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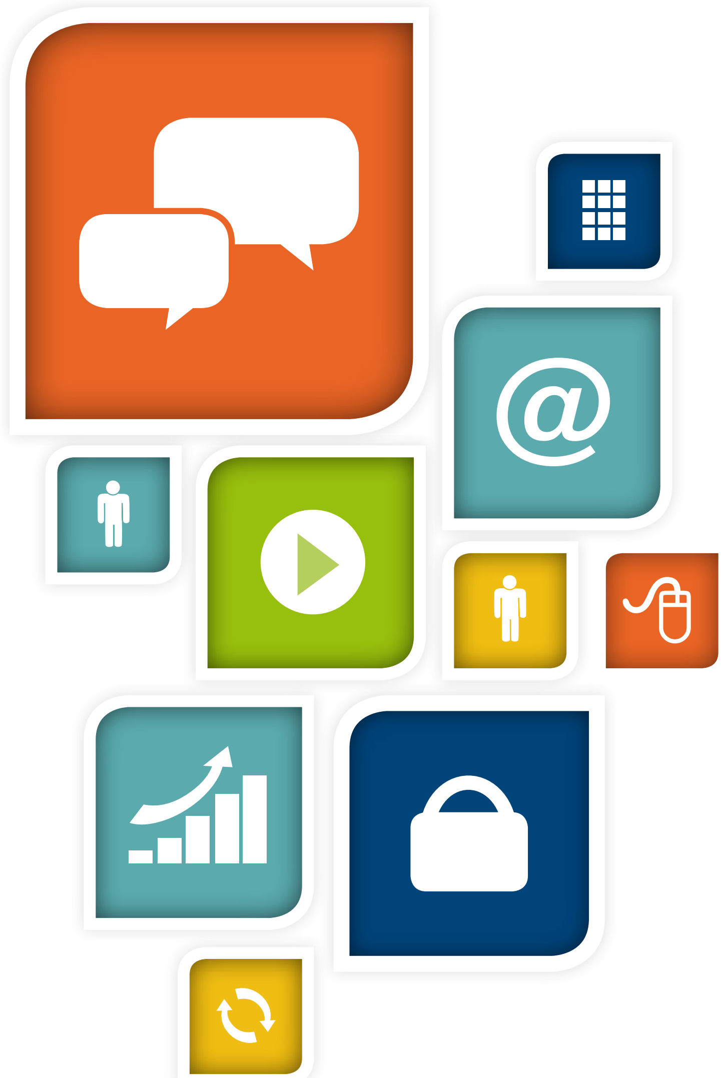
10 Best Business Practices - Tech Edition

Making the leap from early stage to growth stage



High technology companies may move at a rapid pace, but it's important to take it slow and steady when planning for the future. For companies looking to make the leap from early stage to growth stage, keep in mind these 10 best practices to find success and stay competitive.

For every example of an enduring high-tech growth company, there are countless more that don't make it. Some of the most talented entrepreneurs get tripped up by product issues, while others successfully launch but plateau well below their aspirations. Still others may get public, but are unable to achieve consistent growth and ultimately fail to create sustaining value.

- THE GROWTH-STAGE TECH SUCCESS RECIPE,
FORBES, JANUARY 2013

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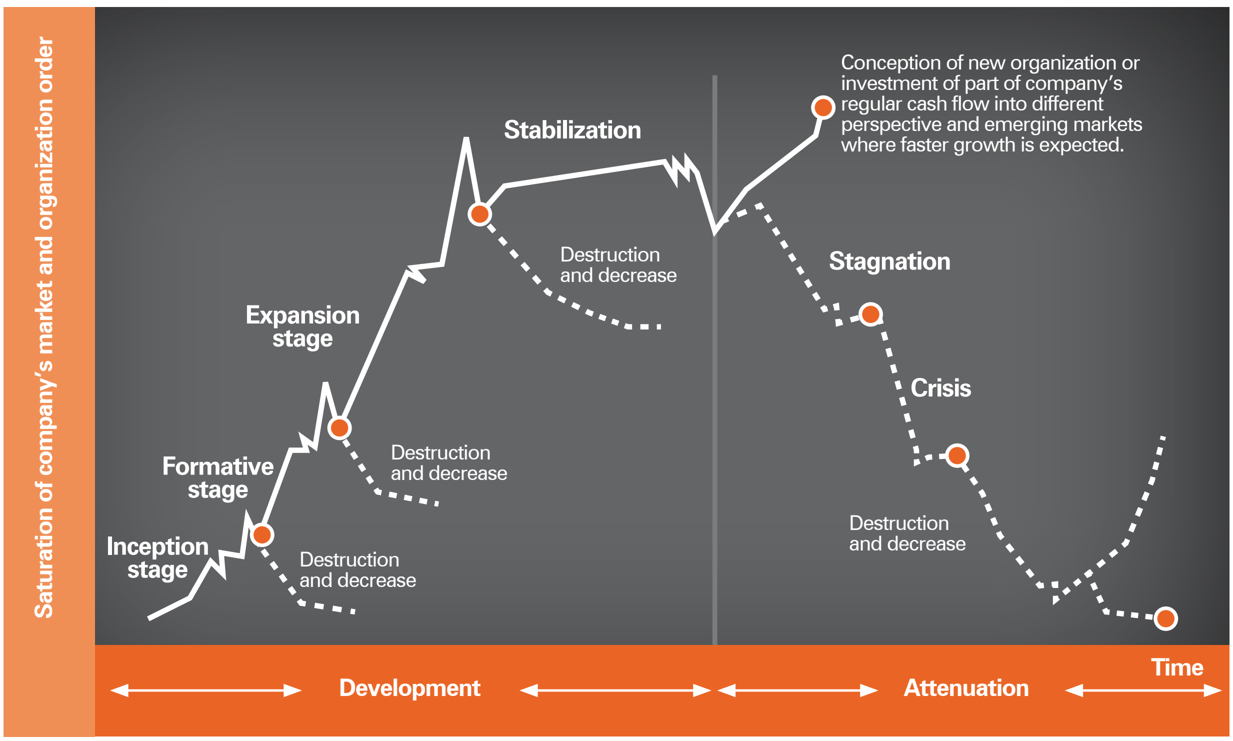
Introduction

The single most difficult transition for a technology company is moving from their **start up or early phase of life into a growth stage,** where they will see increasing sales, high profits, and market entry by competitors. While there have been numerous studies about why high tech firms fail to reach mature, stable organizations, the focus of this report is to identify best practices that help high tech companies move from early or formative stages to a growth or expansion stage.

Life-cycle of organization



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The insights, observations and guidance presented in this whitepaper are based upon the experience of our Firm in helping companies of all shapes, sizes and industries throughout our history. We have seen some companies – albeit a handful – become business superstars, and others fail to reach their promise.

So, we gathered our thoughts and are pleased to present a collection of best practices – focused mainly in the area of finance and operations – that we've seen from great companies making the transition from early stage to growth.

1 Use a team of trusted advisors

Perhaps one of the most critical and fundamental characteristic of early stage companies that successfully make the leap to the growth stage is that the company's management surrounds itself with **trusted advisors**. These advisors not only bring different types of technical skills to the table, they bring a wealth of expertise and experience that can accelerate the leap, see problems or issues before they become company-killers, or serve as reality checkers that can separate hyperbole from reality.

Your early stage high tech company will need trusted advisors such as an accountant, lawyer, banker, marketing consultant, and an insurance broker at a minimum. As your business grows, your cadre of trusted advisors will also grow and include technical experts and other specialized and support professionals.

For more information on this topic, visit our website, or read our blog post, "Who Should Be On Your Company's Team of Advisors and Why" here.

2 Have a multi-layered funding strategies

Regardless of life cycle stage, your high tech company is always going to be involved in a brutal battle for financing its growth. We have found the companies that are successful in making the leap from emerging to growth, use multiple financing tactics and strategies, rather than putting all of their eggs in one basket. Not only will they look at angel funding, but at the same time, they'll be talking to banks, applying for government loans or guarantees, or even looking at options like using equity. One word of caution – make sure you include your trusted advisers in your discussions, as you'll want to make sure that how you are securing financing today doesn't come back to haunt you tomorrow.

For more information on this topic, visit our website, or read our blog post, "Financing Your High Tech Company's Growth" here.

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Have a well thought out and executed business strategy and plan

A business plan is more than just an academic exercise. It has many different purposes; from helping in raising capital to serving as a roadmap that aligns strategies, tactics and expectations of all of the stakeholders involved in the business.

This is particularly important for high tech firms looking to make the leap from early stage to growth stage. As your company matures, so too must your vision and expectations, as the realities of marketing, competitive, human resource and a host of other internal and external factors must be identified and addressed.

For more information on this topic, visit our website, or read our blog post, "A 10 Point Business Plan Checklist for Your High Tech Company" here.

4

Create financial roadmaps and budgets, and have the discipline to follow them

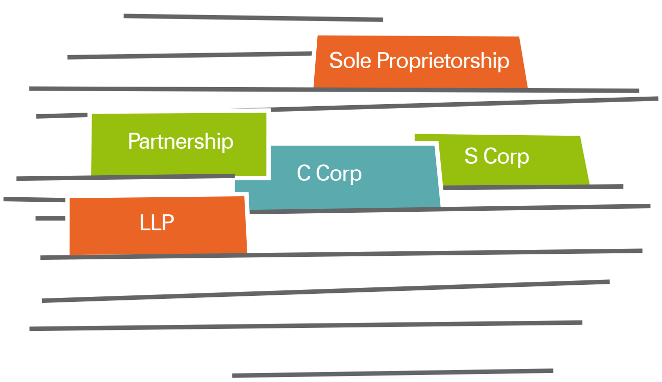
As high tech companies mature, it's no longer feasible (or desirable) to do back of the napkin financial planning and budgeting. Funding sources, vendors and other stakeholders are going to want to see that you have a disciplined and active annual budgeting process that can be relied upon.

But beyond satisfying the needs to deliver information to your stakeholders, going through an annual (or even semi-annual) budgeting process makes sense because it represents an opportunity to do a critical evaluation of performance against projections leading to making adjustments that can improve the performance or profit potential of the company.

For more information on this topic, visit our website, or read our blog post, "6 Reasons Why to Prepare an Annual Budget for Your Early Stage High Tech Company" here.

5 Start with selecting the right type of legal entity

Most high tech start-ups need to pay more attention to their legal status and selection of entity type, as decisions they make today will have longer term consequences for the taxation, ownership and growth of the company tomorrow. Sole Proprietorships, General Partnerships, Limited Partnerships, Corporations, S Corporations and Limited Liability Companies are the most common types of entities, but each comes with consequences such as limitation of liability; impact on taxation; and, flexibility to raise capital for future growth.



It is critically important to discuss this issue with your team of trusted advisors, who will explore issues with you such as how the business will be funded, number of employees anticipated, current and future plans for ownership of the company, where you will be doing business, and your exit plan or strategy.

For more information on this topic, visit our website, or read our blog post, "Choosing the Right Type of Legal Entity for Your High Tech Company" here.

6 Offer stock compensation plans that play by accounting and tax rules

Stock based compensation is a time honored way for high technology start-ups to create incentives for executives and employees to contribute to the company's growth and value. They're a great tool for attracting and retaining employees, as well as a way to protect cash on hand.

There are a variety of different types of plans, each with their own set of pros and cons: including stock options, restricted stock, unrestricted stock, phantom stock, stock appreciation rights, and employee stock purchase plans.

Stock option plans come with a bewildering maze of laws and requirements including securities law considerations (such as registration issues), tax considerations (tax treatment and deductibility), accounting considerations (expense charges, dilution, etc.), corporate law considerations (fiduciary duty, conflict-of-interest) and investor relations (dilution, excessive compensation, option re-pricing). This is often the area that unforeseen mistakes occur such as reporting issues, modifications, etc. Engaging your accountants and attorneys in structuring a stock compensation plan is a critical move.

For more information on this topic, visit our website, or read our blog post, "Options for Your High Tech Company's Stock Compensation Plan" here.

7 Minimize inventory and protect cash

Cash flow management can spell the difference between a firm that successfully makes the transition from early to growth stage, or a firm that stands a good chance at failure.

Part of your firm's plan to make the leap must be to develop cash management strategies and tactics. These can range from tightening customer credit to weeding out unprofitable customers, and more. One of the biggest areas of focus for your firm should be upon inventory management and control, as tying up cash in inventory may not be the best business management practice for a growth oriented high tech company.

Cash management planning and budgeting is a fundamental requirement for companies looking to make the leap from early stage to growth. Your accounting, business and operations advisors should be involved in these discussions.

For more information on this topic, visit our website, or read our blog post, "20 Ideas for Improving Your High Tech Firm's Cash Flow and Inventory Management" here.

8 Use business processes management to increase productivity and reduce costs while generating the same (or better) outcomes

When successful high tech firms move to a growth stage, they're often employing Business Process Management to increase productivity and efficiency. According to SearchCIO (http://searchcio.techtarget.com/) Business Process management (BPM) is "a systematic approach to making an organization's workflow more effective, more efficient and more capable of adapting to an ever-changing environment. A business process is an activity or set of activities that will accomplish a specific organizational goal."

BPM requires identification, analysis and measure of business processes in the company with an eye toward finding ways to execute workflow activities quicker, better and less expensively.
Key benefits of BPM include:

- Increasing accountability for departmental functions
- Simplifying regulatory compliance
- Reducing waste
- Enforcing safety and security measures
- Protect company resources and information

For more information on this topic, visit our website, or read our blog post, "Is it the Right Time for Business Process Management in Your High Tech Firm?" here.

9 Select the right ERP system and software

One of the most difficult, costly and far reaching decisions your high tech firm will need to make at some point in time is whether you have outgrown your current ERP system. To make the leap to growth stage, will it be necessary to replace what you have, or surgery is a better option?

According to data collected for the Mint Jutras 2011 ERP Solution Study, 62 percent of businesses with an ERP system installed are running the first solution ever implemented in the company. That means 38 percent have bitten the bullet and replaced their ERP solution, and of those, their top three reasons were lack of functionality, outdated technology; and the inability to scale with growth of the business.

Making the right decision and consequently, the right selection of an ERP system is generally best done with the advice of an experienced IT systems consultant, who will help you and your management team navigate through a rationalization and needs assessment exercise. A needs assessment should serve as a roadmap for how your firm operates today and how it will operate in the future.

For more information on this topic, visit our website, or read our blog post, "Is Your High Tech Firm Outgrowing Its ERP System and Software?" here.

10 Have internal financial controls to detect and stop fraud

As high tech firms grow and mature, they face an ever increasing array of compliance and enterprise risk issues, from privacy and security concerns to the need for effective internal systems and processes to deter fraud and theft. Growth requires more disciplined controls to deal with problems like embezzlement, shrinkage and other criminal activities.

According to the most recent report by The Association of Certified Fraud Examiners (ACFE) Survey participants estimated that the typical organization loses 5% of its revenues to fraud each year, the median loss caused by the occupational fraud cases was $140,000, and the frauds lasted a median of 18 months before being detected.

Obviously, loses from fraud for a high tech firm looking to make the leap to a growth stage can be a significant threat, particularly as asset protection – particularly cash – is critical. That's why successful firms have internal controls. In fact, the growing awareness of fraud has caused investors and other companies to focus on stronger internal controls at the smaller, private high tech companies, and many firms are finding that banks or other financial institutions want to see stronger evidence of internal controls in the companies that they lend money to.

Your firm needs to take the time to set-up, implement and review a policy of internal controls. Examples of controls include:

- Segregation of duties – related duties should be assigned to different people whenever possible
- Bank reconciliations – receive bank statements unopened and scrutinize for unusual activity
- Safeguard assets, for example, securing blank check stock or restricting access to sensitive records
- Disbursements – review the appropriateness of payments
- Financial statement reviews for accuracy

Your CPA can help you set up internal controls, up internal controls, up to and including sophisticated controls required by regulatory authorizes for publicly traded companies. While you may be keeping an eye on your technology, it's critically important to be vigilant about financial fraud and abuse as well.

For more information on this topic, visit our website, or read our blog post, "Occupational Fraud: Is There a Thief in the Next Office?" here.

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About us

Freed Maxick CPAs, P.C. advises public and private companies on ways to enhance profitability, save taxes, improve accountability and preserve wealth. We specialize in helping our clients discover and achieve their bottom-line potential and we provide sound business advice based upon our vast experience in a broad array of industry groups, including high tech, healthcare, manufacturing & distribution, governmental and not-for-profit.

Among the services we provide to high tech companies looking to make the leap from early to growth stage are:

- Accounting
- Auditing: Financial Statements, Compliance, Employee Benefit Plans, FAR
- Business Process Management Consulting
- Business Valuations
- Compilations and Reviews
- ERP / IT Systems Selection and Review
- Financing and Funding assistance
- Internal Control Strategies and Programs
- Merger and Acquisition Consulting
- Stock Ownership Compensation Planning
- Strategic, Operational and Financial Planning
- Tax Credits, Grants and Incentives
- Tax Planning and Strategies – corporate and individual