

BRILL STYBEL CASE

FOR SEAT AT THE TABLE

HOW AND WHEN SHOULD THE BOARD OF BRILLIANT CONSTRUCTION

FOCUS ITS ATTENTION ON RISK?

Brilliant Construction is a privately held construction company that once was a third-generation \$150 Million family business. The family sold controlling interest to Heritage Private Equity. Heritage is looking at it as an investment for the next 2-4 years. Their goal is to grow the business and then sell it to a larger construction company in the wake of an anticipated surge in Federal construction money on infrastructure.

Brilliant Construction is the nation's leading construction company specializing in metal ceilings. At one end of the customer market company bids on construction of specialty metal ceilings designed for prisons around the world. These metal ceilings keep inmates from escaping. At the other end are beautifully designed metal ceilings that go into museums, airport terminals, etc. Brilliant Technology has developed a reputation within the U.S. architecture community as the "go to" construction company for elaborately designed metal ceilings.

Brenda Woods is CEO of Brilliant and a member of its Board of Directors. It was Brenda who inspired the Woods family to take cash out of the business. She has been pleased with the decision and has a positive relationship with Fred Waverly. Fred is Chair of the Board and a Partner at Heritage.

There are seven five Board members including Brenda and Fred.

June Wagner is an external Board member. The other four Board members are Partners of Heritage.

After one Board meeting, Brenda, Fred, and June are having dinner together.

What Is the Role of the Audit Committee?

June is a retired partner from a Big Four CPA firm and serves on two other Heritage portfolio company boards.

June mentioned recent newspaper articles about ransomware cyber-attacks. She attended a cybersecurity webinar given by her former CPA firm. The cybersecurity expert predicted that ransomware attacks would increase, and the key targets would be firms like Brilliant Technologies.

She stated that there is nobody on the Board with cybersecurity expertise. There is nothing on the agenda to focus on cybersecurity risk management. June thought that the portfolio for managing cybersecurity risk should be with the Audit Committee since it is a risk issue. And Heritage should mandate all Audit Committees of all Heritage portfolio company boards to review cybersecurity protection efforts.

June stated that the Board's failure to review management's effectiveness in cybersecurity would amount to "professional malpractice." If necessary, the Committee should hire an external cybersecurity consulting firm to provide advice/counsel.

Brenda Responds.

Brenda responded by saying she could support the idea. But cybersecurity is only one risk facing Brilliant Construction.

Cybersecurity is indeed important. But Brilliant Construction also face other risks such as future pandemics, climate change, Artificial Intelligence, Robotics, and unionization effort at this nonunion shop. There are probably other risks the company should be thinking about to capitalize on or to mitigate. Is the Audit Committee the proper forum?

"For example," Brenda states, "China is a rising economy. As it builds out, Chinese architects might want metal ceilings. Shouldn't we be establishing our presence with Chinese architects now? Risk also contains opportunities."

Brenda suggested that the full board be spending at least one day a year focusing on risk. In an ideal world. The CEO and her staff would be spending time on these issues as well. But "we get so focused on day-to-day operations. We don't do it. Why not have the Board do it and we attend the meeting?"

June countered that the full Board agenda is already jammed. "If you don't want the Audit Committed focusing on cybersecurity, why not establish a new Committee called The Risk Committee?"

Fred Waverly has been silent during this discussion. Now he was moved to say to June, "Our Board members are already overworked. If we add another committee, we need to increase the size of the Board from seven to nine. That's additional cost and sets a precedent for our other private equity portfolio Boards. Is adding such costs the right thing for our institutional investors?"

Fred is also thinking, "Risk is such a broad topic. How can we structure a full board meeting focusing on risk without boring or overwhelming our Directors? The reality is we Directors don't know what questions to ask and this CEO hasn't a clue either. And management is so focused on day-to-day operations, they don't have time to think about risk the way Brenda is defining it."

By the end of the dinner, no consensus was reached but Fred knew he would have to get back to both Brenda and June.

What Are You Going to Tell Fred?

You are an external Director on the Board of Brilliant. The following day, Fred calls you and repeats the details of the dinner conversation. He asks for your opinion.

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