

TO: ABA Board of Directors

FROM: ABA Governance Committee

April 4, 2006

GOVERNANCE COMMITTEE REPORT FOR FISCAL YEAR 2005

This letter provides a report from the ABA Governance Committee covering fiscal year 2005. The report has three sections:

1. Committee objectives and methodology
2. Committee findings
3. Resulting recommendations

COMMITTEE OBJECTIVES AND METHODOLOGY

The Governance Committee is constituted based on the relevant section of Article VII.1 of the *ABA Bylaws*, which reads:

“The Board shall appoint an Audit Committee constituted of Bookstore Members, none of whom is a member of the Board, but one of whom is a previous Officer, to review annually the Association, Board, and Officers’ practices in accordance with policies and procedures adopted by the Board. The Audit Committee’s term is one year.”

The members of this year’s committee are Mary Gay Shipley (Chair), John Bennett, and Betsy Burton. The committee’s function is described in the ABA’s *Policy Manual*, but briefly it serves as an outside review body on the three issues summarized below where the Board and management may not have arm’s length perspectives:

1. Ensuring that the relationship between the Board and senior management is functioning according to the ABA’s organizational design as laid out in the Bylaws and the *Policy Manual* and that both bodies are otherwise observing their obligations as outlined in these documents
2. Supervising resolution of any issues where the Board or staff has a conflict of interest
3. Providing oversight if there is material question of whether the Board is maintaining fiduciary responsibility

It may be useful to note that it is not the committee’s responsibility to evaluate the Board’s decisions and strategic direction, or management’s execution of the Board’s directives.

In keeping with the decision made in FY 2003 to streamline alternate year committee proceedings, FY 2005 is a ‘full’ year involving a substantial set of in-person interviews. Specifically, this year the committee undertook the following:

1. Structured confidential, in-person interviews based on the ABA Policy Manual and Bylaws with five current Board members, one former Board member, four staff members, and three BAC members:
 - Mitchell Kaplan, President
 - Russ Lawrence, Vice President/Secretary
 - Collette Morgan, Board member
 - Cathy Langer, Board member

- Suzanne Staubach, Board member
 - Chuck Robinson, former Board member
 - Avin Domnitz, Chief Executive Officer
 - Oren Teicher, Chief Operating Officer
 - Eleanor Chang, Chief Financial Officer
 - David Walker, Director of Special Projects
 - Fran Kielty, BAC member
 - Phillip Rafshoon, BAC member
 - Lance Fensterman, BAC member
2. Discussions with the ABA's lead Auditor, Charlene Laniewski, KPMG and LIBRIS lead auditor, Ian Johnson of Grant Thornton.
 3. Review to ensure that the financial Auditors' opinion letters for fiscal year 2005 give an opinion with no qualifications

A copy of the structured interview guide, along with a summary of the interview results, is attached as Appendix A.

COMMITTEE FINDINGS

Upon review of the above sources, the committee found that the several year trend of steady improvements in governance ratings continues although the rate of improvement is leveling off as the policies and practices near maximum ratings. Overall, the result is that the ABA's governance mechanisms appear to be working very well.

The committee noted that in general, satisfaction with governance performance continued high among both the Board and staff. In addition, although several issues had been raised by the Board in response to specific member concerns, the committee found that these issues can be addressed with modest *Policy Manual* adjustments as described in the recommendations section.

No questions received significantly lower ratings than in past years, and several elements of ABA's larger governance scheme seem to have achieved new highs in effectiveness over the past year. These include the following:

- Several respondents remarked on how overall governance of the Board and ABA is reaching the practical limit of effectiveness, although everyone agrees that there is always room for finely adjusted improvements
- Similarly, for the second year, the committee asked respondents to rate the two-year trend for each item. Ratings were quite similar to the previous year, with no "down" trend ratings reported, flat-rated trends were already highly scored, and questions that saw a deceleration in their upward trend had reached new highs
- Through significant improvements in monitoring future trends, many respondents noted and scored highly how the Board has improved its ability to initiate policy - particularly through the use of extended bodies such as the BAC - rather than simply reacting to staff initiatives,

- Most of the ‘ten questions’ that were reviewed at the Board’s request were deemed not to have associated governance issues. A fairly representative example was the review of the process used in the sale of the Tarrytown property. Close questioning by the committee resulted in a clear conclusion that: a) a thorough and logical process was followed; and b) it is not appropriate to make that process into an ABA policy since the occasion to use such a policy would be so rare
- No conflicts of interest were cited
- The only issue of potential materiality mentioned was the increasing liability built up by the gift card program, but all interviewees felt that the Board and staff are applying prudent business judgment to monitor and manage this issue

With that said, the committee noted several areas where issues were raised. Each finding is described in more detail below.

- Interviewees believed that the membership is interested in formalization of the increased transparency and public disclosure from the ABA Board regarding ABA financial information
- Several interviewees commented that the language in the Policy Manual that implies that the Board should initiate policy rather than relying on staff may not match perfectly with the institutional mechanisms that have evolved as the ABA’s governance process has matured. Specifically, the language does not seem to take into account the important role that ‘extensions’ of the Board such as the BAC and forums play in establishing new policy ideas
- Interviewees believed that the membership is interested in formalization of the careful – but somewhat *ad hoc* – processes followed by the Board in establishing the CEO contract and salary
- In addition, several interviewees recommended that heightened transparency be considered with regard to the results of the Board’s contractual negotiations with future CEOs
- Concern was raised by several interviewees that an association member can unreasonably dominate Board member and staff time unless it is formally understood that the President can politely terminate responses to redundant inquiries after due process has been followed
- Several interviewees mentioned that declining membership is an important issues for the Board to address and that in particular, the definition of ‘core’ membership is a specific limiting factor
- Although interviewees noted continued improvements in monitoring future trends, the idea was raised of capitalizing on younger booksellers with the expectation of long association with bookselling to help in determining how to respond to trends in readership and the future conditions of bookselling that are greater than five years out
- Board members reiterated their desire to be updated on current issues between Board meetings. One idea was that the current regularly-scheduled calls between the CEO and the Board President should be followed by brief emails from the President to fellow Board members providing a short overview of current issues

- It was noted that the gift card liability is approaching materiality due to its success in a way that may not have been fully anticipated when the gift card program was originally approved
- Governance committee members would like to have the *Policy Manual* (and ultimately the Bylaws) changed to accurately reflect the purpose and term of the committee
- Finally, although the Governance Committee found that meeting with several BAC members was extremely helpful given the importance of the BAC in the governance process, the current practice of using the governance survey for all interviewees proved to be relatively inefficient with interviewees who are unable to answer the majority of the questions due to lack of context

RESULTING RECOMMENDATIONS

Based on these findings, the committee would like to submit the following recommendations for Board discussion and review:

1. Amend pertinent sections of the *Policy Manual* to formally require the ABA to post three years of financials on bookweb.org in a highly visible location, or with a highly visible link.

Recommendation accepted with implementation to begin immediately.

2. Amend the language in the *Policy Manual* that suggests that “the Board should initiate policy rather than reacting to staff initiatives” with the following language: “the Board in conjunction with the bodies established to provide membership input (such as the BAC and various forums), should play an active role in the development of policy in conjunction with staff”

Recommendation accepted with implementation to begin immediately.

3. Amend pertinent sections of the *Policy Manual* to formalize the CEO contract and salary negotiation process using the steps established informally in the previous three rounds of negotiations including, but not limited to:
 - a. Establishing a Board negotiation committee
 - b. Using independent, third-party analysis of benchmark executive total compensation in non-profit associations that are similar to the ABA
 - c. Instituting a Board vote to finalize the contract
 - d. Announcing to the membership in *BTW* that a CEO has been hired and for what term

Recommendation accepted with implementation to begin immediately.

4. Consider posting the newly formalized policy in *BTW* and elsewhere, and when the next CEO contract is written, consider posting the results of the contract negotiations at the close of the process.

Recommendation accepted with implementation to begin immediately.

5. Discuss a potential policy for how to handle repeated ABA member inquiries that have reached an unproductive level from a staff and Board standpoint and have been dealt with thoroughly. The idea was raised to give the Board President formal discretion to end further communications in such a situation.

The Board recognizes the possibility of a member's individual inquiries reaching a point where any further discussion would be non-productive. It is important to reemphasize that the Board and staff of the ABA believes that all members should be treated with respect and courtesy while acknowledging that there are situations when parties need to "agree to disagree" on a given issue. The Board further feels that there is no specific written policy required to deal with these situations as the ability to disengage is implicate in the President's role as chief spokesperson for the organization.

6. Review the definition of a "core" member as a means to stem declining membership.

The recommendation is accepted with the further comment that the Strategic Planning Committee and the Board review this definition each year when going through the strategic planning process. In preparation for the new five year plan (10-1-07), the Booksellers Advisory Council will be asked to weigh in on the issue of who is a core member of ABA.

7. Establish, as an experiment, an *ad hoc* 'council' to work on long-term trends that consists of booksellers who are committed to being in the business for at least 10 to 15 years. These booksellers would be joined by a staff representative, and a Board representative, to meet twice a year and report to the board on long-term issues facing the bookselling industry and recommended actions to be considered. This council should have the ability to invite knowledgeable outsiders to participate in its deliberations as appropriate.

The spirit of this recommendation is accepted and the Board will act on it with all due speed. The Board has recognized, and the Governance Review Committee has pointed out, that the issue of longer-term environmental scanning remains an issue for ABA. The proposal for an "ad hoc" council to engage in the process is a good one,

however the Board feels that the council should be comprised of some balance between “emerging” booksellers and some more seasoned participants. The Board will be discussing this proposal in some detail at the September,2006 Board meeting.

8. Request that the President keep other Board members briefly updated on current topics (for example, with brief emails at least once each month) after the weekly call with the CEO.

Recommendation accepted with implementation to begin immediately.

9. Require financial analysis that includes a ten-year worst case for programs and actions submitted for Board approval that could reach ‘material’ status (e.g., the gift card program).

Recommendation accepted with implementation to begin immediately and a report to be presented no later than the September, 2006 Board meeting.

10. Amend the ABA *Policy Manual* to update the section describing the Governance Review Committee and how it conducts its process as follows:

The Board shall appoint a Governance Committee constituted of three Bookstore Members, none of whom is a member of the Board, but one of whom is a previous Officer (**member of the Board**), to review annually the Association, Board and Officers' practices with respect to whether the relationship between the Board and senior management is functioning according to these Bylaws and any other policies and procedures adopted by the Board. The Governance Committee shall also supervise resolution of any issues where the Board or the Association staff has a conflict of interest. The Governance Committee shall also provide oversight if there is a material question as to whether the board is carrying out its fiduciary responsibility. However, such oversight shall be undertaken only in the event there is no reasonable doubt that the Board has failed to carry out its fiduciary responsibility. The Governance Committee may in its sole discretion elect in the year following a full Committee review to have the review undertaken only by the Chairman of the Governance Committee. The members of the Governance Committee shall serve for a two year term provided that the Chairman of the Committee shall be in the second year of his or her term and shall then continue for a third year on the Committee to maintain continuity.

Recommendation accepted with implementation to begin immediately.

11. Create a separate interview guide for Governance Committee interviewees (such as BAC members) who are not intimate with the details of ABA governance but can provide valuable input on governance-related issues.

Recommendation accepted with implementation to begin immediately.

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In closing, the committee would like to note the cooperation of all involved as well as numerous comments that the ABA's commitment to putting such a procedure in place is testimony to its continued commitment to transparency and good governance. Please feel free to contact any committee member if questions arise.

APPENDIX A - ABA GOVERNANCE SURVEY RESULTS

FY 2005

Please respond to the following questions regarding governance issues during ABA's fiscal year 2005 (11/04-10/05) and discuss your responses in an in-person interview in Long Beach.

Many of the questions ask you to rate a statement on a 7 point scale where 7 is high. The questions also ask you to describe the trend over the past two years with regard to the question's subject using U (up); D (down); or F (flat). If you do not have an opinion on any question, please enter "NA". Feel free to add comments at the end of this survey. Thank you in advance for your help.

Questions on the Board/Management Relationship and Obligations

As you know, the ABA's Policy Manual outlines Governance Process Policies in section two. The following questions relate to those expectations.

1. On a seven point scale (7 is high), how well is the Board currently accomplishing the following [1st box]? What best describes the trend over the past two years: up (U, 1), down (D, -1), or flat (F, 0) [2nd box]?

	Current	2-year trend
a. Initiating policy rather than reacting to staff initiatives?	5.7	0.9
b. Monitoring future trends?	5.7	0.9
c. Defining desired long-term outcomes rather than programmatic means of attaining those outcomes?	5.9	0.8
d. Maintaining internal discipline on matters such as attendance, preparation, and communications?	6.3	0.2
e. Self-monitoring by discussing board process and performance relative to the expectations in the Bylaws and <i>Policy Manual</i> ?	6.3	0.8
f. Producing written policies on what programs, services, and products should be made available, to whom, and at what cost?	6.3	0.7
g. Establishing prudent ethical guidelines for the ABA and constraints on executive authority?	6.5	0.5
h. Assuring that the performance of the Executive Director is consistent with the Board's desires and expectations?	6.8	0.8
i. Revising as appropriate the ABA's end policies and strategic plan within the last year?	6.4	0.7

j. Reviewing the Executive Director’s performance as outlined in the <i>Policy Manual</i> during the month of July?	6.6	0.7
k. Deliberating in a manner that is fair, open, and thorough, but also timely, orderly, and to the point?	6.8	0.7
l. Using the chairperson as a two-way communication conduit with the Executive Director?	6.3	0.6
m. Avoiding exercise of individual authority except when explicitly board-authorized?	6.9	0.5
n. Directing only the CEO regarding operational achievement and conduct, rather than any other members of management?	6.7	0.6
2. On a seven point scale (7 is high), how well is the CEO accomplishing the following [1 st box]? What best describes the trend over the past two years: up (U,1), down (D,-1), or flat (F,0) [2 nd box]? Feel free to add comments as well:		
	2-year Current trend	
a. Making available to the Board sufficient information and staff work to support their obligation to make strategy and policy?	6.7	0.6
b. Working effectively with the Board as an interface between the Board and the ABA’s staff?	6.7	0.6
c. Causing the staff to effectively respond to issues of importance to the Board and the membership?	6.7	0.6
d. Working within the boundaries of any <i>executive limitations policies</i> (as defined in the <i>Policy Manual</i>) established by the Board?	6.7	0.5

Questions on Conflict of Interest

The ABA’s Policy Manual defines policies regarding Board conflicts of interest in section 2.VI and in section 5. The following questions reflect those policies.

1. Has there been any self-dealing or any conduct of private business or personal services between any Board member and the ABA except as procedurally controlled? (Y;1/N;0)	0
2. Have Board members failed to absent themselves as appropriate if any unavoidable conflict of interest arises? (Y;1/N;0)	0

3. Has any Board member used their position to obtain employment for themselves, family members, or close associates? (Y;1/N;0) 0
4. Has any Board member failed to annually disclose their involvement with other organizations, with vendors, or any other associations that might produce a conflict of interest? (Y;0/N;0) 0
5. If the answer to any of the above is yes, please provide details.

Questions on Fiduciary Responsibility

Fiduciary responsibility requires that Board members live up to high standards with regard to their responsibilities to the organization. Examples include avoiding conflicts of interest, applying due care, candor, and confidentiality as appropriate, and applying prudent business judgment, particularly to matters of great materiality. Because the other elements of fiduciary responsibility are covered in earlier questions, this section concentrates on the last of these obligations.

1. Is there any activity or matter that the Board has endorsed that is currently underway or is anticipated that is of great materiality – that is, could threaten the long-term success or existence of the ABA?

The Gift Card liability

0.4
2. If the answer to question one is yes, has the Board applied prudent business judgment and otherwise fulfilled their obligations to the membership as Directors under the Bylaws and Policies of the ABA? (Y;1/N;0) 1.0

Questions Raised by the Board for Review

On a seven point scale (seven is high), how successful has the ABA been in addressing the following?

1. Board responses to ABA member inquiries? 5.4
2. The organization's adherence to governing documents? 6.5
3. Making financial information available to the membership? 5.8
4. The Board's decision making during the sale of the ABA's property in Tarrytown? 6.5
5. Board procedures for the renewal of the CEO's contract? 6.3

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| 6. Board procedures for arriving at, and negotiating executive salaries? | 6.2 |
| 7. Supporting an open environment for Board deliberations? | 6.6 |
| 8. Board procedures for relations with the financial auditor? | 6.6 |
| 9. The organization's efforts to grow membership? | 5.1 |
| 10. Ensuring a thorough governance review process, and following up on Governance Review Committee recommendations? | 6.8 |

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Thank you for your participation. If there are there any topics that you feel that we should have covered that we have not had a chance to speak about, or if you have further comments on any topics covered in the questionnaire, please attach an additional page.

Please provide your name and contact information. All individual responses will be kept confidential within the Governance Committee.

Your name: _____

Your phone number: _____

Your email address: _____

January 3, 2006