Cooley U: Board Basics
• A Board of Directors is a Legal Requirement for All Corporations
  • DE – One Director is Enough
  • CA – Three Directors are Generally Required Once Stock is Issued
  • Directors Do Not Need to be Stockholders
• Corporate Bylaws Set Parameters for Board & Directors
  • Size of the Board; How it is Set
  • Qualifications (not common)
  • Quorum
  • Filling Vacancies
  • Removal Procedures
  • How Action is Taken (more on this later)
  • Committees (more on this later)
How Directors Join and Leave the Board

- Initial Director(s) Most-Typically Appointed by the Sole Incorporator
- Then: Directors and/or Stockholders (depending on what bylaws say) Fill Vacancies Created by Resignations, Removals, Additional Directorships
- Directors Serve Until:
  - the [Next] Annual Meeting of Stockholders;
  - and Until His/Her Replacement is Duly Elected and Qualified;
  - or Until His/Her Earlier Resignation or Removal.
- Removal Requires Stockholder Action
- Voting Agreements Among the Corporation, Founders and Investors Most Typically Specify Board Membership (designation rights, voting agreement)
- Certificate/Articles of Incorporation Can Specify Specific Class/Series Voting for Directors
- FAQs/Follow-up Points
  - Must We Have an Annual Stockholder Meeting?
  - When/How are Stockholders Involved in these Processes?
How the Board Takes Action

- Meeting
  - Bylaws Set Notice Requirements (typically ~48 hours; can be waived)
  - Bylaws Set Quorum Requirements (typically majority)
  - Majority of Directors at the Meeting Can Take Action
  - Bylaws/Law Set Means of Meeting:
    - In-Person, Always Permitted
    - Does Not Need to Occur in State of Incorporation
    - Telephonic Nearly Always Permitted (all directors must be able to hear and be heard)
  - Written Consent Must be **Unanimous**
- Typically One Director = One Vote
- FAQs/Follow-up Points
  - A Director may not “proxy” or delegate their vote.
What Does the Board Approve?

- Hiring CEO & senior management
- Appointing corporate officers (different than titles)
- Amendments to the certificate of incorporation or bylaws
- Equity grants (stock, options or warrants)
- Formation of subsidiary
- A sale of the company or any other transaction resulting in a change of control
- Items that are “material” to the business (as opposed to day-to-day)
  - Materiality will change as the company grows
  - Borrowing or lending money
  - An annual plan or large capital expenditure
  - Bonus or compensation programs
  - Selection of auditors
• Role of the Chairman = Set the Agenda, Run the Meeting
  • Desired but Not Necessary to Have Chair Appointed
  • Frequently Chair is CEO for Early-Stage Corporations
  • Typically Chair is NOT the CEO for Public or Large Private Corporations

• FAQs/Follow-up Points
  • What is an “Executive Chairman”??
Meetings and Agenda

• At Least Once Per Year; 4-8 Times Per Year is Common
• Advisable to Schedule in Advance for the Whole Year
• Set An Agenda & Manage the Time Carefully
• Typical Agenda Items
  • Corporate Housekeeping (e.g. approve minutes (more on these later))
  • Business Overview (can include detailed updates by executives responsible for particular business unit such as sales, product development)
  • Financial Review
  • Executive Session (usually includes option grants, if any)
• Create a Board “Deck” and Circulate in Advance – Nothing Discussed at the Meeting Should be Brand New Information for Directors; Manage “Bad News”
• FAQs/Follow-up Points
  • What Formalities Are Required?
Who Attends Board Meetings and Where

• Who Attends:
  • All Board Members
  • Key Members of Executive Team (some depending on the agenda)
  • Outside Counsel
  • Board Observers, if any
• Location: Large-Enough Room and Privacy from Employees (borrow space from investor, outside counsel, etc.)
• Considerations: Confidentiality; Sensitive Matters; Need to Know

• FAQs/Follow-up Points
  • Why Should I Have Outside Counsel at Board Meetings?
Minutes and Record Keeping

- It is Important to Keep Good Corporate Records
  - Deal/Financing Diligence
  - Legal Opinions
  - Legal Requirement
- Corporate Records Should be in the “Minute Book”
  - Charter and Bylaws
  - Board Minutes (signed by the secretary) and Actions by Written Consent
  - Stockholder Meeting Minutes and Actions by Written Consent
- Audience for Official Minutes
  - Potential Investors and Acquirers
  - Litigants
- Keep the Minutes Formal, Accurate and High-level; Do Not Include Sensitive Information
- Other Key Records = Personnel, IP, Leases, Debt, Commercial, Financings, Options, Etc.
Committees

- Role of Committees = Handle Delegated Board–Level Matters Without Having to Involve the Full Board; Particularly Used Where Conflicts Exist
- Committee Membership is Limited to Members of the Board (others may attend meetings)
- DE Committee Can Be 1 or More Directors; CA Committee Can Be 2 or More Directors
- Most Common Committees = Audit & Compensation
- Other Committees: Nominating and Corporate Governance (most Public Corporations have this), Financing Committee, Non-Executive Stock Option Committee & Committees Set Up for Specific Transaction or Issue
- Certain Actions Cannot Be Delegated
  - DE: Actions that Require Stockholder Approval & Amending Bylaws
  - CA: Actions that Require Stockholder Approval, Filling Vacancies on the Board or Committees, Fixing Director Compensation, Amending Bylaws, Certain Distributions, Appointment Of Committees
Fiduciary Duties of Directors

• Duty of Loyalty
  • Act Solely for the Benefit of the Corporation and its Stockholders
  • Refrain from Conflicts of Interest

• Duty of Care
  • Be Informed
  • Act Reasonably
  • Act Responsibly After Consideration of Relevant Materials and Information and After Appropriate Deliberation (get input from advisors)

• Other Duties: Confidentiality, Corporate Opportunity, Candor

• Business Judgment Rule: Directors are Presumed to Have Acted in Good Faith and in the Interest of the Corporation

• Interested Transactions

• Procedural Considerations: Independent Directors; Disclosure of Conflicts; Recusal of Directors; Clear Record Keeping; Use Advisors; Stockholder Approval
• Breaches of Fiduciary Duties (i.e. breach of duty of loyalty):
  • Personal Liability for Damages
  • Injunctions
  • Loss of Indemnification (more on this later)
  • Loss of D&O Insurance Protection (more on this later)
  • Court Costs, Legal Expenses, Awards, Damages, Time and Money
• Duty to Stockholders Shifts to Duty to Creditors in the Case of Insolvency
Indemnification of Directors and D&O Insurance

• Certificate/Articles of Incorporation and Bylaws Typically Include Indemnification Provisions for Directors and Officers
• Many Corporations Also Adopt Indemnification Agreements with Directors and Officers; Include More Details of Procedures and Coverage
• D&O Insurance is a Good Idea for Early-Stage Corporations and a Must-Have for VC-Backed, Later-Stage and Public Corporations
  • Covers Directors’ and Officers’ Personal Liability for Corporate Actions
The Role of the Board

- Day-to-day operations typically handled by management, but the Board is ultimately responsible for management and oversight of the company
- Frequency of meetings, involvement in operations, compensation of Board members is highly dependent upon the stage of the company

Pre-Funding
- Primarily founders, but looking for mentorship

Post-Funding
- Investors will be involved, it is important to have an independent voice

Pre-Public/Public
- Public company requirements