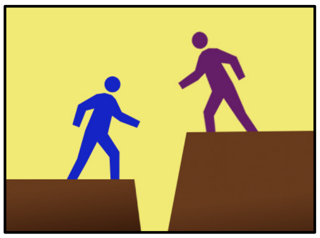
Helping Companies Conquer
Their Financial Challenges

SBell Consulting LLC

Bridging the Information Gap
(Between Management and Investors)



The owners of a company may reach a point when they are faced with entering into debt and capital markets to secure funding for working capital, growth, acquisitions or other needs. There are different private paths to take including conventional bank financing structures, secondary or mezzanine debt, family business or individual investment, private equity, as well as public market sources such as registered debt and public stock offerings.

When looking for funding alternatives, companies usually approach banks for traditional financing vehicles such as cash flow, asset based lending or capital expenditure funding. If the company doesn't have the required cash flow or collateral that is a requirement of traditional banks, management needs to look at one of the other options.

Private sources of capital may step into these situations of increased credit risk. In order to minimize some of this risk, these funding sources or "investors" play a more active role than a traditional bank in the governance and oversight of the company. While they usually don't get involved in day-to-day operating decisions, they will most likely require board seats or attend meetings as a board observer. This involvement gives the investor the opportunity to influence and participate in the formulation and execution of company strategy, keeping a close watch on their investment.

But it is difficult for investors to keep tabs on their interests solely by attendance at board meetings. They will also want to implement a reporting structure that provides a free but structured flow of information between the company and the investors to provide comfort between board meetings.

Before engaging private funding sources, financial reporting and operational tracking is an exercise usually limited to participation by upper management. After obtaining private funding management will find that it has an additional constituency that it must satisfy. Management may not be prepared for that oversight. But even if management is open to the new sets of eyes, it may not be prepared to implement the reporting structure needed for communication to these individuals.

The amount of operational involvement and influence an investor wants to have varies from investor to investor. While they may not have industry specific expertise in each of their portfolio companies, they usually do possess significant business experience and acumen. They will want to provide assistance when they can. They will also expect the company to loop them in when a significant business issue arises between board meetings. They want to know good news and bad news. If there is a problem on the horizon, they want to know about it almost as soon as management becomes aware of it. If an issue later becomes a larger problem, it is always easier to manage investor involvement if they are kept in the know. Investors don't like surprises.

The best way to satisfy investors is to provide periodic, consistent and insightful operational and financial reports and metrics as compared to predetermined budgets and goals. Very often the investors have other portfolio companies and are used to receiving this information in a specific format. Other times, if management's reporting structure is sufficiently detailed, the investor will just accept that format.

Finance teams usually take the lead for coordinating this communication stream since most of the reporting revolves around financial results. But additional information usually required to be reported includes operational and sales data that is key to tracking the performance of the company. It may be best to have the finance team centralize activities internally with the other departments responsible for tracking and producing the data, in order to have just one point of contact between the company and the investors. Follow-up discussion can always be had by the investors and operational and sales teams, but one point of contact for the reporting enhances the consistency around the flow of data and ability to track deliverables.

Some of the non-financial data that is often produced for investors includes sales activities such as proposal tracking, proposal success rates, contract status, pipelines and revenue backlogs. From the operational side the data may include customer specific information such as customer trends, production or development trends, issues or results.

The frequency of reporting often is less focused on monthly financial reporting and more directed at daily and weekly tracking of key operational statistics that foretell positive or negative trends in the business, later ratified by actual monthly financial reporting. Sometimes the rigor of the reporting process required by investors, while it may be an annoyance in the beginning, often results in improving the reporting process and quality of information available to management.

During later stage negotiations and immediately upon consummation of a funding transaction, management should engage the investors in a dialogue about the information that the investor would like to receive, what information the company can readily and periodically make available, and work out a plan for communication of this information to avoid the repercussions of an information gap.

This white paper was written by Steven Bell