



## Microcap Board Governance

by Annalisa Barrett  
August 2018



# Webinar

Wednesday, August 22, 2018

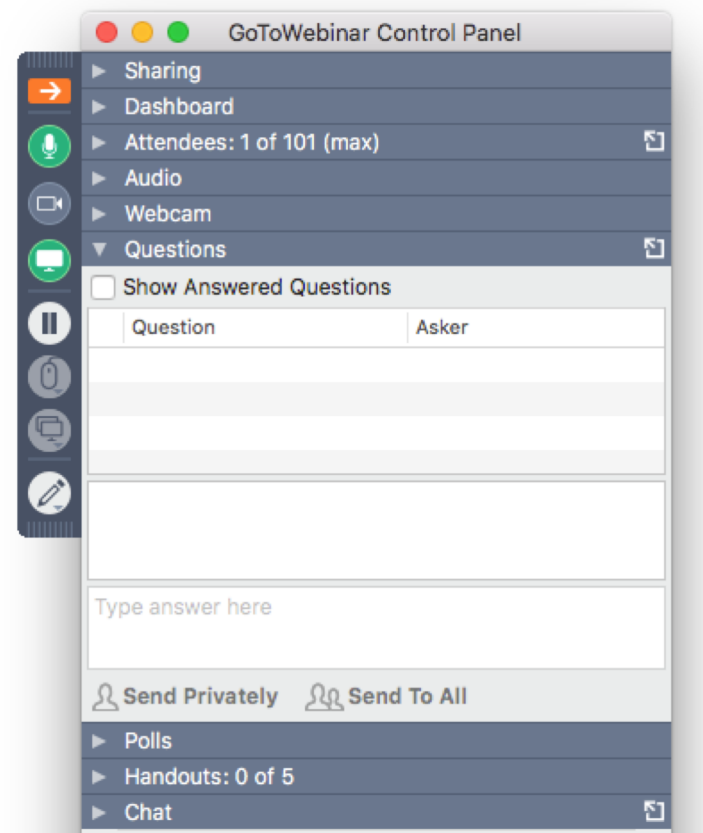
# Agenda

- Introductions
- Research Review
- IRRCi Perspective
- Q&A



# Webinar Logistics

- Attendees in listen only mode.
- Questions encouraged. Type using the “Question” function, answers following report overview.
- Recording webinar, replay will be available.
- Report & replay at [www.irrcinstitute.org](http://www.irrcinstitute.org).
- Share info on social media:  
@irrcresearch and @Annalisa\_BGR
- Audio issues, contact GoToWebinar at 1-800-263-6317.



# Speakers



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## **Jon Lukomnik**

### **Executive Director**

Investor Responsibility Research Center Institute

# Investor Responsibility Research Center Institute

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# The Under-Studied Microcap Company

- Publicly-traded microcap companies out-number larger companies.
- Microcaps do not receive much attention in the corporate governance debate.
  - ✓ Microcaps are not included in the major indices
  - ✓ They have generally not been targeted by large institutional investors for engagement
  - ✓ Many do not have an analyst following
- Therefore, their boards of directors and governance practices have not been the subject of much research.

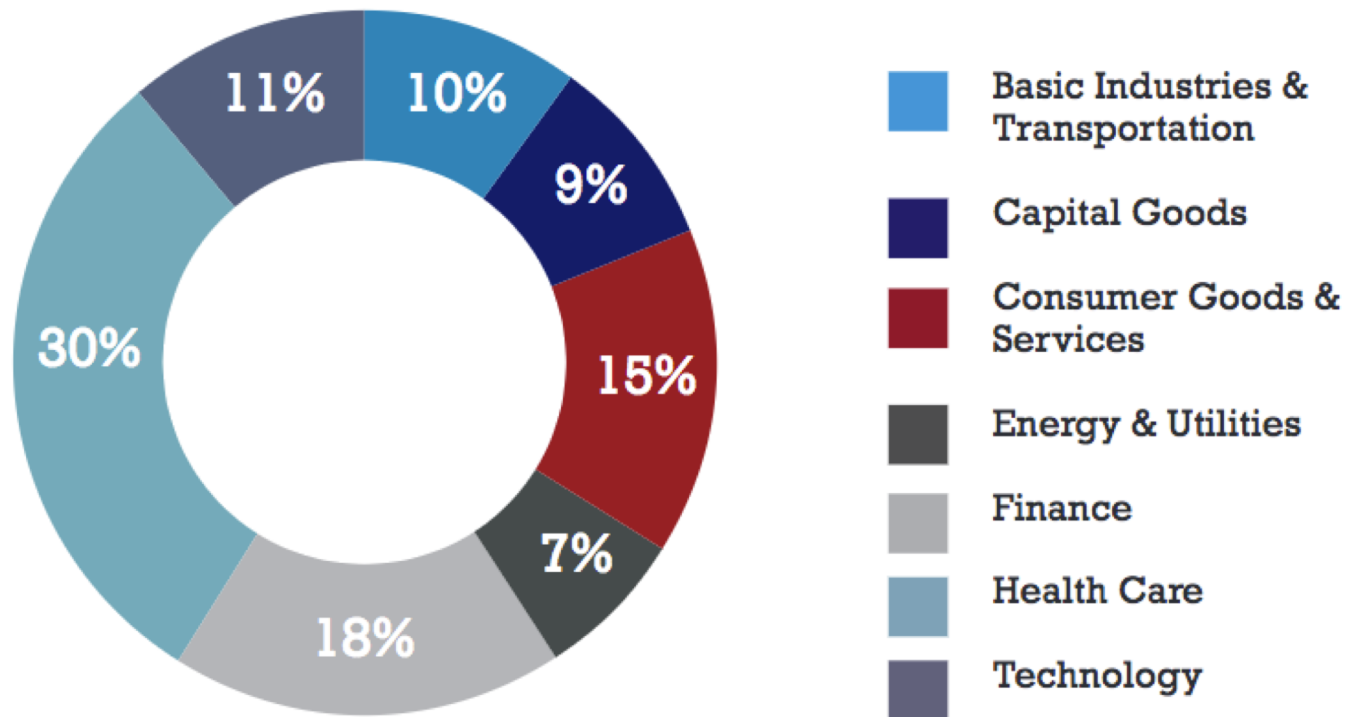
# Study Methodology

- 1,552 publicly-traded companies with market cap less than \$300M which are traded on the NYSE, NYSE American or Nasdaq exchanges were identified.
  - ✓ Note: There are more than 10,000 microcaps traded on the Over-the-Counter markets; however, this study only includes companies traded on major exchanges for purposes of comparing disclosed governance practices to larger companies.
- 160 of these companies were randomly-selected to create a representative list of approximately 10%.
- Most data on the companies, boards, directors and policies were hand-collected by Board Governance Research.
  - ✓ Additional data was secured from Equilar, Inc., MSCI ESG Research, Fund Votes Research Ltd., and Nasdaq.

# Microcap Company Sector

## Sector

Microcap Companies, n=153

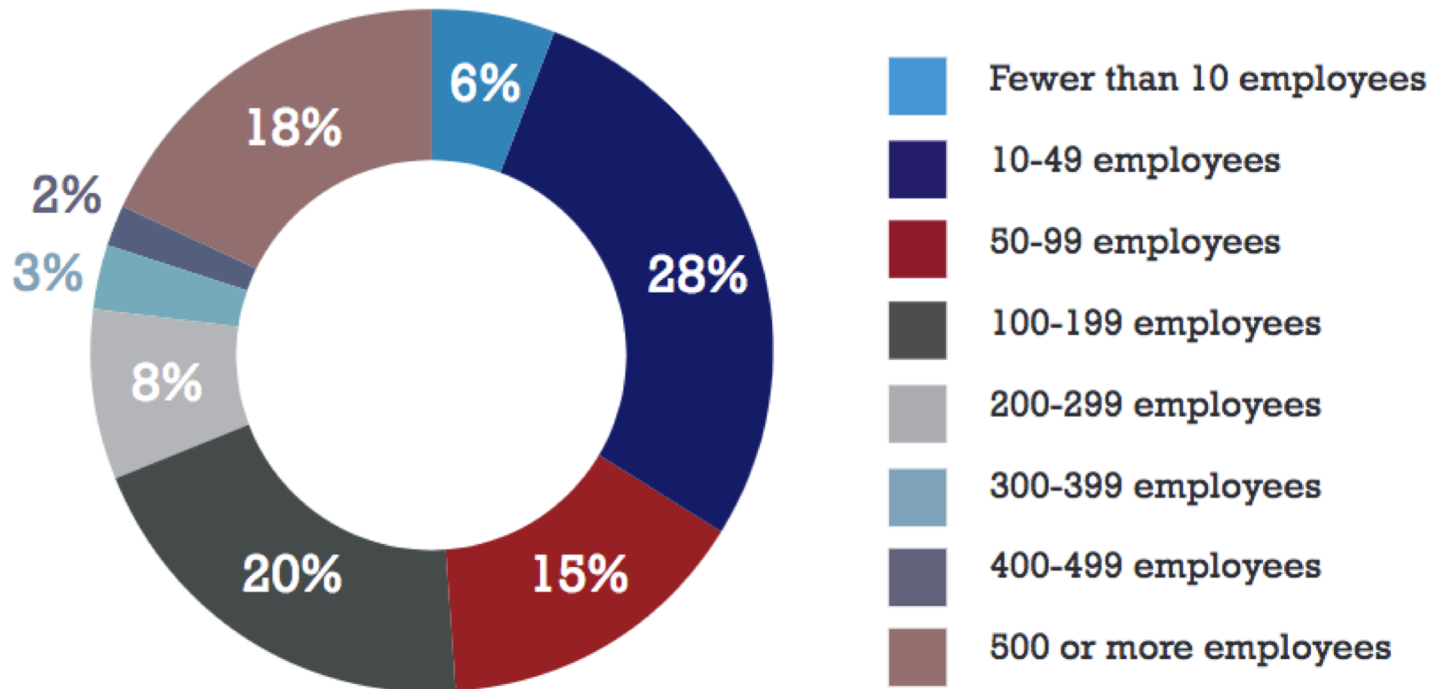




# Number of Microcap Employees

## Number of Employees

Microcap Companies, n=159



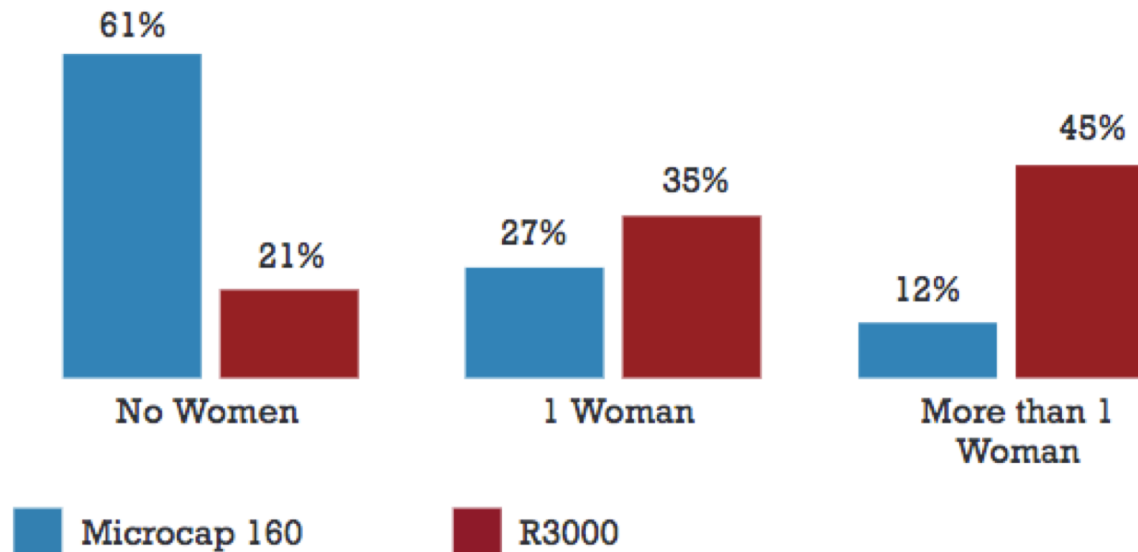
# Busting Misconceptions

- Microcaps are **not**:
  - ✓ Start-ups that have not grown up yet.
    - Only 22% of the microcaps studied went public in the last five years
    - Only 6% were founded in the last five years
  - ✓ Led by their founders.
    - Only 14% of the microcap CEOs studied were the founders of the company
  - ✓ Controlled by a majority shareholder or one who controls the votes.
    - Only 4% have a majority shareholder
    - Only 7% have a multiple-class stock structure

# Microcap Board Gender Diversity

- Microcap boards are much less likely to have female directors.
  - ✓ 61% have no women on the board
  - ✓ Only 12% have more than one female director

## Number of Women on Board

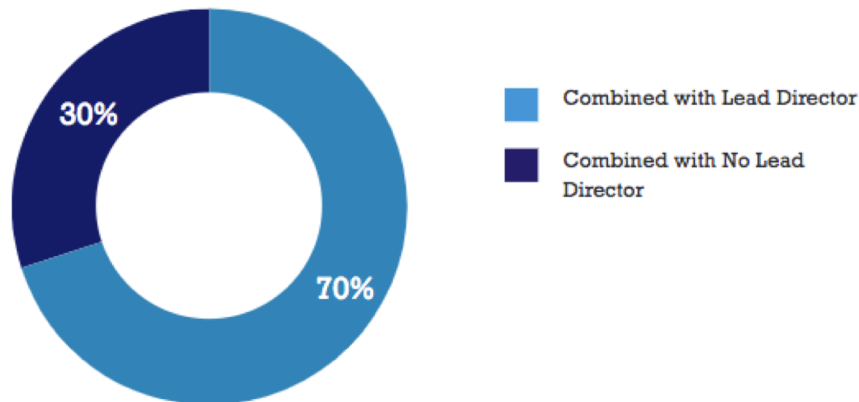


# Microcap Board Leadership Structure

- Microcaps are just as likely as Russell 3000 companies to have split the roles of CEO and Board Chair.
- However, many do not have an independent chair or lead director.

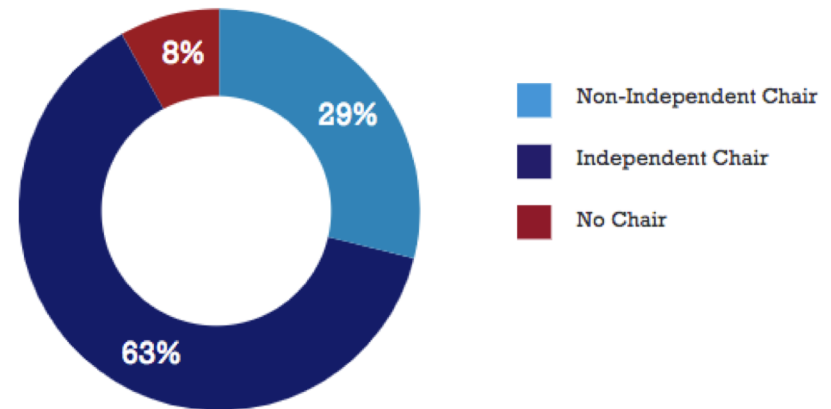
## Prevalence of Lead Director when CEO and Board Chair Roles are Combined

Microcap Companies, n=60



## Independence of Board Chair when CEO and Board Chair are Separate

Microcap Companies, n=100

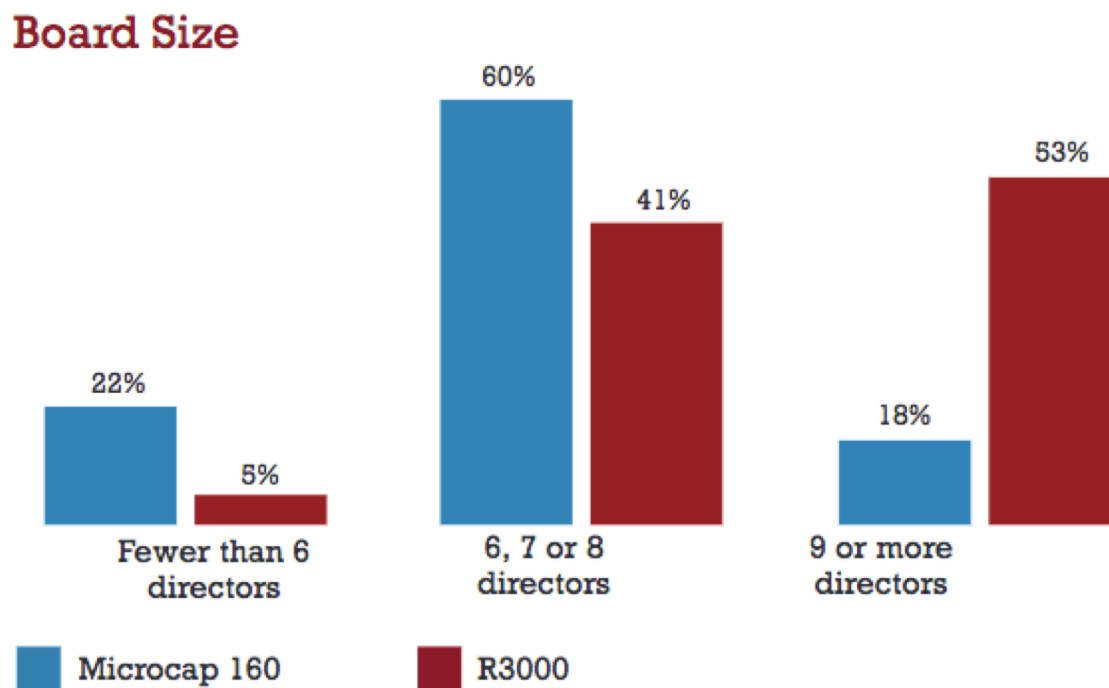


# Microcap Board Leadership Structure

- In fact, many of the microcaps studied stated explicitly that they have chosen to not have a lead director even though the CEO is also the Board Chair.
- The following are examples from 2018 proxy statements:
  - ✓ Biomerica, Inc. (BMRA) *“The Board does not have a lead independent director and does not believe one is necessary. We believe our leadership structure is appropriate for the size and scope of operations of a company of our size.”*
  - ✓ Comstock Holdings Companies, Inc. (CHCI) *“The Board also believes there is a very well-functioning and effective balance between strong Company leadership and appropriate safeguards and oversight by independent directors, although the Company does not have a lead independent director.”*
  - ✓ The Goldfield Corporation (GV) *“In light of the active involvement by all of the Company’s independent directors, the Board of Directors has not named a lead independent director.”*
  - ✓ PrimeEnergy Corporation (PNRG) *“The Directors have also determined that it is not necessary to appoint a lead independent director at this time.”*

# Microcap Board Size

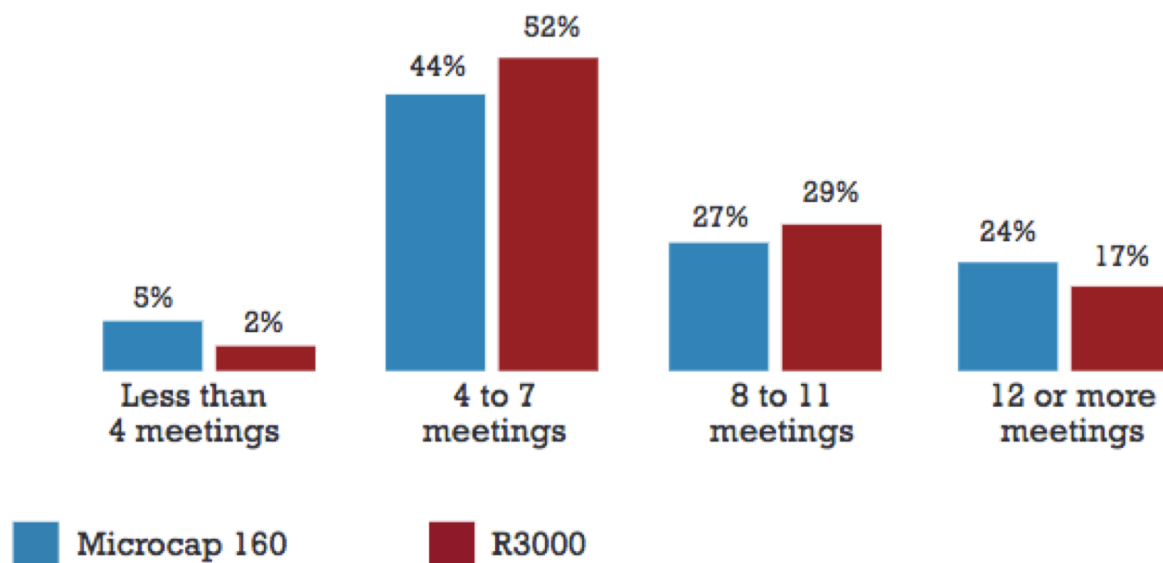
- Microcap boards are smaller than larger company boards.
  - ✓ Nearly one-quarter have fewer than six directors



# Microcap Board Meeting Frequency

- Microcap boards have more variability in number of board meetings held.
  - ✓ Nearly one-quarter held 12 or more meetings in 2016
  - ✓ 5% held fewer than four board meetings in 2016

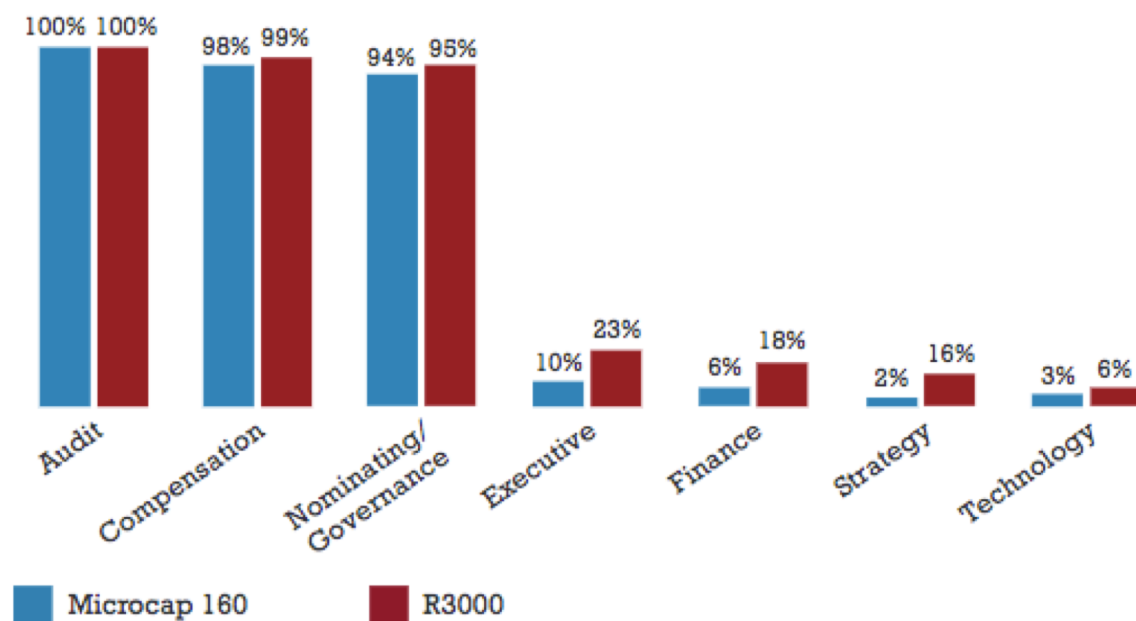
## Number of Board Meetings



# Microcap Board Committee Structure

- Microcap boards have a less complex committee structure.
  - ✓ Less likely to have specialized committees
  - ✓ Possibly due to smaller board size

## Board Committees

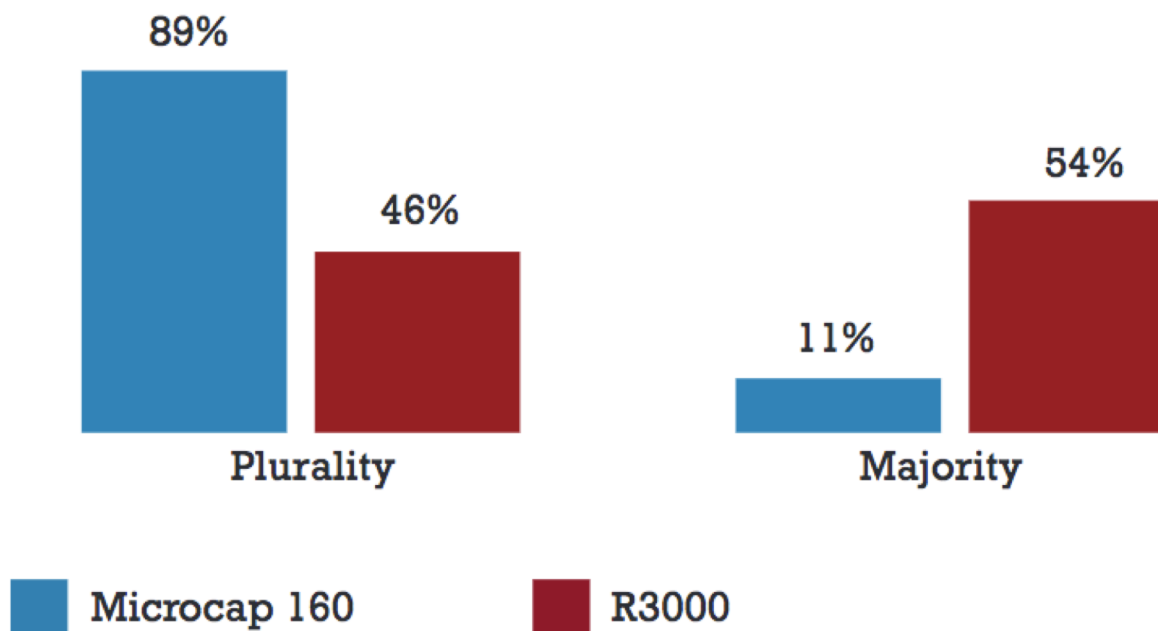




# Microcap Director Elections

- Classified boards are roughly equally prevalent at microcap companies (46%) as at Russell 3000 companies (42%).
- However, director election standards differ greatly.

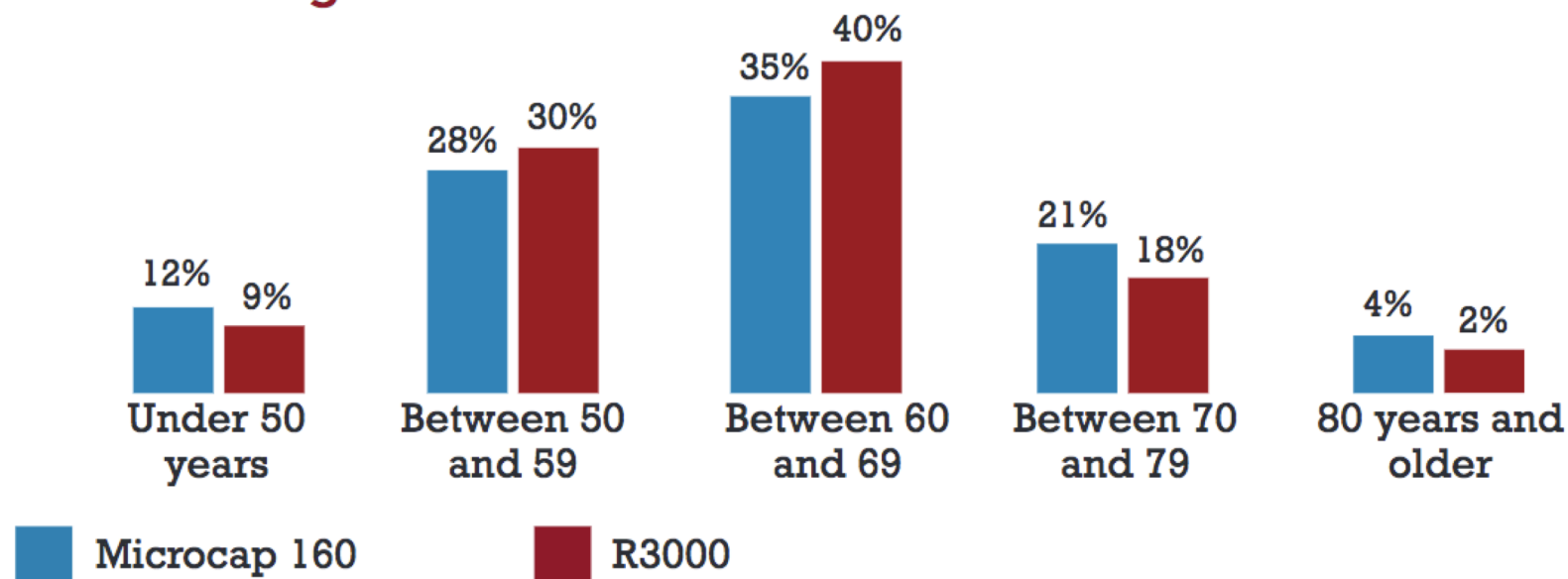
## Director Election Standard



# Microcap Directors

- Microcap directors are more likely to be at the younger and older ends of the age spectrum.
  - ✓ 25% are 70 years or older
  - ✓ 12% are younger than age 50

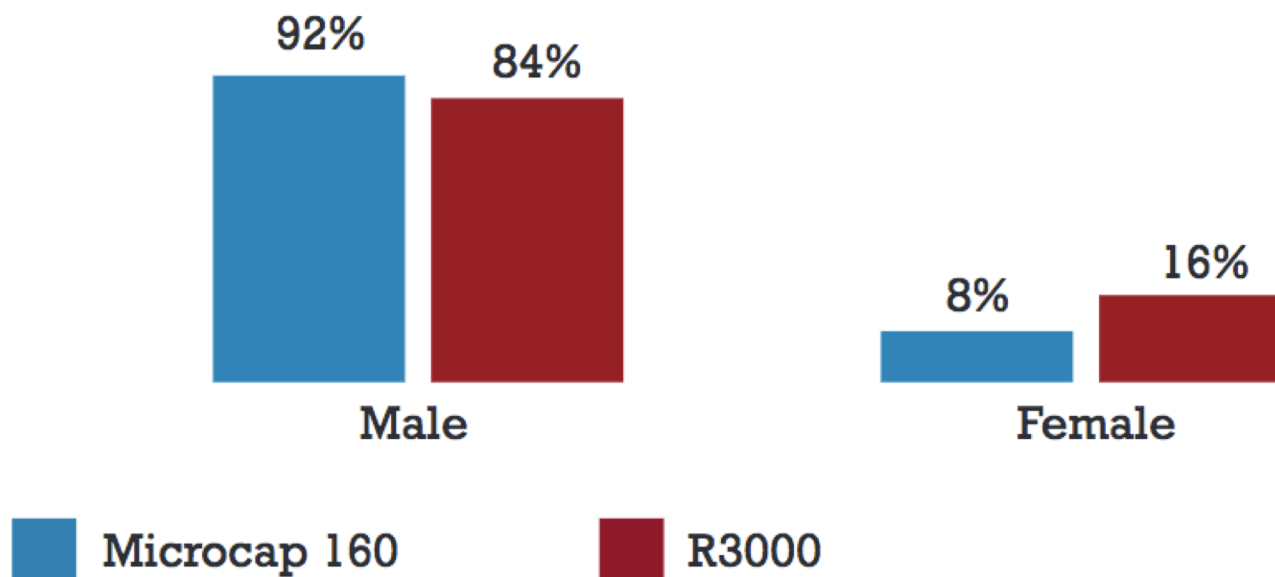
## Director Ages



## Microcap Directors (continued)

- Microcap directors are more likely to be male.
  - ✓ Only 8% of microcap directors studied are female.

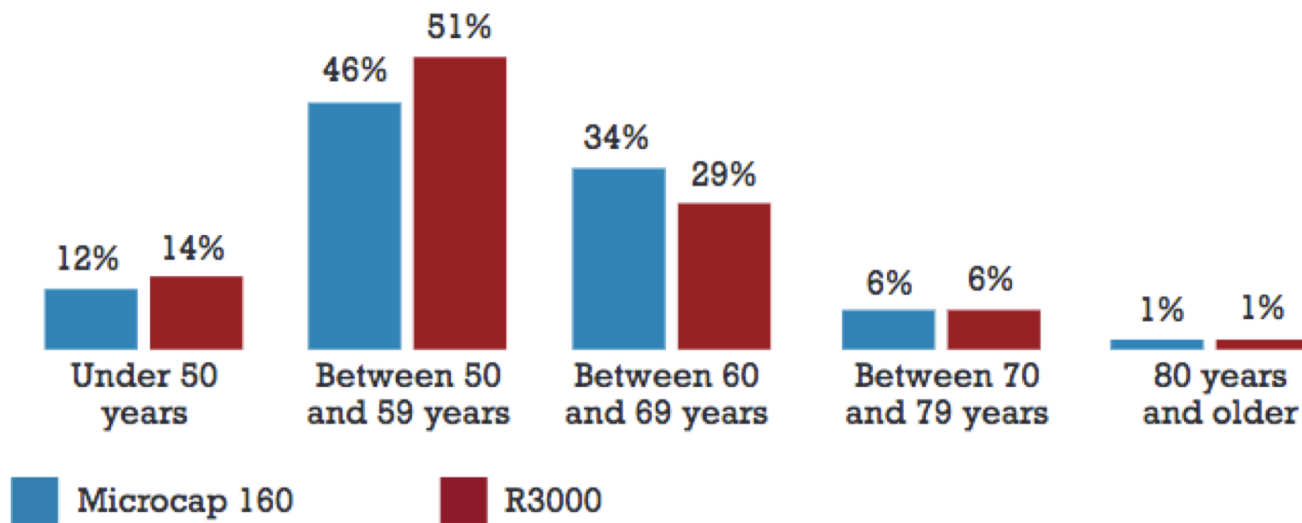
### Director Gender



# Microcap CEOs

- Nearly all (96%) of the CEOs of the microcaps studied are male, similar to the 95% of Russell 3000 CEOs.
- The ages of the microcap CEOs are similar to those of CEOs of Russell 3000 companies.

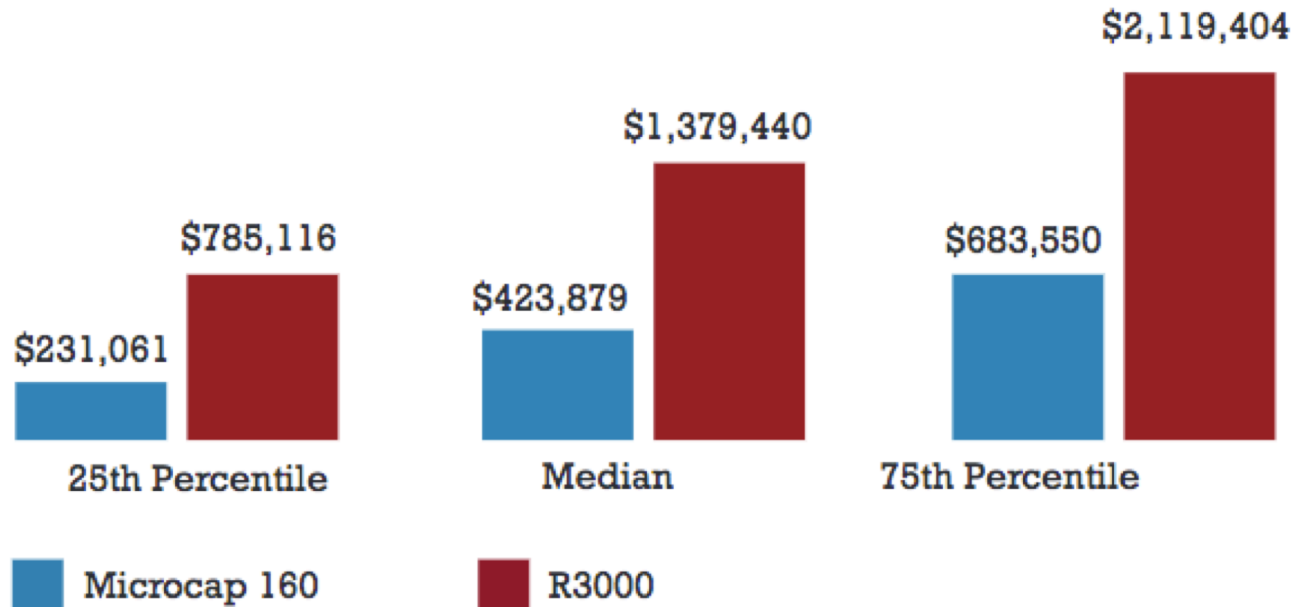
## CEO Ages



# Total Board Compensation

- Microcap companies spend significantly less on board compensation compared to Russell 3000 companies.

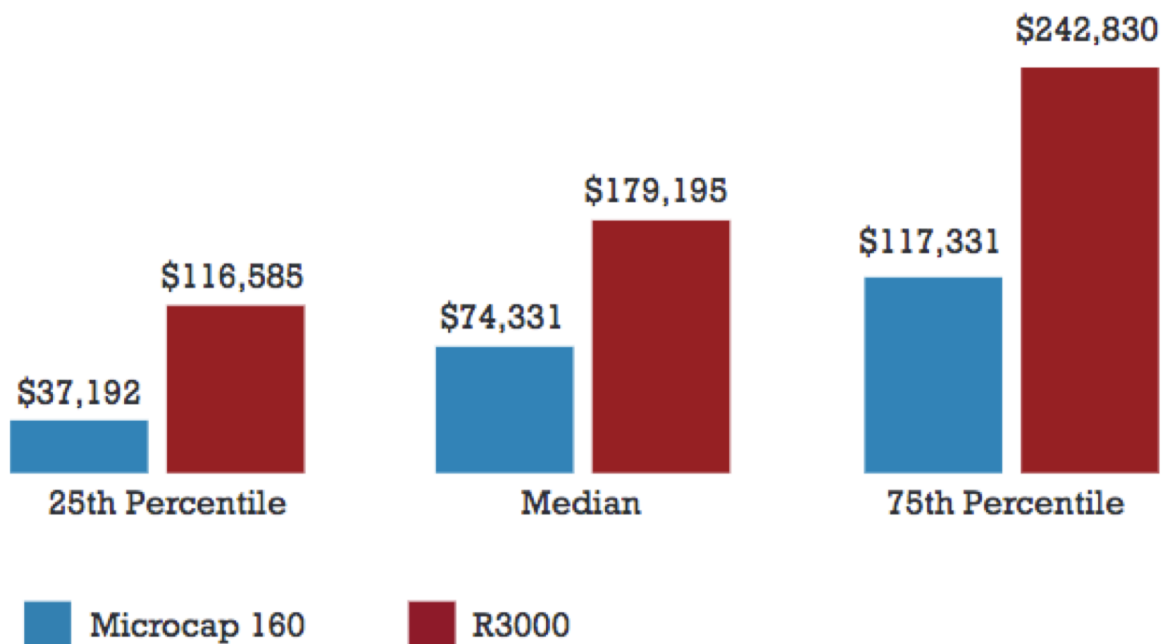
## Total Board Compensation



# Individual Director Compensation

- Similarly, individual microcap directors receive much lower compensation for their board service.

## Average Individual Director Compensation



## From the IRRC Institute Viewpoint

- Important differences between microcap governance and larger public companies.
- Question is: Why?
  - ✓ Something inherent in smaller companies?
  - or
  - ✓ Change just hasn't worked it's way down the capitalization table yet?

# From the IRRC Institute Viewpoint

## ■ Little of both:

### ✓ Smaller size, less complexity plausibly explains

- Simpler committee structure
- Variability in board and committee meeting frequency
- Lower board and individual director compensation

### ✓ Would not seem to explain

- Lack of gender diversity
- Lack of lead independent directors
- Prevalence of plurality voting



# From the IRRC Institute Viewpoint

## **Prediction: Change is coming.**

One size governance fits no one, and microcaps appropriately simplify some governance “standards” to better suit their situation, but...

Governance reforms often work their way down the market capitalization tables.

Microcap practices that are just bad legacies, such as lack of gender diversity and a lack of independent board leadership, will become less prevalent.

# Questions



# Contacts



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