Boardroom INSIDER Reprint

The online newsletter for better boards and better directors Ralph Ward, Publisher/Editor

ESOP BOARDS - THE LATEST TRENDS (3/18)

They're a powerful player in Western economies, but too often fly under the radar of media attention, especially when it comes to their governance -- employee stock ownership plan (ESOP) companies. Employee holdings in their companies come in many forms worldwide, and have various drivers (allowing a family to cash out some of its equity… a takeover defense… etc.) The most common model, at least in the U.S., is the private company ESOP. With 7000 such ESOPs in the U.S. (with assets of $1.3 trillion), they are an economic force to be reckoned with -- and all of them need a board of directors. How do ESOP boards function, how are they different, and what best practices should they pursue?:

- First, a few more statistics. The good folks at the National Center for Employee Ownership (***NCEO***) recently released a governance survey of their substantial ESOP membership. While less than 5% of ESOPs in the U.S. are publicly traded (and thus required to meet public company governance rules), the many private ESOPs also take their boardwork seriously. Median board size is 5 members, and 41% of the boards meet 4 times a year. Almost all of the boards include at least one inside director. The U.S. ESOP model mandates a trustee, who is "shareholder" for employee stock held by the ESOP. An institutional trustee (a bank or trust company) is standard (32%), but a single employee trustee (24%) or an employee committee (23%) are also common.
- ESOP boards typically are made up of management employees, and NCEO founder Corey Rosen finds that these insiders tend to take their governance task seriously. "Usually the board meetings run from 3 to 5 hours." The company CEO most often chairs, but an ESOP chair isn't quite the power center found in other boardrooms. "Everything is done by consensus… board meetings are rarely adversarial." But Rosen finds this doesn't mean a board of uninterested pet rocks. These directors "know that they're making important decisions on sales, strategy, and culture," and they come prepared. Also, the legal structure of ESOPs is very specialized, so inside managers better know the ropes.
- The most cited trend for ESOP boards has been the addition of independent directors. With no requirement for private ESOPs to add independents, why do it? Because more ESOPs are also naming outside independent trustees, and "we definitely see these trustees wanting more independent directors on the board," says Ronald Gilbert, president of ESOP Services consultants. While Gilbert says "I can't think of a single trustee who's actually on the board," they increasingly view their role as a shareholder fiduciary requiring objective, skilled voices in the boardroom.
- Who are these new independent ESOP directors? The companies "may want someone from their particular industry," says Rosen. "Financial, strategic, or marketing" savvy is also popular. ESOPs allow more flex in defining "independence," so former company CEOs or other officers are also popular outside picks.
- What's coming in ESOP governance? Tightening fiduciary standards are in turn tightening boardwork, with more professional meeting agendas, better minutes, greater use of board portals and other tools to improve meeting info, and restructuring the board with committees. For the latter, Rosen sees growing interest in a compensation committee to deal with ESOP exec paysetting issues in a more professional way.

RALPH WARD'S BOARDROOM INSIDER is published monthly for directors, CEOs, those who work with corporate and nonprofit boards (corporate secretaries, corporate counsel, support staff, and consultants), and those who are board prospects.
Ralph D. Ward is author of the books *BOARDROOM Q&A*, *THE NEW BOARDROOM LEADERS*, *SAVING THE CORPORATE BOARD*, *IMPROVING THE CORPORATE BOARD* and *21st CENTURY CORPORATE BOARD*, and a speaker on corporate board issues.
Our address is P.O. Box 196, Riverdale, MI USA 48877. Telephone/fax (989) 833-7615. Our website is at www.boardroominsider.com