Trustee Compensation: What's Appropriate?

Alice C. Buhl
Buhl & Associates

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Introduction

Our newspapers are filled with stories of abuses in the corporate world. The nonprofit and government sectors have their own examples of individuals and boards that have not been accountable. And in recent months, the foundation world has seen headlines that question practices, payments and accountability. The recent legislative attempt to change the definition of private foundation payout has also challenged many ongoing practices and revealed unattractive facts about a few foundations.

Trustee compensation is one of the areas of accountability that continues to attract attention. Recently, many people have again made the case for voluntary foundation boards while others argue for compensated boards.[1] In and outside the foundation field there are strongly held opinions on the subject.

This article in not intended to restate those cases, but rather to pose a related question. If a foundation chooses to compensate board members, how does it decide an appropriate level of compensation? What does a foundation need to consider to assure that its compensation is both reasonable and consistent with the overall mission of the foundation? I talked with a number of leaders in the field (list in Appendix) who suggested ways of approaching this issue. [2]

The Numbers

The Council on Foundations (COF) and the Association of Small Foundations (ASF) both report that approximately 25% of foundations compensate their trustees, with the percentage of such foundations increasing as assets increase. This information is interesting but not conclusive since both COF and ASF depend on self reporting and have relatively small samples. Perhaps more importantly, these figures include public and community foundations, which rarely compensate board members. In the most recent COF study, approximately 40% of independent foundations compensate all board members, 20% compensate some board members, and 40% do not compensate (total responses, 170). The numbers for family foundations are lower, with 15% compensating all, 13% compensating some and 72% not compensating board members (total responses, 238).

A recent study by the Georgetown Public Policy Institute, using information from the IRS 990 forms, suggests that 113, or 64% of the 176 largest foundations (those with assets

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[1] "Board Compensation: Reasonable and Necessary?" by Jason Born, National Center for Family Philanthropy, 2001. "Board Debate: Voluntary or Compensated Boards," by Ellen Bryson and Andrew Schulz, Foundation News and Commentary, September/October 2003. "A Dubious Legacy," by Lee Draper, Foundation News & Commentary, March/April 2001.

[2] This article is also not about reimbursement for expenses or about compensation for specific legal services such as accounting or investment management. Many foundations do reimburse their trustees for travel and other related costs of attending foundation meetings and performing their trustee functions.

over approximately $230 million in 2001) pay trustee compensation.[3] This number is reduced to 61% if the six foundations that pay only bank trustee fees are removed.

Unfortunately, accurate numbers are very difficult to come by since Part VIII of the 990 form that deals with trustee fees also includes foundation officers who are often employees. So in spite of the fact that 990s are conveniently available on line the numbers cannot be used without interpretation. In addition, Part VIII is often inadequately completed by foundations. (For instance, the form asks for the amount of time required of each trustee but relatively few foundations provide that information in any meaningful way.) The numbers are particularly difficult to interpret for smaller family foundations since a family member may be the staff person as well as a trustee.

There is emerging in the field a call for revision of the 990 forms. In addition, many suggest that foundation boards need to review their own 990s to assure accuracy and completeness.[4] (If you are a foundation trustee and haven't seen your 990 forms recently, go on line to Guidestar.com, register--it's free--and check yours. The trustee compensation information is in Part VIII.)

The Legal Issue

The legal requirements are both very simple and frustratingly vague. The Federal law allows compensation as long it is reasonable and necessary to carrying out the exempt purposes of the foundation. Most people probably prefer the vagueness, although one of the leaders I talked with did suggest that foundations are caught because in the absence of legislated standards, they are often judged by differing external expectations.

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[3] "Foundation Trustee Fees: Use and Abuse," by Christine Ahn, Pablo Eisenberg and Channapha Khamvongsa, Center for Public and Nonprofit Leadership, Georgetown Public Policy Institute, September 2003. The authors of this study did a great deal of work to clarify the often very confusing 990 information. However, I believe the study suffers at least two major weaknesses. The total amounts include bank trustee fees and therefore confuse trustee fees with services provided by banks. Secondly, the information from the larger foundations includes most large foundations over roughly $230 million and therefore reasonable conclusions can be drawn. The sample of small foundations is arbitrary. It is an interesting collection of examples, with some at very high fee levels, but the study cannot lead to any overall conclusions about trustee compensation in small foundations. None of the information from the small foundation sample is included in this paper.

[4] Until the 990s are revised, foundations can provide full information on the current form by (1) Including specific hours per week, month or year that trustees estimate they spend on their responsibilities as trustees; (2) Clearly differentiating between paid staff officers and trustees or directors; (3) If trustees have staff responsibilities, separating the salary paid for those responsibilities from the fees paid for trustee responsibilities; (4) Making some note of the services provided by a corporate trustee or bank.

Considerations in Determining What Is Reasonable

The remainder of this paper deals with the question of how a foundation decides what is reasonable. And what most agree is that there are many factors to be considered. Remember, however, that each factor has its limits; each needs to be evaluated in light of all the others. At some point most people look at a situation and say, "That is unreasonable." As one person put it, "It's a bit like obscenity. We **do** know it when we see it."

Donor Intent

American philanthropic laws have tried to balance the rights of the donor and the public obligations of a tax deductible contribution. It is broadly accepted that this country has a strong tradition of philanthropy and giving in part because our laws encourage private philanthropic giving and give fairly broad latitude to the donor.

One point of view is that the donor's intent is as relevant regarding trustee fees as it is in understanding what the donor hoped to accomplish with the dollars. This point of view says, "If a donor wanted certain kinds of people to serve on the board and so expected the foundation to pay trustee fees, that wish should be respected. If a donor was active in the corporate environment and believed that trustee fees were an important attraction for corporate board types, that too should be respected." Some fear that without this ability to assure that the foundation will have appropriate oversight (as defined by the donor) some donors might do other things with their dollars than establish foundations.

Expectations of Individual Trustees

A critical matter in determining reasonableness is weighing what is expected of individual trustees. Most foundation trustees are expected to attend two to four meetings per year, prepare for those meetings and possibly serve on a committee. These trustees provide broad oversight, policy and financial advice.

Beyond those basics, some foundations call on trustees to attend more than four board meetings per year (a few even monthly), participate in site visits, either individually or as part of a joint board event, serve on several committees, attend conferences or workshops, and represent the foundation at other gatherings. In smaller foundations board members often play very active roles on grant review committees. Some trustees attend board meetings in the community they live in but many, particularly in the larger, national foundations travel to attend board meetings.

Some foundations also consider differing trustee responsibilities. It is not uncommon for a board chair, for instance, to receive a different level of compensation based on the added responsibility and time required.

All of these factors add up to an amount of time that an individual trustee ordinarily spends in order to responsibly fulfill his or her responsibility as it is defined by that foundation board. Foundations can be more deliberate about tracking this time, not just to validate compensation, but also to provide a potential board member with a realistic idea of what will be required. Obviously the total of expected time varies significantly from foundation to foundation, an indicator of why it isn't sufficient to merely compare trustee compensation numbers without understanding the demands behind them.

Most work situations connect time and dollars in some way, the more time spent, the more dollars received. However, one person pointed out that there is a bit of Catch 22 in this equation.   If trustees feel they need to justify their compensation by spending time for the foundation on tasks that might be better done by staff, that could also create problems.

Characteristics, Background and Skills of Individual Trustees

One of the calls today on both corporate and nonprofit boards is for the board to be more accountable.   This kind of accountability could well require a board to include a range of people with appropriate knowledge, experience or skills, depending on the work the foundation does. As one foundation executive said, "If you believe trustees should be something other than stooges for staff, you need trustees who are capable and . . . can be wise and involved."   What that will take varies from foundation to foundation. Some foundations are dealing with complex issues, a national or international scene, communications challenges or community based strategies which may require special skills, experience, oversight or even public stature.

Ensuring there is sufficient diversity in the backgrounds, skills or income levels of trustees is often cited as a rationale for compensation, and therefore of particular interest in setting fees.

For example, third and fourth generation members of families engaged in organized philanthropy are not always wealthy. Some of these young people are teachers, social workers, or are nonprofit organization employees. Some are at the early stages in their careers and must give up vacation time to attend board meetings, often with extensive travel time. Serving on the family foundation board may impose real personal financial challenges in the absence of trustee compensation.

Similarly, both family and independent foundations may want to attract academics who receive modest salaries. Others may wish to include people who are self employed, such as expert consultants, for whom a day away is lost income. Some wish to include newly retired community leaders who may have time but only modest retirement benefits. Finally, some foundations wish to attract very busy people who have experience serving on corporate boards, who have opportunities to serve on many boards and who are accustomed to receiving significant fees.

The notion that a foundation will attract trustees across a complete range of class and income may well be as improbable as it is for most nonprofits.   However, several leaders cited examples of including people who bring ethnic or economic diversity and for whom serving on the board would result in lower income, taking a day off work, or might require serious time trade offs for family or personal interests.

The Big Picture: Size, Risk and Context

There are very different points of view on whether the size of the foundation should influence the level of trustee fees. On the one hand, there's the argument that the same due diligence is required whatever the size of the foundation. This point of view suggests that service on a smaller foundation board might require even more effort since such an organization is not likely to have a bank of sophisticated staff to provide information in all areas where due diligence is required.

On the other hand, it is arguable that the complexity of larger organizations requires a higher lever of background and experience among at least some of the trustees, implying possibly higher fees. In fact, larger foundations do pay higher levels of trustee fees according to surveys done by the Council on Foundations.

And what about risk? People who have served on corporate boards suggest that foundation boards bear comparatively little risk. However, legal challenges are a possibility which is why most large foundation board members are covered by insurance for fiduciary acts short of a deliberate malfeasance.

Does it make a difference if the foundation is organized in the charitable trust form? Although there are technical and legal differences, no one I spoke with saw significant differences of a practical sort to justify higher fees for trustees of charitable trusts.

The big picture issue on which people do agree is that trustee fees are just one piece of the larger context in which accountability is measured. Trustees need 1) regularly to review administrative costs as a percentage of assets, and the amount of payout going to grants as well as the level of trustee fees and 2) to be able to coherently describe how and why these numbers are consistent with the goals and strategies of the foundation. Foundations that pay trustee fees are not necessarily more or less responsible or efficient in achieving their mission or in using charitable dollars. It takes a look at the whole picture to begin to answer that question.

Ways of Compensating

Foundations use a variety of approaches to compensate trustees. Some provide a monthly or yearly retainer. Some pay an amount per board meeting that is intended to include all preparation for the meeting. Some foundations do both—the model used by most corporations. Some pay for committee meetings in addition to board meetings. Some operate more on a time-based model, paying per day. And some pay additionally for the added responsibility of board chair.

The leaders I talked with agreed that pay should be equitable and should not be based on the actual wealth or need of the individual. However, some family foundations do pay fees only to non-family members. Several foundation trustees suggested that they automatically contribute their fees to philanthropic causes and believed that was not an unusual practice among their colleagues. One foundation trustee said that his foundation was helpful to trustees by matching these donations with foundation dollars.

Some foundations that are very opposed to trustee fees do provide discretionary dollars so trustees can contribute to organizations of special interest to them. They may see this as a form of thanks for the time and commitment of trustees.

Levels of Compensation

There are many rationales for levels of compensation. But let's start with a few facts. The Council on Foundations reports that the median annual fees paid to board members in 2001 was $10,000. The median individual maximum fee on the Georgetown study was between $26,000 and $30,000. Approximately two thirds of individual maximum fees were under $40,000. [5] Although the Georgetown Study is several years old and the data is not complete (mostly because of the difficulty of interpreting the 990s), it does offer at least a snapshot of fees paid by larger foundations (with assets above $230 million).[6]

The Council on Foundations has a policy that states it is firmly opposed to excessive or unreasonable compensation and that even the public perception of excessive compensation can be damaging to the entire field of philanthropy. Are the 16 individual trustee fees reported in the Georgetown study over $100,000 excessive? (One trustee received $750,000 in fees.) Most people would say yes. What about the additional 14 over $50,000?

On the other hand, the total fees paid to trustees can also be important. Several foundations with the largest fees paid that amount to only one trustee. If we look at total trustee fees paid, the median for larger foundations in the Georgetown Study is about $115,000. However, approximately two thirds of the total individual fees were under $200,000. (The highest total was $1.9 million.)

Those who believe the size of the foundation is important in considering the level of trustee fees might want to also look at the total trustee fees as a percentage of assets. I looked at seven foundations whose total fees were around the median and found a wide range of percentages, from a low of .0038% to a high of .0337%.

Several of the leaders I talked with connected their thinking about trustee compensation with practices in the corporate world. They didn't expect the fees to be equal, but did believe larger foundations needed to be aware of those practices if they hope to attract some trustees with corporate board experience. As a comparison, a recent survey from the National Association of Corporate Directors reports direct cash compensation averages from $20,926 for smaller companies to $39,485 for medium-sized companies. Directors receive stock awards in addition, bringing the total value to $47,486 for smaller companies and $88,228 for medium-sized companies (of course, that's assuming the

[5] These numbers all use the median of those who pay fees. If the total sample of larger foundations from the Georgetown study is included, counting those who pay no fees, the median individual maximum would be around $10,000.

[6] Because the numbers in the Georgetown study are not complete, I deliberately used approximate numbers in my reporting, so as not to imply more accuracy than exists. Individual maximums can also be misleading since many foundations pay a higher fee to the board chair.

stock retains its value). [7] *Corporate Board Member* reports that fees will very likely increase in the future because expectations of oversight responsibilities and liability risks have ballooned.

Two leaders suggested using professional consulting fees as a measure to determine the level of fees. However, professional consulting fees vary widely, from a low of perhaps $500 per day to the $4000 to $5000 per day charged by a few consultants with very special expertise.

The Georgetown Study suggested that $8000 a year should be a maximum for individual trustee fees (but preferred there be no fees).[8] On the other hand, the leaders I talked with had various ideas of the maximum that might be appropriate. One opponent of fees suggested several thousand dollars, but only if the fees would diversify the board. Several supported fees reluctantly and looked at $10,000 as a possible maximum. Several others came down in the range of $20,000 to $25,000 as an absolute top. Others were willing to stretch further if there was a case for the amount of time or other factors taken into consideration. Above $50,000 most leaders wondered whether it would be possible to document reasonableness.

Determining Comparable Fees

It isn't easy to get comparable information on trustee fees, but it is easier than it used to be to get the raw numbers. Because information is now easily available on line it isn't a huge task to get together information about what similar-sized foundations pay their trustees. However, the information at this point still needs interpretation. Assuming the 990 forms get revised to deal with these problems, it would be a great service if COF would put together trustee fee information for all foundations over a minimum size and report it regularly and publicly. This would be far superior to the current dependence on the salary survey which is completed by a relatively small number of foundations.

However, this takes care of just the numbers. What about the many other factors described above? Some larger foundations regularly check with colleague foundations of a similar size and grantmaking style for information on trustee compensation just as they collect comparable salary information. Most foundations could, over time, develop a list of 10 or 20 foundations that they believe are similar to themselves with respect to the role the board plays and in the complexity of their grantmaking. Comparing trustee fees with this group would add meaning to the numbers.

The Process Used to Decide Trustee Compensation

Most people believe it is important that there be a clear review process for determining trustee fees so that they meet the test of reasonable. Abuses often occur when boards don't exercise due diligence. At a recent seminar on corporate abuses, Ambassador James A. Joseph, former CEO of the Council on Foundations and head of the Duke

[7] Smaller companies have revenues of 50 to 200 million dollars and medium-sized ones are in the 600 million to 1.7 billion range.
[8] This conclusion came from using a base salary of $96,000 and assuming that the maximum time commitment by a trustee would be no more than one month's work time annually.

University Center on Leadership and Public Values, posed key questions—a decision making framework trustees might use—for dealing with the issue of director's compensation in the corporate or foundation world;

(1) Is it legal, meeting the conflict of interest test?

(2) Is the decision made independently, in a disinterested way, providing for an objective consideration?

(3) Is it reasonable?

(4) Does the board look at comparable data in terms of what other trustees are compensated for performing similar work in similar foundations with a similar time commitment?

(5) Is the process documented and transparent?

Foundations who have had trustee fees for some time without a formal review would be well advised to collect information and schedule a discussion so that the board is exercising due diligence. Most boards approve fees yearly as a part of budget approval. Other boards might schedule a regular review of fees every three to five years. Some foundations satisfy the transparency requirement by listing trustee fees as a separate line item in their public financial reports.

Concluding Thoughts on Public Self Awareness

Several interviewees expressed a concern about the perception of the field when unreasonable fees are paid. One said, "Most foundations start out as essentially clubs of the like-minded, a family, a clan. Clubs tend to be closed moral universes. Each and all have to keep asking, in the world of real value outside, what is really acceptable, defensible, and act accordingly."

Several people also believe that the foundation world needs to expose those who pay unreasonable fees. COF for many years has talked privately with foundations seen not to be exercising due diligence in some arena, but it may now be necessary to go further. As one person put it, "Initially it has to come from a group of the like minded. We take our stand that this is not tolerable, dangerous for the field. Associations have to keep vigorously raising these issues over and over again. We have to be very public about things people prefer to discuss privately."

Leaders Interviewed.

Note: all of these leaders have many titles and affiliations. I have included only a few that might be relevant to this study.

I would like to thank the leaders below for their time and careful thinking about the issue of trustee compensation. Without their gracious and candid contributions, this paper would not have been possible.

Hodding Carter, CEO of the Knight Foundation (Florida), former assistant Secretary of State for Public Affairs.

Rick Cohen, head of the National Center for Responsive Philanthropy, former Vice President of the Enterprise Foundation and of the Local Initiatives Support Corporation

Pablo Eisenberg, Center for Public and Nonprofit Leadership, Georgetown Public Policy Institute, former head of the National Center for Responsive Philanthropy.

Virginia Esposito, President of the National Center for Family Philanthropy and former Vice President of the Council on Foundations

James A. Joseph, former CEO of the Council on Foundations, former ambassador to South Africa, head of Duke Center on Leadership and Public Values.

Rush Kidder, President of the Institute for Global Ethics, member of the Mott Foundation (Michigan) board.

Robert Lynn, Lake Family Institute on Faith and Giving, Center on Philanthropy, Indiana University, former Lilly Endowment officer.

Margaret Mahoney, former CEO of the Commonwealth Fund (New York), former member of the MacArthur Foundation board.

Curtis Meadows, head of the RGK Center for Philanthropy, LBJ School of Public Affairs, former board member and CEO of the Meadows Foundation (Texas), chair of the National Center for Family Philanthropy Board.

Mary Mountcastle, board member and chair of the Z. Smith Reynolds and Babcock Foundation Boards (North Carolina); current chair of the Council on Foundations Board.

William Richardson, CEO and President of the W. K. Kellogg Foundation (Michigan), former Board chair of the Kaiser Foundation, former chair of the Council on Foundations Board.

Charles Rooks, former head of the Meyer Foundation (Oregon), and former Executive Vice President of the Council on Foundations.