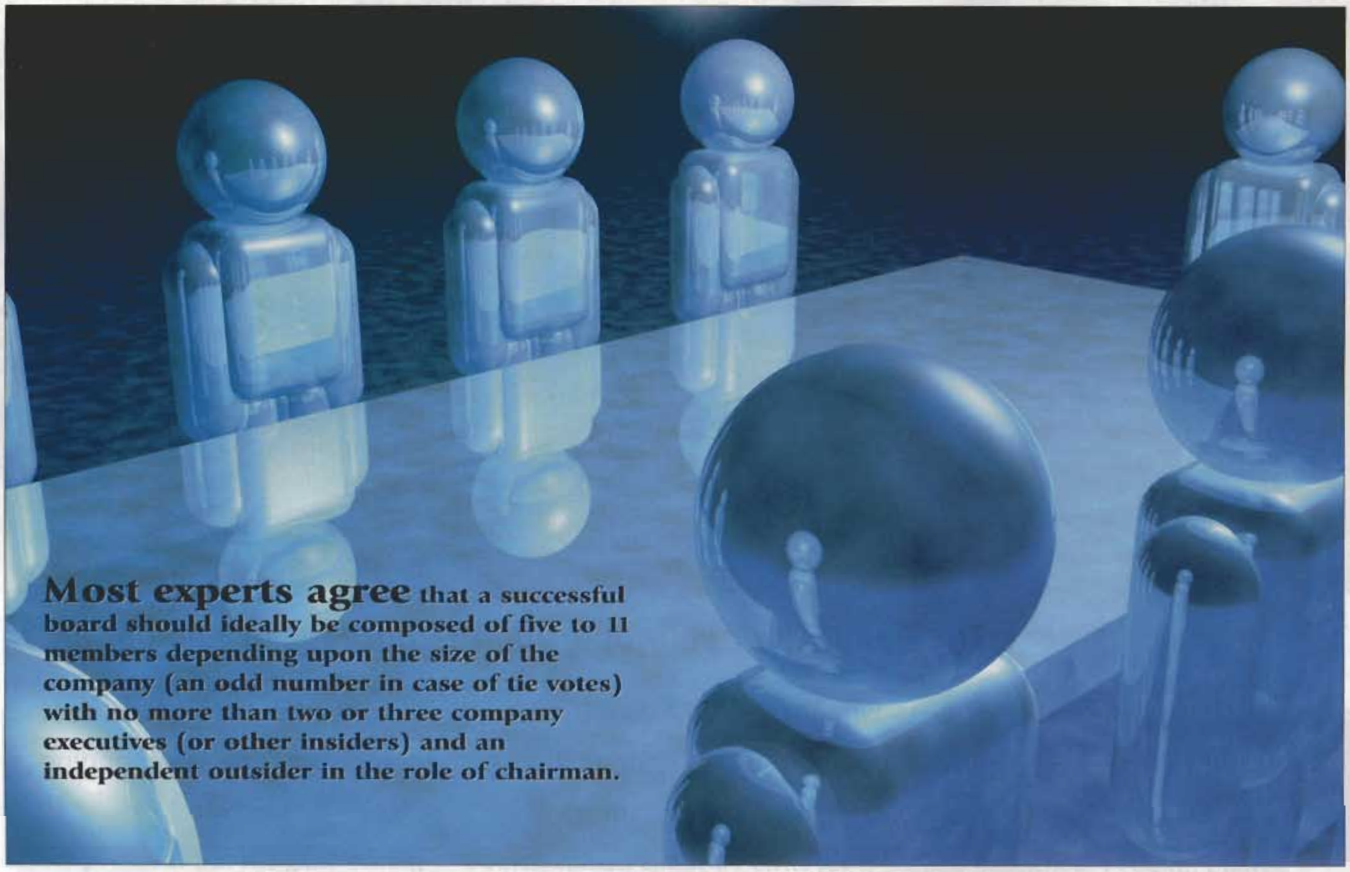
Directing balance

Gaming's best boards in 2005 exercised diversity and discretion in their handling of corporate governance

■ BY KEITH KEFGEN AND STEPHEN GOEBEL, HVS INTERNATIONAL



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Our eighth annual study of best practices in the boardrooms of public gaming companies finds many firms that have responded to public (and regulatory) demand for accountability in corporate governance.

As we do every year, we have analyzed the public documents of 45 public traded gaming companies, and conferred with other experts on corporate governance to rate each company in the following four fundamental areas:

- The size, makeup, and independence of the board
- Committee structure and effectiveness
- The presence of interlocks, insider participation, and related transactions
- Fundamental commitment to pay-for-performance

Last year we modified some of our criteria in response to evolving market conditions. As an example, we now deduct one point from companies that continue to have an executive committee. Executive committees are seen today as a simple way for the CEO/chairman to hijack the board.

We also give an additional point to any company that appoints a lead director and found six firms that had done so, compared to none in last year's study. Appointing a lead director is a highly recommended practice, particularly for companies that do not have an independent chairman.

The following are some general trends we observed:

Sixty percent of the board chairmen were also CEO.

Of the 18 chairmen who were not CEO, 11 were independent outsiders.

More than 85 percent of the >>

2005 GAMING BOARD OF DIRECTORS PERFORMANCE CHART

Company**	Size/Makeup	Committees	Interlocks	Compensation	Total*
GTECH	9	10	10	10	39
Multimedia Games	10	9	10	8	37
Harrah's Entertainment	7	8	10	10	35
Wynn Resorts	4	10	10	9	33
Shuffle Master	2	10	10	10	32
Aztar	4	7	10	10	31
Progressive Gaming-Mikohn	6	6	10	9	31
Trump Entertainment	6	6	10	9	31
Churchill Downs	7	7	10	6	30
Pinnacle Entertainment	5	7	10	8	30
Daktronics	5	7	10	7	29
IGT	3	9	10	7	29
Gaming Partners International	6	5	10	7	28
Global Payment Technologies	7	5	10	6	28
Ameristar Casinos	1	6	10	10	27
Canterbury Park	3	5	10	9	27
Century Casinos	5	5	10	7	27
Scientific Games	8	7	5	7	27
Venture Catalyst	5	6	10	6	27
Boyd Gaming	2	10	5	9	26
Isle of Capri	5	10	5	6	26
Sands Regent	7	8	5	6	26
Dover Downs	3	5	10	7	25
MTR Gaming	2	7	10	6	25
Nevada Gold & Casinos	1	6	10	8	25
Station Casinos	1	7	10	7	25
MGM/Mirage	1	5	10	9	25
Alliance Gaming	6	6	5	7	24
Carnival	3	8	5	8	24
Full House Resorts	5	2	10	7	24
Youbet	2	6	10	6	24
TransAct Technologies, Inc	1	6	10	7	24
Wells-Gardner Electronics	2	6	10	6	24
Cash Systems, Inc.	2	5	10	7	24
Monarch Casino	1	5	10	7	23
Riviera Holdings Corp.	6	6	5	6	23
WMS Industries, Inc.	2	7	5	9	23
Las Vegas Sands Corp.	4	2	10	6	22
Penn National	4	6	5	7	22
Vending Data Corp.	4	5	10	2	21
Trans-Lux	6	4	5	5	20
American Vantage	4	5	5	5	19
Magna Entertainment	3	6	5	5	19
American Wagering	2	2	5	6	15
Archon Corp.	1	3	5	6	15

*Based on total possible score of 40, 10 in each category **Based on public documentation for fiscal year 2003

group has now drafted governance policies, committee charters, and a code of ethics.

Six gaming companies now have appointed a lead director.

Twenty two companies still have three-year terms and separate classes of directors.

Twenty two companies either have no corporate governance committee or it did not hold a meeting.

Fourteen companies allow insider participation or had significant related transactions, almost one-third fewer than the 20 in last year's study.

No public gaming company allows board interlocks.

Only one company does not have a compensation committee, though eight other companies' compensation committees met only once or not at all.

Board size, makeup, and independence

Most experts agree that a successful board should ideally be composed of five to 11 members depending upon the size of the company (an odd number in case of tie votes) with no more than two or three company executives (or other insiders) and an independent outsider in the role of chairman. Many of our top performing boards, including GTECH Holdings Corporation, which is our top performing board for the second consecutive year, lost most of their points in this category *(see chart)*.

Multimedia Games scored 10 of 10 available points, and other perennial top performers would improve on their scores in this category if they consider separating the role of CEO and chairman, and going to a one-year term for directors.

Balance and independence are crucial to board effectiveness. Small boards can be appropriate for smaller companies as we see at Multimedia Games, but in the cases of Canterbury Park, Monarch Casino Resorts, or Venture Catalyst, their five- and six-member boards had too many insiders compared to outsiders.

Like most experts on corporate governance, we believe that on a board of five members, the CEO should be the only company executive who is a director. Larger boards can suffer from the same imbalance however, as in the case at Boyd Gaming, or Carnival Corp. Boyd's 13-

member board is 46 percent insiders, while at Carnival their 15 member board includes six who are company executives or insiders. There is simply no reason for management to have this great a presence on the company's board.

Furthermore many of the independent members of these prestigious boards sit on as many as five or six other boards. We continue to predict that with the greater commitment required to be an effective board member; directors will be forced to reconsider how many boards they can effectively serve.

Committee structure

The four committees that we and other corporate governance experts deem mandatory are audit, compensation, nominating and governance committees. Every company in gaming now has an audit committee, and most have recruited or designated members in the past two years who are qualified financial/accounting experts to satisfy regulatory requirements. Compensation committees are almost as pervasive and only one company in the group had not formed one. This is in comparison to our year 2000 study when only 50 percent of the public companies in gaming had a compensation committee.

However, committees that do not meet will be hard-pressed to be successful and as noted earlier, 20 percent of the industry's compensation committees met just once or failed to meet at all.

The industry has recognized the importance of staffing these essential committees with independent directors as only five companies still have insiders on sub-committees compared to eight a year ago. More than 60 percent of gaming companies combine the nominating and governance committees, but 19 companies still do not have a nominating committee and 22 do not have a governance committee or the committee did not meet.

Though 13 companies still have executive committees, we continue to encourage the disbanding of this committee altogether.

Interlocks, insider participation

The investment community has taken a very harsh view of companies that >>

allow board interlocks (you sit on my board, and I'll sit on yours), as this situation creates biased opinions. To their credit, gaming industry boards have now entirely done away with interlocks.

Many more of gaming boards—31 percent—still allow insider participation and related party transactions, though this is down from 49 percent a year ago.

For example Trans-Lux Corporation paid over $400,000 in fees to a law firm of which one of their directors is president, and engaged a company partially owned by another of their directors to provide consulting services to the company. These relationships are an obstruction to the impartiality of otherwise independent directors and can no longer be tolerated in today's climate of board ethics.

Pay-for-performance

Governance experts agree that management and shareholders must be committed to the same goals. A primary method for aligning the interests of both groups is a commitment to pay-for-performance.

Recent ISS research shows that companies that have a well-conceived pay-for-performance plan almost always out-perform those who do not. Nearly 80 percent of the public companies in gaming have adopted the basic components of a well-designed compensation program which include:

- A well thought out, and articulated compensation philosophy
- Salaries that are set using peer group analysis
- Quantifiable bonus metrics
- Long-term incentives that are performance based and are not excessive
- Benefits and perquisites at appropriate levels

GTECH tops again

This year's best performing board was once again GTECH Holdings Corporation, which had perfect scores in three of the four categories. Other top performers in this years study, Harrah's Entertainment and Shuffle Master, have been top performers in previous years and always show commitment to quality governance. Rounding out the top five are Wynn Resorts and Multimedia Games, Inc.

The consistency of the top performing boards shows that once good governance practices have been put in place, they are self-perpetuating.

Archon Corporation is the only company to repeat in the five-worst performing boards category as this year has seen a number of boards move up in our list by making fundamental changes in their structure.

The main thing that the boards which get the poorest performance ratings have in common is the existence of insider participation and weak or ineffective sub-committee structure. These can be easily re-evaluated and changed for the better and we have already seen many of the gaming industry's boards do in recent years. **CJ**

HVS International is a human resources consulting firm dedicated to the gaming, lodging and restaurant industries. For further information, contact Keith Kefgen, president, at kkefgen@hvsinternational.com, or Stephen Goebel, vice president, at sgoebel@hvsinternational.com.