

The Boards:

The Legal Board of Directors and The Strategic or Scientific Advisory Board (SAB)

J. Christopher Lynch
CED

Research Triangle Park, North Carolina
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Objectives for Today

1. Understanding differences between Legal Board of Directors and the SAB
2. Understanding reasons why people might serve on either type of board
3. Understanding risks for Board members and what members of either type of board can do for your company
4. Guidelines for structuring the legal Board and the SAB
5. War stories and Q&A

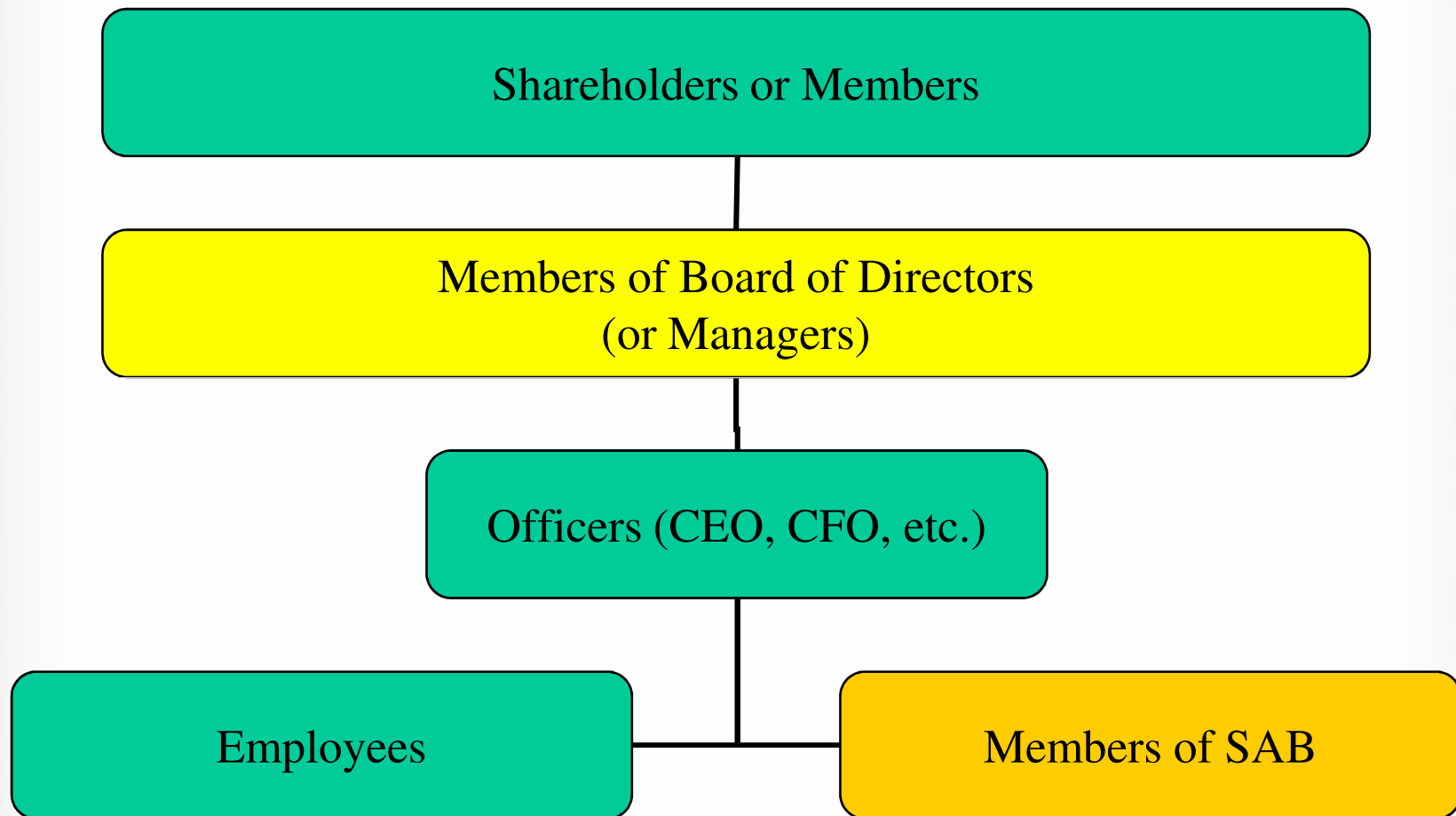
Legal Board and SAB Differences

- Legal Board: highest level of authority in a corporation
 - Accountable only to shareholders
 - In LLC, can have either “Managers” or a “Board of Directors” with similar authority
- SAB: prestigious advisory group reporting to management (CEO or Chief Technology/Science Officer)
 - Accountable only to management

What's the Real Difference?

- The **YOU** is in a different place
 - Board of Directors
 - **YOU** work for them
 - SAB
 - They work for **YOU**

Corporation / LLC Organization



Why Have a Board of Directors?

- Keeps you honest and accountable
- Strategic guidance
- Connections
- Money sources
- (Required by corporate statutes)

What should your Board look like?

- Founders
- Significant investors
- Possibly one independent director
- For public companies, the rules are different
 - Because of large, passive investor base

Legal Duties of the Board of Directors

- “Fiduciary Duties”
 - Duty of Care
 - Duty of Loyalty
 - Duty of Good Faith
- Potential Personal Liability
 - Investors and Other Shareholders / Members
 - Creditors
 - IRS and NC Department of Revenue
 - Other

Examples of Director Liability

- WorldCom
 - Directors pay \$18 Million to former shareholders
 - 20% of their collective net worth
- Enron
 - Directors pay \$13 Million to former shareholders
 - 10% of their trading profits
- Disney
 - Board authorized a \$140 Million severance package to Michael Ovitz
 - Ultimately, case dismissed

Why Serve on the Legal Board?

- Legal requirements
- To protect your investment
- For compensation
 - Range of approx. \$15,000 to \$75,000 in annual cash retainer (public companies only)
 - Stock or options for 0.5% to 1.0% of outstanding shares

Why have an SAB?

- Access to, and credibility with, strategic partners
- Credibility with investors
- Access to inside information on university / industry research and developments
- Relatively inexpensive consulting on business strategies and business plans

Where to Look for SAB Members

- Academic research institutions
- Trade organizations
- Former government officials (mainly for regulated industries)
- Former successful company founders
- Other wealthy individuals

(The common denominator is access to connections, especially money connections.)

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Why Serve on the SAB?

- No liability concerns
 - Note: possible issues under university conflicts policies
- Limited responsibilities
- Prestige
- For compensation
 - Range of \$0 to approx. \$2,500 in per-meeting fees
 - Stock or options for 0.1% to 0.5% of outstanding shares

Rules for the Board of Directors

1. Keep number of Board members to a minimum
2. CEO should set Company performance expectations (and ensure that Company meets them in a timely manner)
3. Avoid granting Board observer rights
4. Be prepared to obtain “D&O” insurance
5. Avoid even numbers on the Board
6. Don’t look at the Board composition as the primary means of “control”

Side Discussion on Control Issues

Different Means of Control:

1. Majority of Board
2. Majority of Stock
3. Ownership of Patents or other IP
4. Control of Needed Cash
5. Key Customer Loyalty
6. Employee Loyalty

Managing Board Meetings

1. Forget Roberts Rules of Order
2. Plan for meetings of 1-2 hours at most
3. No more than 1 meeting per month
4. Prepare an agenda and send it out at least 2 days before a meeting, with a “Board Package”
5. Include detailed financial information in the Board Package

Managing Board Meetings (cont'd)

6. Every agenda should discuss current cash position and plans for funding operations
7. Avoid using Board meetings for strategic planning sessions
8. Ask the Board to help with key issues (such as raising capital or hiring key management)
9. The CEO should run the meeting
10. No need for reports from all officers

Questions?

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THANK YOU.

J. Christopher Lynch
781-4000
clynch@wyrick.com

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