compensation Committee functions for the entire board or (b) establish formal Audit and Compensation Committees Those directors responsible for (a) or (b) should take responsibility for implementing corporate governance policies 	<ul style="list-style-type: none"> Review critical accounting policies and assess competence of finance team If an audit is performed, Audit Committee or board as a whole should meet with auditors in executive session 	<ul style="list-style-type: none"> Assess finance infrastructure needs in light of planned growth Make adjustments to financial reporting processes and controls, as appropriate
Late Stage Expansion	5 - 7	Management 1 - 2 VC 2 - 3 Independent 2 - 3	<ul style="list-style-type: none"> Establish formal Audit, Compensation Nominating/ Governance Committees Consider naming formal board Chairman Consider implementing public company governance practices, as appropriate 	<ul style="list-style-type: none"> Consider more formal discussion and/or analysis of financial reporting risks Consider requesting and reviewing additional management reporting on internal controls, as appropriate 	<ul style="list-style-type: none"> Assess infrastructure and implement appropriate changes to support expansion Consider high level Section 404 planning
Liquidity (IPO or Acquisition)	7 +	Management 1 - 2 VC 2 - 3 Independent 2 - 3	<ul style="list-style-type: none"> Name formal board Chairman/ Lead Director (in IPO process) 	<ul style="list-style-type: none"> Consider implementing public company internal controls practices, as appropriate 	<ul style="list-style-type: none"> Commence Section 404 planning and scope appropriate compliance activities



Board Composition

■ BOARD COMPOSITION

- There is no firm rule for VCBC board sizes or their composition because boards, by their very nature as small groups, are heavily influenced by individual personalities, interpersonal relationships, and individual skill sets.
- Recognizing that the average time from creation of a new VCBC to exit, six years at the time of the writing of this paper, is the longest it has been in over a decade, VCBC boards should pay particular attention to board composition in order to avoid duplicative skills among board members.
- While it is outside the scope of this paper to address this issue in greater detail, VCBCs should strive to constitute a board where the members have different strengths from each other (technical, operational, financial, managerial).

In addition, skills of VCs should complement those of the independent directors (who may have different but relevant sector domain expertise, such as accounting credentials required for Audit Committee chairs, etc.)



Role of Board Observers

■ ROLE OF BOARD OBSERVERS

- Some investors, particularly strategic investors in later stage rounds, will negotiate for the right to have a representative, referred to as a board observer, attend board and committee meetings and receive materials distributed to directors.
- An observer does not have the legal status of a director. Importantly, the observer does not have the right to vote on board matters and is not subject to the fiduciary duties of a director.
- Accordingly, the role of the observer should be set forth in a contract between the company and the investor.
- For example, the company will often require that the observe
 - (i) treat all information he/she receives confidentially; and
 - (ii) may be excluded from board meetings (and receipt of board materials) if the observer has a conflict of interest or the observer's participation would adversely affect the company's attorney-client privilege.



Role of Company Counsel

- Directors frequently ask who company counsel represents – investors, founders, the board, management or employees?
 - Company counsel represents the company and plays an important role in advising the board as to its legal responsibilities. For example, company counsel often assists the board in:
 - Discharging its fiduciary duties (e.g., in equity financing and liquidity events)
 - Complying with applicable legal and regulatory requirements (e.g., option granting practices and procedures)
 - Structuring and implementing corporate governance policies and procedures (e.g., audit and compensation committee charters and responsibilities and codes of business conduct)
 - Advising the board about management matters (e.g., CEO compensation and management changes)
 - Documenting board and committee actions (e.g., preparing and approving board minutes).



Legal and business basics 101 before joining

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- 1. Defining the Board's Essential Role**
- 2. General Duties and Responsibilities of Private Company Directors**
- 3. Summary of the Legal Requirements of Board Service**
- 4. Common Characteristics of**
 - **Effective Private Company Boards/Directors**
 - **Ineffective Private Company Boards/Directors**
- 5. Minimum Service Expectations for VCBC Directors**
 - 1. All Directors**
 - 2. Management Directors**
 - 3. Independent Directors**
 - 4. VC Directors**

In advance of the first meeting of the board, and whenever a new director joins the board, the material on the following pages, should be distributed to ALL of the board members and briefly be reviewed at the beginning of the board meeting.

This should be easily accomplished in 15 minutes.

An in-person initial meeting with new directors to review the director's key responsibilities and the board's process and culture is also recommended.



Defining The Board's Essential Role

- Maximize shareholder value for all of the company's shareholders
- Attract, recruit, and retain talented management team and board members
- Mentor, task, and measure the executive team
- Provide a level of insight, business perspective, and expertise that is otherwise unavailable to the company's management team
- Oversee and promote fiscal, legal, and ethical governance standards



General Duties And Responsibilities

- Serving as fiduciaries for all shareholders
- Hiring, evaluating, and firing the CEO and approving officer selection
- Overseeing company performance / Establishing oversight mechanisms
- Reviewing and confirming basic company objectives and business strategy
- Identifying barriers to company progress and proactively dealing with the barriers
- Inquiring into performance deficiencies and establishing metrics for measurement and remediation
- Seeking continuity and strengthening the board
- Approving equity incentives and establishing executive compensation
- Overseeing regulatory and legal compliance



Summary Of The Legal Requirements Of Board

- Duty of Care
 - *Requires a director to act with the care that an ordinarily prudent person in a like position would exercise under similar circumstances.*
 - Requires directors to:
 - obtain information they believe is reasonably necessary to make a decision
 - make due inquiry
 - make informed decisions in good faith



Summary Of The Legal Requirements Of Board

- Duty of Loyalty
 - *Requires a director to act in the best interests of the corporation and not in the interest of the director or a related party.*
- Issues often arise where the director has a conflict of interest:
 - where the director or a related party has a personal financial interest in a transaction with the company (*e.g. the inherent conflict between VCs as directors and as representatives of their funds' interests*)
 - where the director usurps a “corporate opportunity” that properly belongs to the company
 - where the director serves as a representative of a third-party corporation and the third-party corporation’s objectives are in conflict with the best interests of the company
 - where the director abdicates his or her oversight role; does not act in good faith.

Examples of not acting in good faith:
– consciously or recklessly not devoting sufficient time to required duties – disregarding known risks – failing to exercise oversight on a sustained basis

Generally, state corporate laws have procedures for handling interested transactions and corporate opportunities, such as by requiring full disclosure and disinterested director approval.

Failure to act in good faith can have serious adverse consequences to a director, such as being exposed to personal liability for breaches of the duty of care or losing coverage under indemnification provisions or insurance policies.



Summary Of The Legal Requirements Of Board

- Confidentiality and Disclosure
 - *Duty of Confidentiality*. A subset of the duty of loyalty. Requires a director to maintain the confidentiality of non-public information about the company.
 - *Duty of Disclosure*. Requires a director, pursuant to the duties of care and loyalty, to take reasonable steps to ensure that a company provides its stockholders with all material information relating to a matter for which stockholder action is sought.



Business Judgment Rule

- *Creates a presumption that in making a business decision, the directors of a company acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.*
- The business judgment rule helps protect a director from personal liability for allegedly bad business decisions by essentially shifting the burden of proof to a plaintiff alleging that the director did not satisfy its fiduciary duties.
- This presumption and the protections afforded by the business judgment rule are lost if the directors involved in the decision are not disinterested, do not make appropriate inquiry prior to making their decisions, or fail to establish adequate oversight mechanisms.



Common Characteristics

- Establish a clear and mutual understanding of expectations between the directors and the CEO
- Conduct a formal annual performance evaluation of the CEO
- Have routine executive sessions among non-management board members only
- Have directors who work as a team and who make important contributions outside the board room.



In the boardroom

- Encourage open/honest communications
- Resolve differences of opinion constructively and quickly
- Have directors who are accountable to each other
- Promote continuing director education about current best practices
- Know and understand their responsibilities as directors are informed when they arrive at the board meeting, know the industry, and know the company's context in it
- Do not attack the CEO or other board members when he/she answers their questions –Participate in free and easy communication outside of the boardroom
- If appropriate, provide a different perspective as an individual member of the group

While it is the responsibility of a board to challenge the CEO and the team, care must be taken to do so respectfully and without creating personal animus. – The CEO's credibility should not be undermined in front of his/her team, even during a transitional period,



Ineffective Boards/Directors

- Fail to communicate— both in and out of the boardroom
- Suffer from denial— fail to act and make decisions
- Fail to reconcile diverging viewpoints
- Avoid addressing existing conflicts
- Regularly hold excessively long board meetings (over three hours without a strategic planning or other extraordinary agenda)
- Allow the use of PDA's and computers during a board meeting for purposes not related to board business
- Feel compelled to say something and to be heard, disregarding whether they are relevant or effective in their comments



Ineffective Boards/Directors

- Become disengaged because they no longer feel that their opinion matters—this could be over a strategic disagreement
- Fail to resolve disagreements quickly and constructively
- Do not maintain regular board meeting attendance
- Deliver inconsistent messages between the actual meeting and their post-meeting behavior— passive-aggressive behavior
- Succumb to lead investors who discourage constructive discussion from the rest of the board
- *Smaller firms in particular are afraid to break ranks with a dominant investor for fear of not getting into future deals.*
- *They should speak up and express their views independently.*



At minimum all directors

- All Directors Are Required to:
 - Attend all board meetings (outside of unexpected emergencies)
 - Prepare in advance for board meetings/conferences
 - Maintain open communications with the Board not only at board meetings but whenever pertinent information needs to be disseminated
 - Communicate openly and honestly between each other
 - Openly discuss points of difference rather than passively resist
 - Make themselves available for informal consultation with management and the board outside of the normal board schedule



At minimum for management directors

- Maintain open communications with the Board not only at board meetings but whenever pertinent information needs to be disseminated
- Provide adequate, timely information to enable the board to fulfill its duties
- Prepare board material to enable in depth discussions on requested topics
- Respond positively to board input
- Deliver both good and bad news promptly and in a direct and balanced manner
- Engage with non-management directors in between board meetings
- *Proactively draw on directors' know-how, contacts and ability to help in order to promote the company's business*
- *Avoid surprises at the board meeting*



At minimum independent directors

- Work as a team with fellow board members
- Serve as a sounding board for, and in some cases mentor, the CEO
- Provide independent perspective and constructive inputs
- Chair or participate on board committees that require independent directors
- Mediate between management and investor directors when conflicts of interest arise in financial negotiations and other matters and serve as disinterested directors in acting upon such matters



At minimum VC directors

- Understand the company's competitive position and maintain awareness of developments in the relevant industry sector
- Help companies close new business and build sales success outside the board meeting
- Serve as a sounding board for the CEO and, in some cases, mentor the CEO
- Proactively share relevant company knowledge from their portfolio experience with their fellow board members
- Make themselves available for informal consultation with management and the board outside of the normal board schedule
- Take a lead role in financing the company
- Contribute their knowledge and experience during liquidity events
- Understand and differentiate between their responsibilities as directors, and their role within their particular fund
- Invite and respect input from non-VC directors, even when those non-VC directors have relatively small ownership stakes by comparison to their own



You are a board member

- How to evaluate your own participation on the board
- *List of questions that each director should ask himself or herself once per year with respect to the proper fulfillment of board service obligations.*
- The self-evaluation should be a formal agenda item, once per year. In addition, each director should ask him/herself one overall question:
- Did I meet the minimum expectations for myself as a director of this company?



Sample Self-Evaluation

- Attended every board meeting?
- Consistently read the material in advance of the meeting?
- Consulted with the CEO as needed prior to the meeting to make sure you know what will be emphasized on the agenda, what help is needed from you specifically, and from the board as a whole?
- Worked with the company outside of the board on any projects and gotten to know the management team and other key contributors?
- Communicated with fellow directors as needed regarding alignment of interests?
- Contributed positively and at least tried to make a difference for this company?
- Established and maintained an effective oversight role?
- Stayed focused during the board meeting and limited use of PDA or laptops to designated breaks?
- Explicitly identified (and discussed with co-directors) any potential conflicts of interest that have arisen?



Annual CEO performance review

- Boards should conduct a formal annual performance evaluation of the CEO.
 - This deserves particular focus because anecdotal evidence in the venture capital industry suggests that the CEO is the least reviewed employee of the typical venture backed company.
- A board is highly unlikely to support the notion that the CEO should adjust employee salaries or issue new options grants without first reviewing individual employee performance.
- Why should the board be held to a lower standard when it comes to reviewing the CEO's performance?
- The importance of having in place a process for board review of the CEO cannot be overstated. Having this process in place facilitates an effective mechanism to promote the proper management of expectations between the board and the CEO.
- An annual CEO review process does not need to be cumbersome, and it need not be associated with compensation adjustments for the CEO.
- It should be viewed as an opportunity to make sure that the CEO and the board are on the same page with respect to the CEO's current business plan objectives and priorities.
- It can be particularly useful to combine the CEO review by the board with a 360 degree review of the CEO by all of his direct reports.



Recommendations

- Create a common, short, written questionnaire to be used by the directors and by the direct reports.
- Separate the reviewers:
- Designate a non-management director to circulate the questionnaire to each of the non-management directors
- Designate either an outside consultant or the head of human resources to perform the same aggregation function for the CEO's direct reports
- The board reviewer should consolidate the director questionnaires into a single document that is shared among the directors. This document should represent a consensus view by the directors.
- The designated director should coordinate with the consultant or HR person conducting the 360 review and receive a written synopsis from the team reviewer which summarizes the comments from the direct reports.
- Comments from the direct reports and the directors will remain anonymous, but they are NOT confidential. (For example, the report could say, one employee felt that the CEO did not do X sufficiently, but the majority disagreed with this observation.)
- The designated director will compare the two reports and generate a final report for the board that will be given to the CEO which reflects both the consensus of the team and of the board.
- A subset of directors, typically the designated director and one other, should meet with the CEO and deliver the report orally, discuss the conclusions with the CEO, and present a written copy of the report to the CEO, signed by the entire board, at the end of the oral discussion.



Annual board peer review

- While venture capitalists on private company boards normally acquire their board seats through contractual and/or charter provisions, this does not absolve them of the responsibility of being effective directors.
- Peer review can bring to the foreground issues that are difficult for directors to surface directly in a face-to-face conversation—issues such as contribution, communication, accessibility, engagement, professionalism, and courtesy can greatly improve the functioning of the entire board.
- The later the stage of the company's development, the greater the need for good self-evaluation and peer review.



Logistics For Implementation

- The following questionnaire is designed to be completed confidentially and individually by each of the directors. It should be transmitted confidentially by each director to a third party, either the company's outside counsel or an outside facilitator, for aggregation of comments and review.
- Conducting an annual board self evaluation establishes a process for the communication of disagreements or misalignments that directors may be reluctant to address openly. If you consider it a safety valve and a consensus building tool, this review process should only be a positive force on the board.



Reference

- Adapted from A Simple Guide to THE BASIC RESPONSIBILITIES OF VC-BACKED COMPANY DIRECTORS by the WORKING GROUP ON DIRECTOR ACCOUNTABILITY AND BOARD EFFECTIVENESS. Originally released January 2007 and expanded October 2007.

_____, INC

BOARD OF DIRECTORS
Privileged and Confidential

The following assessment tool is designed to solicit your thoughts regarding the performance of the Board of Directors as a group. It is intended to enhance the Board's overall effectiveness. Please complete the questionnaire and return it in the enclosed envelope to [_____]. Your responses are requested by [_____].

Please evaluate the extent to which each of the following statements is true with respect to this company's board using the following rating system and add your comments as appropriate in the far right column.

1 – Completely False 2 – Generally False 3 – Generally True 4 – Unqualifiedly True NA= Not Applicable

Principal Components	Ratings <i>(See point system above)</i>	Comments/Action Plan to Improve Effectiveness
SECTION I: Structure and Composition of Board		
1. Board Size. The current size of the Board (____ members) is appropriate.	1 2 3 4	
2. Board Committees. The Board has an appropriate number of formal committees given the company's current stage of development.	1 2 3 4	
3. Board Composition. The Board has the appropriate balance and breadth of backgrounds, business experience, skills and expertise in areas vital to the Company's success given its present markets served and stage of development.	1 2 3 4	
4. Director Performance. Independent directors are adequately contributing to the Board.	1 2 3 4	
5. Director Performance. VC directors are adequately contributing to the Board.	1 2 3 4	

Principal Components	Ratings (See <i>point system</i>)	Comments/Action Plan to Improve Effectiveness
<p>6. Director Performance. Management directors are adequately contributing to the Board.</p> <p>7. Familiarity with Company. The Board is appropriately familiar with the Company, the markets it serves (including competitive factors) and its strategies and business plans and reflects this understanding on key issues throughout the year.</p>	<p>1 2 3 4</p> <p>1 2 3 4</p>	
<p>SECTION 2. Board Culture and Communication</p>		
<p>8. CEO–Board Communication. The Board members individually communicate informally with the CEO on a regular basis in advance of board meetings in order to have advance knowledge of issues that will be discussed at the meeting.</p> <p>9. Director–Director Communication. The Board members communicate with each other informally and are well informed about each other’s positions on issues affecting the company.</p> <p>10. Overall Effectiveness. The Board grasps and deliberates on the important issues and brings decision topics to closure in a timely manner.</p> <p>11. Board Initiative. The Board asks the penetrating questions necessary to uncover serious problems.</p> <p>12. Board Support of Management. The Board is appropriately balanced in challenging and supporting management.</p>	<p>1 2 3 4</p> <p>1 2 3 4</p> <p>1 2 3 4</p> <p>1 2 3 4</p> <p>1 2 3 4</p>	

Principal Components	Ratings (See <i>point system</i>)	Comments/Action Plan to Improve Effectiveness
<p>13. Board Candor. The Board encourages a culture that promotes candid communication.</p>	<p>1 2 3 4</p>	
<p>14. Board Collegiality. The Board and management work together to achieve a constructive decision making atmosphere that encourages a respectful examination of different views.</p>	<p>1 2 3 4</p>	
<p>15. Board Relationships. There is a relationship of mutual trust and respect among Board members.</p>	<p>1 2 3 4</p>	
<p>SECTION 3. Board Information</p>		
<p>16. Accuracy of Information. The information provided to the Board by management and outside advisors is accurate and reliable.</p>	<p>1 2 3 4</p>	
<p>17. Relevance of Presentations. Presentations to the Board are appropriately focused on the key issues for Board consideration.</p>	<p>1 2 3 4</p>	
<p>18. Digestibility of Presentations. Presentations to the Board are appropriately “to the point” and do not contain an inappropriate amount of unnecessary data and/or analysis.</p>	<p>1 2 3 4</p>	
<p>19. Timeliness of Information. The information provided between Board meetings is timely, enabling members to fully prepare.</p>	<p>1 2 3 4</p>	
<p>20. Access to Management. The Board has appropriate access to the Company’s senior management.</p>	<p>1 2 3 4</p>	
<p>21. Director Requests. Director requests for information from management are reasonable in amount and time frame and are responded to appropriately.</p>	<p>1 2 3 4</p>	

Principal Components	Ratings (See point system)	Comments/Action Plan to Improve Effectiveness
SECTION 4. Board Process		
22. Board Meeting Agendas. The Board has appropriate input into the preparation of the agendas and there is proper priority of agendas.	2 3 4	
23. Time Allocated for Board Meetings. Ample time is allocated for Board meetings to assure full discussion of important matters.	2 3 4	
24. Number of Meetings. The Board has an appropriate number of meetings per year and schedules its meetings at appropriate times.	2 3 4	
25. Conduct of Board Meetings. Board meetings are conducted in a manner that ensures effective utilization and prioritization of the time available.	2 3 4	
26. Executive Sessions. There is sufficient time and opportunity for outside directors to meet independently during the time allotted for the formal board meeting.	2 3 4	

Please evaluate and answer one final question with respect to this process.

BOARD REVIEW PROCESS

27. Are we doing a good job at assessing and improving the performance of the Board through this self-evaluation process?

_____ Yes _____ No

If no, please describe the reason for your response. How would you recommend we improve the process?