

Founders and corporate governance part 1: Starting your business plan

Executives & Entrepreneurs

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- Corporate governance describes the structure of rules, practices, and policies that underpin how you direct and manage your company.
- Governance covers a variety of issues. Examples include compensation, risk management, employee treatment, reporting unfair practices, and your business's impact on the climate.
- In a series of three articles, we shall explore why corporate governance can be a worthwhile early investment for founders.
- This first part seeks to show how robust thinking, documenting, and execution of corporate governance can help founders start their business plan.



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You're a founder. You're working all hours. Your to-do list is endless.

Corporate governance—the structure of rules, practices, and policies that underpin how you direct and manage your company—is not your top priority. Corporate governance is a privilege for the established firm, a luxury to tackle once your first funding rounds have been successful.

If the above statements ring true for you, we believe it is important to stop. And reconsider.

In short, corporate governance can help founders start their business plan by:

- Setting clear expectations for who does what and who owns what. This potentially minimizes disputes and maximizes your time for creating value.
- Articulating sustainability objectives with the same clarity and importance as your market offering. This

may maximize financial and societal returns, while broadening your startup's appeal to stakeholders.

- Challenging you to choose the most flexible legal structure and writing down why. This can give you a wider range of options to scale your business or sell it when the time is right.

In a series of three articles, we shall explore why corporate governance can be a worthwhile early investment for founders.

In this first part, we show how robust thinking, documenting, and execution of corporate governance can help founders **start** their business plan.

In part 2, we highlight how corporate governance can help **scale** your business.

And in the third and last part, we discuss how corporate governance can help **switch** your business—whether a sale, a family transition, a buy-out, or a winding down.

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We also hope to demonstrate that corporate governance is good practice for all business owners. Governance metrics also matter to stakeholders—whether employees, suppliers, regulators, or potential investors (on the last point, please see our paper [Three ways sustainability transparency can affect your business exit](#)).

Something important to note: corporate governance is a living process. Governance works best if it evolves with your startup, family, and financial plan.

We advise making corporate (and family) governance a dynamic, not static, process. And drawing on external expertise can provide different perspectives or alternative scenarios, so your governance plans stay current to your needs and resilient to uncertainty.

So, can corporate governance help *start* your business plan?

For many founders, their first priority is speed. Speed to build their product or service. Speed to take their offering to market. Speed to generate their first sales.

But we believe founders should consider the adage: “More haste, less speed.” And founders can potentially set up their startups more solidly if they focus on several aspects of corporate governance.

Corporate governance can help startups to start up if you:

1. Formally document who owns what and who does what

Corporate governance begins at incorporation. Founders would do well to look beyond “cookie cutter” templates or conventional thinking at the very first stages of their startup. Examples might include accepting model articles of association without considering your particular circumstances, or unquestioningly accepting that founder, CEO, and the board are all one person.

There is another, potentially more robust way to begin your startup’s corporate governance process.



Source: Getty Images

Begin by understanding, discussing, and documenting the consequences of your articles of association.

For example, do economic and operational interests look the same for each founder when there are more than two? Does an early buy-sell agreement ensure continuity of operation in case one founder leaves?

(Remember to that financial tools that underpin buy-sell agreements, like a financial portfolio or life insurance approach, are likely to require the least amount of payout, and therefore the fewest investments, when a firm’s value is lowest at the start.)

You can then consider formalizing the roles and responsibilities of your firm’s employees.

While it may be tempting (or necessary as a solopreneur) to have a single supervisory, operational, and economic leader, it’s unlikely to be optimal.

Discuss and document how much influence owners have over operational decisions. Identify information gaps—legal structure, market research, regulatory demands—and consider whether these would best be filled by operational talent or an external supervisory board.

2. Record sustainability policies, so they become core to operations, not complementary

If founders have environmental or social ambitions for their startup, we believe recording these aims in robust, company-wide corporate governance documents cannot start soon enough. Why?

First, founders’ crucial market research might uncover that sustainability considerations are “must-haves” even to get their business off the ground. In our paper [Three steps to](#)

[becoming more sustainable...and profitable](#), we noted that compliance, regulation, consumer demand, and stakeholder demand are all making sustainability an integral part of doing business for growing industries and sectors.

The costs of non-compliance with sustainability regulation are rising. In 2019, the US Environmental Protection Agency opened 170 criminal cases and charged 137 people for environmental breaches (both figures rising from the prior year), and it collected USD 471.8mn in overall penalties and fines.^[1]

The risk of not meeting your target audiences' sustainability expectations is considerable, especially for B2C startups. A survey of nearly 20,000 consumers across 28 countries found that close to 80% of people say sustainability is important to them, and 57% of shoppers would change their buying patterns to reduce their environmental impact.^[2]

Second, we believe that corporate sustainability delivers the most commercial and societal impact when founders tackle the material issues. Materiality is another term for mattering—the sustainability issues that will impact your revenues, costs, and profits.



Source: Getty Images

Not all founders will have explicit sustainability goals. But for those that do, it is arguably easiest to define and codify sustainability at the same time as you define and codify what your startup's material impact will be.

The early planning stages of your startup are when you decide what problem you're trying to solve, what product or service you'll propose to the market, and how to turn real-world impact into a sellable solution. For sustainability-minded startups, the environmental and social aspects are integral to your product development. They're not a consequence of it.

Deciding on your sustainability plan and writing it down could help startups find their niche. Entrepreneurs should look at existing problems through a sustainability lens; ask customers, employees, and other stakeholders their views on the topic; then make materiality a management or founder decision backed by data, robust policies, and clear communication.

3. Deliberate on your legal structure and document why you chose it for stakeholders

Your startup's choice of legal structure may seem like a boring detail compared to the excitement of creating a new product or service and beginning production. Practical implications of your legal structure—how the firm is owned, how it is taxed, the ease of transferring shares, and your ability to separate voting interests from economic ones—can seem like luxury problems when starting out.

However, choice of legal structure at inception can affect the entire course of your business.

There are many reasons why deliberating on legal structure and documenting your choices make sense. We'll focus on two.

First, careful selection of legal structure can give your firm's stakeholders confidence in their future rights and responsibilities—and formal materials and mechanisms for resolving disputes.

It is particularly important to give careful thought about how your firm maintains operational control if or when you accept external investors' capital. Your legal structure should have the flexibility to accommodate changes in managers, investors, and supervisors.

You may want to consider the implications of your legal structure for stakeholders to exit the company. For example, your choice can, in some jurisdictions, cut off later exit paths for both you and your other stakeholders. Your decisions at inception can, in the extreme, cut off certain types of investors before your firm has even begun. We shall discuss how corporate governance can help you switch your business in part 3. For now, please see more on this topic in our paper [Talk, plan, do – a guide to business succession and exit](#).



Source: Getty Images

Second, your choice of legal structure can have major implications if your startup is a family business.

It may seem premature to consider transferring economic or operational value to your loved ones when you're just starting out. Yet it can make sense from numerous perspectives—control, equality, or taxation—to consider the relationship between your business, financial wealth, and family at an early stage. In some instances, founders may benefit from adding a financial advisor to their listed of trusted advisors at the inception stage.

Look out for the next two parts of this series.

[1] US Environmental Protection Agency "EPA Announces 2019 Annual Environmental Enforcement Results," 13 February 2020, accessed 16 October 2020. URL: <https://www.epa.gov/newsreleases/epaannounces-2019-annual-environmental-enforcementresults>.

[2] IBM Institute for Business Value in association with National Retail Federation (2020) *Meet the 2020 consumers driving change*, accessed 16 October 2020. URL: <https://www.ibm.com/downloads/cas/EXK4XKX8>.

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