

# DOES MY BUSINESS NEED AN ADVISORY BOARD?

BY MIKE FERRARO

There are currently 12 million small-to-medium companies in the U.S., and 70% of them are expecting ownership changes in the next 5-10 years. Given the existing demographic trends, there will be many more sellers than buyers. Therefore, at a minimum, valuations may suffer. More likely, however, only the best companies will sell at any price. The rest will simply cease to exist, bringing NO value to their owners.



## *How would you rate your business? How would an outsider rate it? Do you consider yourself among the very best? Or, are you more like all the rest?*

Owning a closely held business is a challenging task in today's business environment. Having spent 40 years advising closely held business owners, and the last 20 of those years with many retail lumber dealers and their suppliers, I have seen owners struggle getting access to independent and confidential financial and business advisors. Public companies have boards of directors and audit committees. Their financial information is shared openly and on a relatively comparative basis.

Closely held businesses often compete locally, have unique circumstances that make financial information comparisons difficult to baseline, and do not share their financial results in an open fashion. When I am able to get under the hood and analyze a closely held business's financial operating results, there are always unique items that require further review in order to get to the "true" operating results.

The best companies all have similar qualities and characteristics. What are they? How do you know if you measure up to the best companies?

Consider that all the best companies have the following attributes and business practices in common. No company is too small to have them; they are not reserved for just large companies. How many of these attributes do you have? How would you rate yourself in each area? Ask yourself, how would an independent observer rate you? The same, or different? How would a potential acquirer rate you?

- 1 Vision and mission statements that clarify the company's long-term objectives
- 2 A business plan designed to fulfill the vision and mission
- 3 Specific short- and long-term goals to execute the business plan
- 4 Strategies, by functional group, to achieve the specific goals
- 5 Tactical plans to support the strategies
- 6 An effective organization designed around the tactical plans
- 7 Systems to leverage the organization

Take a closer look and understand that all companies, good and not so good, operate with the same core areas. Once again, no company is too small to have them all.

- 1 **Planning.** Have a plan, have a purpose, avoid drifting along.
- 2 **Leadership.** Great companies have strong, qualified leadership.
- 3 **Sales.** The best companies have a sales plan and are held accountable to it.
- 4 **Marketing.** In today's social media- and technology-driven world, the best companies have an image, a brand.
- 5 **People.** Is every position in your company staffed with the best, most qualified candidates who are motivated to help your company achieve its mission, contribute to the vision, and live up to the values and the overall plan for success?
- 6 **Operations.** Are your systems, processes, and procedures highly efficient and effective? Have you kept pace with technology and industry advances? Have you invested in the future?
- 7 **Finance.** How sound is your balance sheet? Your P&L? Your cash flow? Do you stay on budget and meet or exceed forecast? Is your debt and capital right for your business?
- 8 **Legal.** Do you have the right balance to mitigate internal and external risks and controls?

If your self-assessment indicates you have room to improve, perhaps it's time to consider an outside Advisory Board to help guide you in the right direction.

Is your business designed to meet challenges in a reactive or proactive fashion? I find the majority of owners of closely held businesses do not have formal outside boards of directors and audit committees to turn to for independent and confidential advice on a regular basis. Many times, their financial advisors and other centers of influence are helpful when certain challenges arise, but they may not be close enough to the business on a regular basis to be proactive. The response is typically reactive.

Where does leadership spend its time? In the business? Or on the business? I have seen an increase in the number of closely held business owners who recognize the significant contributions that a few independent and confidential advisors can make when there are regularly scheduled meetings where the agenda is focused on working on their business rather than the daily task of working in their business. Often times the role of the advisory

board member is expanded to provide advice on many other matters that are important to the closely held business owner.

Advisory board meetings typically include discussions around historical operating results and the unique items that impact those results. In addition to a review of historical operating results, there is usually discussion around expected future operating results and the challenges facing the business that may impact achieving those results. Many times, these discussions not only involve the external challenges, like competitor expansion or regulatory changes, the discussion also includes internal challenges like facilities constraints, capital improvements, financing needs, etc. The best advisory board meetings are usually the meetings where the agenda is amended on the spot to include real time challenges that need to be addressed in the immediate future.

In today's competitive labor market, I have worked with several closely held business owners to design specific incentive compensation programs for key employees. Oftentimes closely held business owners have worked closely with a select group of key employees for many years, and the institutional knowledge that these employees possess is critical to the company's success. Advisory board members can bring creative compensation planning ideas that include design of deferred compensation plans unique to each key employee or phantom stock plans that are applicable to a group of key employees, or they can assist closely held business owners with designing qualified retirement plans that motivate certain classes of employees through long-term qualified retirement plan participation. The broad experience of an outside advisor can oftentimes be very helpful in getting the closely held business owner to think outside the box.

When you factor in today's competitive workforce environment, with baby boomers entering their retirement years, many closely held business owners are finding that the development of a succession plan is now becoming critical. Whether it's a sale to a strategic buyer, transfer to a family member (or members) through a gift or sale, or an internal sale to employees through an employee stock ownership plan, the role of an advisory board in the development of a succession plan can be critical. Successful succession planning begins long before it becomes critical. Planning should begin several years before a closely held business owner is ready to exit. An advisory board can help the owner identify and develop the appropriate strategy. An advisory board can also keep the closely held business owner focused

on implementation of the plan, in addition to all the other daily responsibilities the owner has. It's the role of the advisory board to also keep the owner focused on ensuring that the owner's inner circle of management is focused on the daily tactics required to properly implement the plan.

Some final thoughts. Companies that regularly work on their business and improve their business scores in the core areas identified above more often than not achieve:

- 1 **Higher Value.** A higher value for your company, often by 20%-50% or more.
- 2 **Healthier.** A healthier, more competitive company, better able to support long-term growth.
- 3 **Successful Exit/Transfer.** A better chance of executing transactions on your terms and timetable.
- 4 **Satisfaction.** Happier, more productive, and efficient employees/family.
- 5 **Lower Risk, Less Stress.** Less stress and more peace of mind for the CEO/business owner/family

As you can see, a well-run advisory board can be very valuable to the owner of a closely held business. Having access to independent, knowledgeable advisors will give the business owner an added edge in today's competitive and ever-changing business environment. The return will be well worth the investment. **LC**



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