Stifling debate at board meetings can destroy value at your portfolio company

By CHRISTOPHER J. HEWITT and JAYNE E. JUVAN

In order to achieve high-performing results, portfolio companies of venture capital and private equity firms need well-functioning boards that afford room for individuality, debate and discussion. Theranos, the now largely discredited Silicon Valley startup that initially gained a lot of buzz for its revolutionary blood-testing technology, serves as a cautionary tale about how a dysfunctional board destroys value.

The company recently announced that it is closing its doors, and investors have lost significant capital. It is possible that the Theranos story would have had a much happier ending had Tevanian’s questions been taken seriously. Presumably, Tevanian raised these issues before Theranos began rolling out its technology worldwide. If Holmes and the board had engaged with Tevanian and addressed his concerns, perhaps they could have put more reasonable timetable in place to perfect the technology before actually deploying it for patient use. The following are a few lessons from the Theranos situation for boards of venture capital or private equity-backed companies:

THE IMPORTANCE OF HAVING A WELL-FUNCTIONING BOARD CANNOT BE OVERSTATED.

Most corporate laws require the business and affairs of a corporation to be managed by or under the direction of a corporation’s board of directors. The board is responsible for overseeing the corporation’s strategy and ensuring compliance with an array of often overwhelming laws and regulations. Given that boards have enormous responsibilities, they should develop strong processes in an effort to ensure they are well-functioning and behave in a manner that enhances the value of the enterprise.

BOARD COMPOSITION SHOULD ENSURE DIVERSITY OF THOUGHT.

Many boards are appropriately characterized as “clubby.” When recruiting board members, it is easy to gravitate toward individuals who are friendly, who will go with the flow and who will take the path of least resistance. Opening up a closed club and recruiting accomplished individuals who do not have deep-seated relationships with others will help to avoid a culture of groupthink.

INDIVIDUAL DIRECTORS SHOULD HAVE THE ABILITY TO EXPRESS CONTRARY VIEWPOINTS WITHOUT FEAR OF RETALIATION.

The board should adopt a shared philosophy that affords individual directors the ability to express honest viewpoints and debate matters. Other board members and shareholders should not pressure directors to refrain from asking questions or challenging decisions. Diversity of thought can help to minimize the number of blind spots the board has and may lead to better decisions that help to bring about more favorable outcomes. Boards should take care to ensure that politicking does not occur behind the scenes and that the real work of the board occurs in actual board meetings, not in “meetings outside of meetings.” Corporations are stronger when directors are empowered to debate issues, and directors should be able to perform their duties without fear of retaliation.

Christopher J. Hewitt and Jayne E. Juvan are partners and co-leaders of the M&A practice at Tucker Ellis. Contact him at 216-696-2692 or christopher.hewitt@tuckere Ellis.com. Contact her at 216-696-5677 or jayne.juvan@tuckere Ellis.com.