

Davey Tree Stands Tall with Employee Ownership

Karen Thomas

Over 25 years, The Davey Tree Expert Company's employee owners built a good small company into one of the premier companies in its industry, with an entrepreneurial zest for new products and acquisitions. The company's development would have pleased its inventive founder and probably surprised the family members who sold it to hesitant employees in 1979.

"The lifeblood of Davey are the field managers and employees, and broad employee ownership is the glue that binds us together," explained CEO Doug Cowan. "Each of our field managers is a true entrepreneur who sells the work, hires the people, and makes sure the job gets done. The majority of our 113 original stock investors back in 1979 were the District Managers."

Headquartered in Kent, Davey is the largest 100% employee-owned firm in Ohio and the 16th largest in the U.S. Since the ESOP was established, the number of employees has almost doubled from 2,800 to 5,100, the number of employee-shareholders has increased six to seven fold from 438 in 1979 to over 3,000 today. Revenues have grown from \$60 million to \$346 million, per share price has grown from \$0.47 to \$15.70 and shareholders' equity has grown from \$9 million to \$62 million.

"We like the idea of broad employee ownership," said Cowan, "It fits our entrepreneurial culture and fosters a common interest across our locations in the U.S. and Canada."

A Frustrating Journey from Idea to Reality

But it wasn't easy to establish employee ownership at Davey. The buyout occurred after a frustrating 18-month process that began on November 1, 1977, when the Davey family announced their intention to sell the company. The idea of employee ownership was initiated by former president Jack Joy, former executive vice president Jim Pohl, and then-controller Cowan, who quickly formed an Employee Ownership Committee. They found widespread support for the idea of employee ownership and two weeks later made a formal purchase offer.

Employee ownership was attractive to the family because the motivation and commitment of employees is key to the company's locally-based services. They encouraged the Employee Committee to continue to explore financing. The employees made a second offer in May of 1978, but the funding for their business plan was tight.

"Direct employee stock ownership by all the employees was our vision, so the ESOP was not part of our planning," explained Cowan. But an ESOP was included in their third purchase offer two months later. This offer coincided with offers from two other groups which brought the employees' buyout negotiations to a standstill.

Finally, amid growing frustration and uncertainty about the future, the Board approved the Committee's fourth purchase offer. It took seven more months to finalize financing and get approval from the Securities and Exchange Commission. On March 15, 1979, controlling ownership was transferred to the employees. After the buyout, the family owned 21% of the shares, retirees owned 11%, and employees owned 68%. One major family shareholder held shares under a buy-sell agreement for a future transaction.

Then came the first disappointment. "We wanted everyone to buy stock through the subscription plan, but only 113 employees did," recalled Cowan. "We were disappointed. Yet all

438 eligible employees were enrolled as participants in the ESOP the next day."

Despite a reluctance to become direct shareholders, employees have enjoyed the rewards of ownership ever since. In their first year as owners, sales rose 15%; earnings from operating income rose by 79.3%; and equity increased 30%.

Father of Tree Surgery Finds a Tree Care Industry

"John Davey, the company's founder, would have liked employee ownership because he was a common, hard-working guy," said Cowan. Davey grew up in rural England, apprenticed in horticulture, and arrived in Kent to seek his fortune as groundskeeper at the local cemetery. By 1880 he was recognized locally for his methods of tree surgery, his writings and lectures on tree care, and his plantings. He incorporated The Davey Tree Expert Company in 1909 (at the age of 63) and established a school of tree science.

Davey gained national recognition for tree preservation through his wealthy customers, most notably the Rockefellers, who continued to recommend Davey tree care services when they moved from northern Ohio to New York. Davey's son, Martin, set up sales/service territories nationwide, staffed by enterprising managers trained in Davey's school. Martin had a knack for sales promotion and won contracts to maintain trees at the White House and around Washington D.C. He later became active in Ohio politics, serving as Governor from 1935-1939.

While tree care is the core of Davey's residential services, the company has branched out into vegetation management, utility line-clearing, big tree moving, nursery operations, golf and sports turf maintenance, and specialized research, planning, and education projects. Davey also sponsors The National Register of Big Trees and Global ReLeaf.

The Power of the Davey Culture

Education and training is a big part of Davey's culture, as it has been for the past century. Davey is the only company in the industry that provides such extensive training in tree care, especially distance learning. There are currently 600 online students. Most managers have studied at the Davey Institute of Tree Science which runs a program during the winter.

"We are seen as an employee-friendly company," said Karl Warnke, Davey President & COO, "and this helps our acquisition strategy. Most of the companies in our industry are local 'mom and pops' who know we will provide a safe haven for their employees. Some selling owners got their start with us years ago and won't sell their business to anyone else!"

A Profile of Employee Share Ownership

"If an employee is here a couple of years, they start to take an interest in buying our stock," said David Adante, Davey's CFO. Davey offers four types of employee stock ownership.

Stock Subscription Program. The stock subscription program is the company's attempt to get each generation of young managers to make a commitment to Davey. Employees can buy shares with 10% down and a note over a 7-year payoff period.

Over the past 25 years, three subscription programs have been offered—one per decade. The first was part of the employee buyout in 1979. The second offering was in 1989, and 144 signed up.

The third was in 2002, and more than 350 subscribers purchased over \$10 million in Davey stock.

First an ESOP, now a 401KSOP. The ESOP was started in 1979 because of the financing advantages. "We set up a slow release of ESOP stock through refinancing and paying the loan over a longer period because we wanted to allocate a smaller percentage of ESOP stock each year and include new employees joining Davey," Adante said. "We finally paid off our original ESOP loan in 1996."

In 1997 the company setup a 401KSOP, which incorporated the ESOP accounts, as the primary employee ownership/retirement benefit program. Employees put their own money in and their contribution is matched with Davey stock at 50 cents on the dollar. Over 2,900 employees participate and, as of December 31, 2003, own approximately 2.77 million shares or 32% of the company."

"The ESOP represented 48% of employee stock ownership in the beginning. But we prefer to see more shares owned directly," commented Cowan and Adante.

Stock Purchase Plan. The stock purchase plan was started in 1982 as an affordable means to get all Davey employees involved as shareholders. "This strategy has succeeded," explained Adante,

"we have averaged about 1000 employees per year participation. We offer two enrollment periods a year when employees can buy stock at a 15% discount." In 2003, 900 employees purchased 83,061 shares.

Stock Options. Stock options are periodically granted to company managers in both the U. S. and Canada. "Our Canadian employees can't participate in the 401KSOP," explained Adante, "so they are offered some stock options which are not given to the US managers; and they can participate in our stock subscription and stock purchase plans."

Run Like a Public Company

"We run the company as if we were a public company," explained Cowan, "While our 20 officers and directors own 25% of the shares, they do not own a controlling interest, and no one owns more than 5%. While employees are owners, they have no more rights than they would as shareholders in a public company."

The employees who own shares directly vote their shares as investors would in a public company, to elect directors and for shareholder proposals. Over the years, about 80% of the employee shareholders on average have voted their shares either in person or

by proxy. More than 100 employees and retirees attended the 2004 Annual Shareholders Meeting. The employee participants in the 401KSOP also vote the stock in their accounts through a directed trustee who votes the unallocated shares on a proportional basis.

The composition of Davey's Board of Directors is similar to a public company, with a majority of outside directors. The two inside directors are Cowan and Warnke. Davey's outside directors bring a mix of talents; and all are selected because they are people focused.

Stock Repurchase Obligation

"We redeem \$5-8 million in shares per year," said Adante. "About 20% of our total cash flow goes for stock repurchases, including ESOP distributions which are around \$1-1.5 million per year. Our future stock repurchase liability now is about \$150 million."

"To manage repurchase liability, stockholders can only sell so many shares for cash during one year," explained Adante, "and they must take five-year notes for the remainder." The percent of the com-

pany owned by retirees is currently 20% and growing. Retirees can only pass the shares down one generation and cannot sell their stock to others.

Transitions in Leadership

"Most of our officers have been with the company for 25 or more years, so management succession is a major concern," explained Cowan. "We can bring outsiders more easily into our scientific, IT, and accounting areas than in operations because our culture is so unique. We have a successful, entrepreneurial culture of strong individualist field managers who run their own operations. They do not respect outsiders easily, nor any interference that is too bureaucratic. Transition has to be a top priority—we work at it to give people broad exposure."

Warnke added, "Developing the future leaders for any of the top positions in the company is an on-going process. The successful ones not only have the practical experience behind them, but also the business skills to keep the company financially sound. Additionally, and of utmost importance for the continuation of our successful business model is that succession candidates demonstrate total understanding and steadfast commitment to the ideals of employee ownership and our rather unique culture. Without question, these are some of the strongest competitive advantages we have and with continuous improvements, will carry us to future successes. Not everyone can totally commit to this philosophy, but then Davey Tree may not be for everyone." For more information, see www.davey.com **OAW**



In 1908, The Davey Institute of Tree Surgery, a school for Davey Tree employees, was founded to teach scientific knowledge, technical skills, and to provide off-season employment. The tradition lives on in the Davey Tree Institute of Tree Sciences (top). (above) Signatures on a document were the final step in transfer of ownership of the company from the Davey family to its employees. Employee committee members (seated l-r) J.H. Pohl, J.W. Joy and R.D. Cowan and (standing l-r) P.V. Auletta of Society Bank and J.H. Humphrey of U.S. Trust took part in the ceremonial signing. (right) Davey employee owner works from the air.

