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Private Company Board Governance

2007 NATIONAL DIRECTORS INSTITUTE

PRIVATE COMPANY BOARD GOVERNANCE

Private companies increasingly are under pressure to adopt or enhance corporate governance practices; however, the task of identifying and implementing corporate governance best practices is particularly challenging for private company boards because of the variety of private companies that exists.

Ed Mason, a partner and co-chair of Foley's Chicago office Business Law Department, led a panel discussion entitled "Private Company Board Governance," a breakout session of Foley's sixth annual National Directors Institute held on March 8, 2007 in Chicago. Other panelists included Stephen A. Cruise, managing director, investment banking at UBS Securities LLC; Glen Hackmann, managing director and general counsel at Robert W. Baird & Co., Inc.; Jeffrey Klein, managing director at Equity Group Investments, LLC; William Kunkler, executive vice president of CC Industries, Inc.; and William Mynatt, chairman, president, and chief executive officer of Dovenmuehle Mortgage, Inc.

Consistent with a "one size does not fit all" approach to corporate governance, the session offered insights on various approaches to corporate governance as implemented by a variety of private companies.

Forces Driving Private Companies to Adopt or Enhance Corporate Governance Practices

Overall, the bar has been raised with respect to private company governance, even though the corporate governance requirements imposed by the Sarbanes-Oxley Act (SOX) apply only to public companies. To that end, the following forces are driving or prompting certain private companies to adopt or enhance corporate governance practices:

- Sale of the private company — Better corporate governance practices lead to more transparency and a faster sales process, which equate to a better sales price
- Need to access capital markets — Sources of capital and their advisors carry high expectations regarding reliable and comprehensive information about companies and their businesses
- Sophisticated shareholders — They may have high expectations of corporate governance practices
- Regulatory environment — Depending upon the industry in which a private company operates, regulators may require audited financial statements and transparency regarding information relating to the business
- Imposition of more stringent standards by accounting firms — Accounting firms have imposed more stringent requirements on private companies, including certain SOX requirements

Specific Governance Practices

Examples of specific corporate governance practices adopted by private companies include:

- For private companies wishing to go public or to sell to a public company, three years of audited financials and independent directors are absolute requirements, and an audit committee expert also is essential

- The inclusion of a document retention policy, a whistleblower policy, directors and officers (D&O) insurance, a related-party transactions policy, auditor and director independence, establishment of board committees, a code of ethics, and disclosure controls in best practices policies

- For private companies looking to tap private markets for liquidity, the board is charged with coaching management to create and implement certain governance processes and procedures in order to safeguard the company from a due diligence perspective

- If a portfolio private company is part of private equity fund, the company needs to determine where they are headed (i.e., public or other family generations) and assess the skills of the management team to help lead the company down the chosen path

Best Independent Director Candidates

In the search for independent directors, integrity is paramount. The best candidate is not a "revolving door director," but one who understands the company's business. An ex-CEO director will bring different experiences and skills to the board than an ex-CFO director or a director with a different business background, so private companies should target what they want and need from an independent director.

Value of Independent Directors

Independent directors generally do provide value to private companies, but the company carries the responsibility of educating their directors. Independent directors can help manage a family deadlock by taking the issue out of a family perspective and putting it in a larger corporate perspective. Additionally, independent directors can bring outside accountability and expertise to the company, and they typically have a network of valuable outside contacts.

Advisory Boards

Many private companies assemble advisory boards to help them gain an independent perspective. Advisory boards can bring special expertise and credibility that would not otherwise be available to most private companies, and its members generally are easier to recruit because the position does not involve the same liability and extensive time commitment required of traditional directorships.

For More Information

For more information on this session or the sixth annual National Directors Institute, visit Foley.com/ndi2007 or contact the panelists directly.

Ed Mason
Foley & Lardner LLP
emason@foley.com

Steve Cruise
UBS Securities LLC
stephen.cruise@ubs.com

Glen Hackmann
Robert W. Baird & Co., Inc.
ghackmann@rwbaird.com

Jeffrey Klein
Equity Group Investments, LLC
jklein@egii.com

William Kunkler
CC Industries, Inc.
bkunkler@crown-chicago.com

William Mynatt
Dovenmuehle Mortgage, Inc.
william.mynatt@dmicorp.com

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Save the date! The 7th Annual National Directors Institute will be held on March 6, 2008 in Chicago. Learn more at Foley.com/ndi.