Considerations for High-Growth Company Boards in the New Year

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Governing pre-initial public offering (IPO) and small-cap public companies is a radically different challenge than governing enterprise-scale companies. In the year ahead, boards of high-growth companies will be considering some of the critical issues outlined below that are unique to their ecosystems.

Pre-IPO Companies

There are two different kinds of pre-IPO companies in today's marketplace: traditional venture-backed companies, and smaller, independently financed companies intending to undertake Regulation A+ (Reg A+) offerings.

Plentiful late-stage capital is inducing venture-backed companies to stay private much longer than in years past. One byproduct of this is that seed stage, Series A, and Series B venture investors are on boards for longer periods of time. I increasingly interface with CEOs of these companies who tell me: "Our early-stage investors no longer contribute any value because their expertise has been rendered obsolete by changes to our business model since they invested many years ago." Memo to Sand Hill Road: limited partners in venture funds don't benefit at all when venture capitalists lack the requisite expertise to contribute to portfolio company boards.

Enacted in 2012, the Jumpstart Our Business Startups Act's provision for more streamlined capital raising methods for small growth companies has resulted in a surge of mini IPOs that utilize Reg. A+.

On the one hand, optimizing capital formation for small businesses (which drive the majority of job growth) is a boon to the economy. But somewhat lost in all of the Reg A+ IPO hype is a conspicuous downside: small businesses are often unprepared for public company life. For boards considering this route, disregard the IPO encouragement you hear from lawyers and investment bankers, and simply speak directly to exchange-listed companies that are similar to your company and ask whether they would travel the same route if they had to do it all over again.

Small-Cap Public Companies

Many small-cap companies struggle to garner institutional sponsorship and effectively navigate Wall Street.

Since the financial crisis, trading volume has become increasingly important to small-cap companies (and correspondingly harder to come by). For small-caps with less liquid stocks, financings are smaller and more expensive—two handicaps that smaller public companies can ill afford. For any small-cap company that needs to access the equity capital markets, trading volume should be treated by the board as an enterprise risk.

In addition, unlike in larger companies, many small-cap CEOs are operating and governing a public company for the first time. Despite this fact, small-cap boards routinely presuppose that CEOs are capital markets experts. When small-cap boards assume that the CEO has the "Street stuff" covered, two things typically happen: one, CEOs will never ask boards for help in that regard lest they be regarded as less fulsome leaders; and two, CEOs will outsource critical capital markets decisions to service providers that have material conflicts of interest. Both are typically bad for shareholders.

A small-cap director asked me at the National Association of Corporate Directors' 2017 Global Board Leaders' Summit: "Do you think most corporate governance thought leaders realize that the issues they dwell upon don't matter to 90 percent of the public companies in this country?"

Small-cap boards and investors don't care as much about, for example, executive compensation, proxy advisors, or environmental, social, and governance issues. Rather, in the boardrooms of the more than 14,000 public companies outside of the S&P 500, most directors are concerned about things like capital formation, garnering sell-side equity research, exchange listings, and, you know, surviving. It's yet another illustration of how corporate governance practices are not one size fits all.