



## ***Scion Knowledgebase FAQ*** **On governance and the private, closely-held company**

***What is governance?*** “Governance” is about communications and decision making. This becomes exponentially more difficult as your business increases in complexity. A well structured governance strategy will improve business performance and reduce tension among family members, owners and business participants through better communications.

This strategy will typically include a combination of formal meetings among family members and business leaders: (1) Family council which helps families keep family issues in the family circle (matters of financial, social and emotional importance to family); and (2) Board of Directors, which advises with legal authority and fiduciary responsibility on the business, *or* (3) Board of advisors, which advises but does not have legal power.

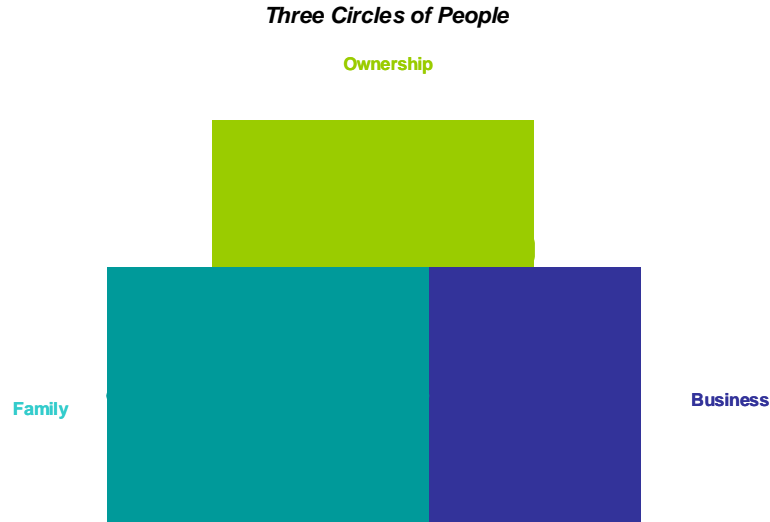
The objective of this more formal meeting structure is to catalyze more open, meaningful direct discussions; to share and discuss underlying feelings about changes in the business and ownership; to develop family policies that support consistent and balanced decision making; to educate and update on key family, ownership and business events and issues; and of course, to drive more effective decisions affecting business performance.

***Why develop governance?*** Family businesses with governing boards consistently outperform those without boards. From our work, we know why some owners avoid hiring outsiders to their boards: *fear of losing control.*

**Stronger                      Accountability                      =                      Superior                      Results**

In fact, the opposite happens: **good governance helps you maintain control of a healthier business.** With the objectivity, balance and professionalism of good governance practices, your business gains superior agility and endurance.

# Why Governance in private companies?



Governance assists you, as the CEO of the business, in focusing the overall direction of your business and enables senior management and owners to become more confident in your leadership of the private business enterprise.

Governance impacts three circles of people (see chart: *Three Circles of People*): (1) builds a united *ownership group* that can maintain its commitment to the business; (2) a *competitive business* consistent with the owning family values; and (3) a *highly functioning family* that can contribute to the business.

**“By creating a board that incorporates the outside perspective, we’ve enabled four business owners to drive solid decisions for the good of the company, accelerating growth in profitability and brand equity.”**

Hank Salvo, Chair  
**Patz & Hall Winery**

Good governance presents several key benefits.

- Encourage accountability in management and provide insight on key executives
- Offer opinions on compensation, performance, strategy, and other business matters
- Assist in strategic planning and monitoring of implementation
- Aid in creative thinking and decision-making
- Provide confidential and empathetic counsel
- Access to valuable corporate relationships and networks
- Establish priorities and policies
- Represent, protect and report to shareholders
- Act in crisis to ensure company survival; Act as an arbitrator
- Act as a sounding board to assist the business owner(s)
- Lend credibility and enhance company image, promote the company



## Why Governance in private companies?

***What types of governance exist (successfully in the wine industry)?*** The wine industry does not yet have well developed governance practices, because so many businesses in the wine industry are still run by the founders (82%\*) who have not experienced the transition to the next generation of owners. Examples of boards that are functioning well are as follows:

- Formal Board of Directors, with outside directors and legal responsibility for governance. Industry examples include: Cakebread Cellars, Delicato, Patz & Hall Wine Company, Clos Du Val
- Formal Board of Directors with family members only: many examples, Seghesio, Rodney Strong
- Board of Advisors including family members and outside advisors (CPA, Bank, and attorney): many examples
- Family Council with family members only: Cakebread family, Indelicato family, Seghesio family, Ledbetter family, Chappellet family

### **SVB/Scion Report on the Wine Industry\***

- Only 18% have some form of a board of directors or advisors.
- Less than 5% have outside board members participating actively in the governance process.
- Only 16% have family policies in place

***How to build successful governance?*** Two tips: (1) Since your board will have such potential impact on your business long term, you should seek help from outside experts who are experienced in developing a specific governance strategy for the particular phase of your business and ownership group. This will shorten your learning curve and accelerate your path to success. (2) Don't be cheap with your director's fees. Consider that if you choose real 'A' players to join your board, you will get far more in return than the fee they are being paid. *Attractive compensation, interesting challenges, and your willingness to take their advice seriously are factors that will attract A players.*



\* Ownership Transitions in the Wine Industry, February 2008. Rob McMillan, SVB Silicon Valley Bank Wine Division and Deborah Steinthal, Scion Advisors



## Why Governance in private companies?

Directors will also require reasonable protection from company liabilities; will need key information and a supportive process. A recent McKinsey study<sup>†</sup> reflects most Directors will want to know **more** about your market and organizational health than any other measure of company performance (financial, network or operational).

### Considerations in forming a Board

- Directors and Officers Insurance
- Corporate and Shareholder Indemnifications
- Product and Environmental Liability Insurance
- Use of Advisory Panel or Council to eliminate liability concerns
- Create an effective Buy-Sell Agreement

### Typical information Board Members will need

- Articles of incorporation and bylaws of company
- Financial statements, tax returns, estate plans, wills
- Corporate books
- Strategic business plan
- All reports to shareholders
- All corporate policies governing financial operations
- Operating and capital budgets
- Organizational charts
- Any matters involving litigation
- Performance reviews, compensation information, employee bios, employment contracts
- Sales analysis
- Details of banking arrangements
- Details of incentive plans, benefits, bonus plans
- Analysis of competitors, vendors, customers
- Current problems, prospects, issues in business
- Board meeting agenda and future meeting dates / issues to be reviewed at first meeting

***What are typical board functions?*** Your Board provides access to independent advice and specific expert insights and becomes a means for you to optimize opportunity and manage risk more successfully. Typical Board functions include:

### Ensuring Effective Governance

- Director searches and evaluations
- Assess corporate mission and organizational culture
- Encourage effective governance practices

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<sup>†</sup> The view from the Boardroom by Robert F. Felton and Pamela Keenan Fritz. The McKinsey Quarterly, 2005 Special Edition



## Why Governance in private companies?

### **Monitoring and Improving Business Policy and Strategy**

- Review auditors report and monitor business performance
- Review business goals, budgeting, capital structure
- Assist in determining value of firm, return on capital targets
- Review major capital expenditures, mergers & acquisitions
- Monitor business ethics
- Evaluate and approve strategic plan
- Establish compensation/incentives and human resource policies
- Monitor risk management
- Approve distributions to shareholders
- Ensure accountability to all stakeholders
- Contingency planning

### **Providing Advice and Counsel to Management**

- Sounding board to business leader, encourage strategic thinking
- Evaluation of key executives and outside advisors
- Set learning goals for the business
- Encourage creative thinking and problem solving
- Ask challenging questions

### **Overseeing Succession Planning**

- Assist in planning and implementation of management succession
- Develop successors
- Director succession

### **Supporting Family Shareholders**

- Monitor liquidity plans
- Assist in family education /ensure adequate information flow
- Encourage consensus reaching among family members
- Strengthen the business culture
- Foster positive image in the community

### ***What are some resources?***

- *The Imperfect Board Member: Discovering the Seven Disciplines of Governance Excellence*, by John Wiley and Sons Ltd; Dec 2006.
- Scion Advisors. Call Deborah Steinthal, 707.258.9130 or Ellen Hunt, 707.266.4065.

