"Are We Paying Our Executives Appropriately?"

Answer these 3 questions and you'll know

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"Are we paying our executives appropriately?" I am frequently asked this question by board members and these questions have become even more frequent in the current COVID-19 environment. Amidst all the uncertainty, the question seems more relevant than ever. Whether it is an organization taking its first formal look at executive pay, a new board member serving on a compensation committee, or a question raised following our presentation of an annual compensation "checkup," it is a key question that every board should be able to confidently answer. Regardless of the type of nonprofit organization, there is an expectation (and IRS regulations!) that board members must be good stewards of the organization's assets. This is especially true regarding the most highly compensated members of management.

Board members are specifically charged with responsibility for managing the pay for top executives, but many have little to no experience with the subject. Those individuals with some compensation experience with other organizations frequently have little to no experience directly related to the nonprofit board on which they serve. This is likely the explanation for the prevalence of the "Are we paying our executives appropriately?" question.

It is a good question. And it is one that all boards, or at least their compensation committee, should be able to answer. If a board member does not know the answer, there should be no reluctance to ask the question. Unfortunately, people are sometimes hesitant to do so. People not familiar with the compensation topic or new to the organization's board hold back. Whether unwilling to admit they have questions or feeling a need to "go along with others who seem to know what to do" or "continue to do things the way we've always done them" — the important question above just does not get asked. The path of least resistance is to simply chime in for the all-too-familiar "All those in favor, say Aye" board chorus.

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In these COVID times there are, however, some new questions about executive compensation that need to be answered. Many of the familiar and essential factors normally included in board decisions about executive pay are no longer available or relevant. The disruption related to the virus has broadly impacted all sectors of the economy. The issue of competitiveness in terms of compensation is muted at least for the moment. Uncertainties abound and everyone is searching for answers about what they should do. For most organizations, the answers will come from within. Each must chart its own way for the foreseeable future. For this reason, I'd like to suggest that the following three new questions be considered to arrive at an answer for **your** organization related to whether executive pay is appropriate in these COVID times when unknowns seem to be the order of the day.

Question #1

Do our current financial condition and outlook for the next 18 to 24 months allow us to continue our current methods and levels of compensation for staff members and our executives?

Affordability is a critical issue and possibly the most urgent one. If there are concerns about finances, there are a series of progressively more stringent techniques that can be taken, including: discontinuation of "voluntary" plans/payments; salary freeze; salary reduction; furloughs; staff reduction, etc. Each of these must be carefully weighed to arrive at the best answer for your organization. The consideration is not solely financial.

Retention of key personnel, staff morale/engagement, continuation of critical services, stakeholder reactions, etc. are also important factors to consider.

Once decisions have been made about any cost-saving actions, they should be fully communicated to all concerned with as much advance notice as possible. In particular, all the details about the duration of the change(s) should be included to the degree that they can **confidently** be set. Future communications should be made as conditions change, as well as to affirm that the subject has not been forgotten.

Question #2

Under current conditions, should our competitive pay positioning policy be maintained?

Even if the organization's financial condition can support holding current executive compensation at target levels in the competitive market, should they stay the same? There are several factors to consider.

COVID times have disrupted the availability and relevance of many sources of competitive compensation data. Newer IRS Form 990 filings are not being posted and are even more outdated than in normal times. Most compensation surveys are reporting on data collected pre-COVID and do not reflect current conditions. Reliable information on competitive compensation may not be available to guide pay decisions.

In some instances, competitive compensation levels have likely decreased due to temporary salary reductions, suspension of bonus/incentive plans, etc. The pressure to keep up with the market has decreased significantly for most organizations.

Finally, there are other factors that may weigh more heavily in executive compensation during these times such as: public/stakeholder perception of executive pay actions, equitable treatment of staff members vs. executives, etc.

For the next 12 to 18 months, executive compensation should be carefully considered as part of a thorough assessment of the organization's situation and circumstances. As mentioned previously, competitiveness may not be as prominent a consideration now. Again, regular communication to all concerned about any change/moderation of traditional approaches to pay is critically important.

Question #3

What factors should be considered in executive pay decisions that are needed for 2020 or 2021?

COVID times may have deprived the organization of its traditional benchmarks or made its performance metrics no longer relevant. For this reason, many organizations will need to make pay decisions on a largely discretionary basis. Discretionary should not imply a hastily made monetary "thanks for everything" at year end. I am suggesting a thoughtful approach, one that requires pre-planning and discussion by the compensation committee of the criteria that will be used for any pay-related decision making.

Rather than delaying a discretionary decision until the final compensation committee meeting for 2020, boards would be well-advised to begin discussions and planning now for the specific factors that will be considered when these decisions are made. Board members can exchange and consider ideas to arrive at a general consensus about several critical factors that will be used.

For example, boards may consider:

- How well has management cared for the organization's employees?
- How have the organization's stakeholders been treated?
- How have the organization's vendors been treated?

These types of questions focus on the executives' stewardship of the organization for the longer term. Once decided, the factors should be communicated to all concerned parties in advance. That information will highlight the behaviors and results that are important for moving forward through this time.

In summary, good answers to the three questions we've raised here are essential for a good answer to the "big" question — "Are we paying our executives appropriately?" — during these unprecedented times. Arriving at the right answer for your organization is critically important.

If you do not know the answer to "Are we paying our executives appropriately?" for your organization, please ask!

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