

## **At Issue: Voluntary or Compensatory Boards — Which Is the Better Policy?**

### **Introduction**

Should your foundation board members be compensated for service, or should they serve in a voluntary capacity? Whether you are considering this issue for the first time, or whether it's a question that has arisen before, compensation has become more than an internal management question. It has become part of keeping the public trust.

What follows is a description of the basic legalities of compensation, a sampling of the most common practices and a breakdown of the pros of both compensated and voluntary board service. Unless otherwise noted, the word “compensation” throughout this brief refers to payment for overall board service and should not be confused with reimbursement for expenses such as travel or professional development, or compensation for professional services such as investment management, accounting or legal advice.

### **Excessive Compensation**

The board of directors of the Council is firmly opposed to excessive or unreasonable compensation. Even the public perception of excessive compensation can be damaging to the entire field of philanthropy.

For more information, consult *Determining Reasonable Compensation for Foundation Directors and Trustees* at [www.cof.org/files/Documents/Governing\\_Boards/trusteecomp2003.pdf](http://www.cof.org/files/Documents/Governing_Boards/trusteecomp2003.pdf)

### **What is legal?**

Under federal law, all types of foundations are allowed to compensate their boards as long as the compensation is reasonable. The source of the requirement differs, however, depending upon whether the foundation is private (such as independent or family foundations) or whether it is public (such as community foundations). Private foundations must keep compensation “reasonable” under the self-dealing rules.<sup>1</sup> A similar obligation applies to community and other public foundations under the intermediate sanctions regulations.<sup>2</sup> Regardless of the defining rule or regulation, however, “reasonable” for all foundations is determined through comparisons of what similarly situated people are paid for similar work.

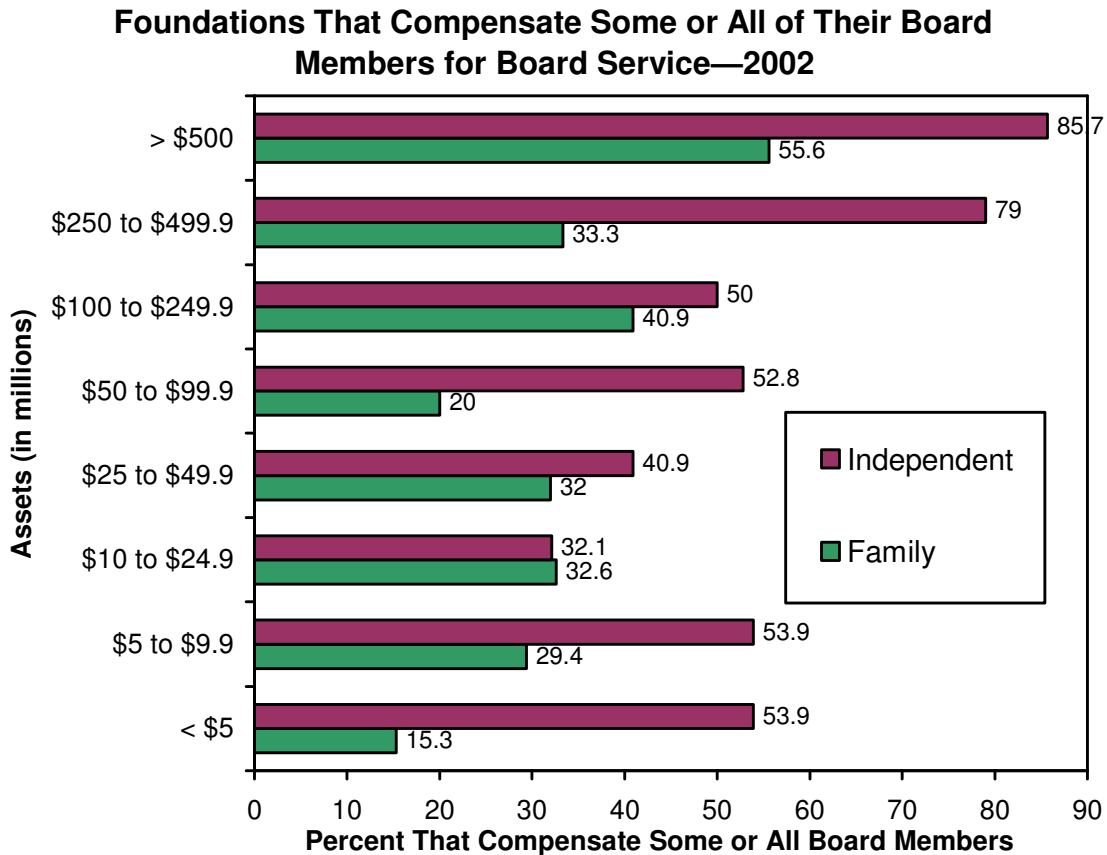
<sup>1</sup> For discussion on the self-dealing rules, see *Rules of the Road: A Guide to Law of Charities in the United States*, Betsy Buchalter Adler (Washington, DC: Council on Foundations, 1999).

<sup>2</sup> For more information on intermediate sanctions, refer to *Legal Compendium for Community Foundations* (Council on Foundations, 1996).

## Who compensates?

Even though compensation is legal, only about 25 percent of foundations pay some or all of their trustees for their board service.<sup>3</sup> Many nonprofit board members view their board service as an extension of their public service. The percentage, according to the Council on Foundations' *Foundation Management Reports*, has stayed fairly even over the past two decades. In its 2002 Member Survey Report, the Association of Small Foundations also reported that 25 percent of foundations compensate their boards.

These studies also show that compensation practices vary by type and size of foundation. Of all the foundation types, independent foundations offer compensation more frequently and at somewhat higher levels. Community foundations, on the other hand, rarely if ever compensate their board members. Somewhere in the middle are the family foundations that are frequently unstaffed and whose boards often serve a variety of staff and management functions. Typically, the larger the foundation, the more apt they are to compensate. The chart below gives a quick overview of the common practices by independent and family foundations.



*Note: Community and public foundations are not included above because so few compensate board members.*

<sup>3</sup> Council on Foundations' biennial *Foundation Management Reports*, various years.

## What do you pay for?

If your practice is to compensate, it's important to know and document what you (and others like you) are paying for. The work board members are compensated for varies from foundation to foundation depending upon factors such as asset size, spending level, program complexity, staff capabilities and foundation culture.

Some trustees receive an annual fee in payment for performing a broad oversight role. Sometimes, in newer boards or boards without staff, members may be paid for being involved operationally and taking on part or all of typical staff functions. Occasionally, individual board members may perform specific professional services—legal, accounting, investment management or advisement—but rather than be paid on a fee-for-service basis, those duties are rolled into their annual compensation.

There are also some foundations that compensate their boards for attendance at each board or committee meeting.

Among those foundations that compensated board members, 90 percent used some combination of set fees, with most paying an annual fee (69.3 percent) and/or a fee per board meeting (65.4 percent). Only 33.3 percent pay per committee meeting.

## How much should you pay?

Remembering that what's typical changes depending upon the type and size of a foundation, statistics suggest that the actual amount of board compensation has increased at a slow but steady rate since 1986. (See chart.)

Both the Council on Foundations and the Association of Small Foundations<sup>4</sup> have collected information on the amount and type of trustee compensation. Although neither study is a comprehensive indicator of current practices for all foundations, they both list ranges to help you determine whether your compensation practices fall within the norm.

**Median Annual Fees Paid to Board Members  
(Nominal and Inflation-Adjusted), 1986–2001**

Year	ANNUAL FEES	
	Nominal	Real
1986	\$4,500	\$4,500
1988	5,000	4,736
1990	6,000	5,201
1992	5,000	3,963
1994	8,000	5,997
1997	6,300	4,342
1999	10,000	6,494
2001	10,000	6,186

Source: Council on Foundations, *Foundation Management Series*, various years

<sup>4</sup> See the bibliography for more information on the Council on Foundations studies. Association of Small Foundations Membership Survey Reports can be found at [www.smallfoundations.org](http://www.smallfoundations.org).

Taking into consideration the type of your foundation and the expectation in place for board service, how do you determine what is reasonable and fair? Most foundations have specific criteria by which they determine how much to pay. Factors that affect compensation include the following:

- Size and anticipated growth of the foundation's current assets
- Number and amount of the grants and the frequency of the grant making process
- Experience and management responsibilities of the board member
- Amount of time spent on foundation matters
- Complexity of the foundation
- Independence of the individuals who establish the compensation level.

Finally, for those who do compensate, it's valuable to remember that, under federal law, all board compensation must be reported on the IRS form 990 or 990-PF. This information must also be made available in some form to the public.

## **Should you or should you not compensate?**

Assuming you work within accepted compensation levels, there are a number of arguments for either practice.

### **The Case for Compensated Boards**

**Quality of member:** Compensation is needed in order to attract quality candidates. Too often, people with high visibility and valuable contacts won't serve without pay.

**Technical expertise and talent:** A board is often expected to bring a level of sophistication to complex topics. Compensation helps attract individuals with strong technical, professional or subject matter expertise.

**Risk:** There are personal and professional risks inherent in board service. Compensation may help tip the balance in favor of serving.

### **The Case for Voluntary Boards**

**Inspired board members:** Serving without compensation encourages board members to express their philanthropic values, encourages altruism and places public benefit above self-interest.

**Charitable resources:** Board compensation reduces the amount of money available for grants and programs. Money not spent on compensation frees up resources to further the foundation mission.

**Fairness:** Public charities rarely compensate their boards. Since the obligations and responsibilities of foundation boards are essentially the same, why should they be paid?

## The Case for Compensated Boards

**Loyalty:** A paid person is less apt to take advantage of board service for personal gain. Being compensated might strengthen one's obligation to duty.

**Interest:** Because trustees, like anyone else, have only so much time, compensation may help sustain their interest, helping them to be more responsive and pay greater attention to their board responsibilities

**Equal pay for equal work:** Both trusts and for-profit boards have a history of paying their trustees. Since the obligations and responsibilities are similar for foundation boards, why shouldn't they be paid the same for the same work?

**Diversity:** Compensation promotes the recruitment of a diverse board. It opens service up to individuals from different cultures, classes, ages or personal situations who might not otherwise be able to serve as volunteers.

## The Case for Voluntary Boards

**Conflict of Interest:** Because volunteers aren't paid, they are free from potential conflict that might result from trying to protect an income stream. Therefore, they are less susceptible to conflicts between what is the right thing to do and what is in the best interest of those who are signing their paycheck.

**Leadership by example:** Foundations often expect grantees to make the most of their charitable dollars, including keeping their administrative overhead low and using volunteer boards. A foundation can set the tone by modeling the same behaviors.

**Public trust:** Compensation sends the wrong message and erodes the quality of public perception. Foundations should be particularly concerned about the models they present.



"It's time to vote on the board's raise.  
Larkin, go warm up the getaway car."

By Leo Cullum

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### **In Sum, Ask Yourself...**

- **What is our practice when it comes to compensating our board?**
- **How do we compare with other foundations that are of similar type and size?**
- **How does public perception shape our views?**
- **How do we document compensation on our IRS Form 990 or 990-PF?**

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