Girl Scouts. **Memo**

Attachment D

Girl Scouts of Western Ohio

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Date: February 12, 2010

To: Board of Directors

From: Nancy C. Dawes, Chair

Subject: Compensation Philosophy

Attached are several documents that will be reviewed at the February board agenda concerning the establishment of a compensation philosophy for Girl Scouts of Western Ohio:

1. *Executive Compensation in the Nonprofit* – a white paper with background information
2. PowerPoint – Executive Compensation
3. Draft Compensation Philosophy (reviewed by Sharon Czebotar, Director, Council Staff Resource Development, GSUSA)

The issue of executive compensation has captured the attention of the national media, Congress, and the general public. GSUSA is recommending that the best way to ensure not only legal compliance, but also protection of the council's integrity and reputation, is for Girl Scout boards to institute a written compensation philosophy.

Prior to the merger, salaries from all four legacy councils were analyzed by a Human Resources consultant and compared to GSUSA and local salary surveys. This information was shared with management and formed the basis for current compensation. The council's benefits program was established prior to the merger through the work of a staff task group and included reviewing the benefits of each merging council and drafting a new set of benefits to compete in the local market. Since the merger, all current positions have been graded by GSUSA and new job descriptions provided to staff. Establishment of the compensation philosophy will support the ongoing work and strengthen our human resources policies.

Please review the attached documents and be prepared to discuss this issue at our February board meeting. After discussion, I will ask for a motion to approve the compensation philosophy.

Executive Compensation in the Nonprofit

Introduction

A council's ability to attract and retain key executive talent in the marketplace is critical to its ability to deliver on its mission. In order to attract high-caliber executive-level talent, a council must offer a competitive compensation package. When developing an executive compensation package, each council must balance the compensation demands of a competitive labor market with its overall financial picture and ability to pay competitively. Additionally, councils (along with other nonprofits) must adhere to IRS regulations covering nonprofit executive compensation levels.

In these turbulent economic times, executive compensation has captured the attention of Congress, the press, and the general public. Even if an organization meets the technical standards outlined in the IRS code, the organization may still face scrutiny from state regulatory officials, the media, internal constituents, and the public. The best way to ensure not only legal compliance but also maintenance of the organization's integrity, reputation, and public goodwill is to institute sound, proven practices around executive compensation.

Legal Framework

Prior to September 1995, revocation of a nonprofit's 501(c)(3) status was the only remedial action the IRS could take against a nonprofit that awarded executive compensation in excess of the fair market value of the services the executive provided to the nonprofit. The regulations refer to this imbalance of compensation level relative to services rendered as an "excess benefit transaction." In many cases, revocation of 501(c)(3) status seemed to be an extreme penalty measure relative to the level of transgression. As the nonprofit sector evolved and grew and cases such as that of William Aramony of United Way came to public attention, Congress passed legislation allowing for sanctions that were more in line with the level of regulatory transgression involved. These regulations (known as Intermediate Sanctions) are detailed in Section 4958 of the IRS code; they impose excise taxes on executives and other insiders who improperly profited in their dealings with a nonprofit public charity. Girl Scout councils fall under the nonprofit, public charity entities covered by section 4958.

The Intermediate Sanctions are aimed at preventing public charities from engaging in "excess benefit transactions" (such as payment of excessive salary and bonuses) that benefit individuals with substantial influence over the public charity. Individuals with substantial influence are referred to as "disqualified persons" under the regulations. The regulations define disqualified persons as:

- Voting members of the governing body, which would likely include board members in a council environment (even though board members are unpaid, they could conceivably benefit from "excess benefit transactions" involving the purchase or sale of services, equipment, or property vis-à-vis the council);
- Persons who have ultimate responsibility for implementing the decisions of the governing body or for supervising the management, administration, or operation of the organization, which would likely include CEOs and possibly COOs and others with considerable decision-making authority; and/or
- Individuals who have ultimate responsibility for managing the finances of the organization, which would likely include CFOs and treasurers.

In determining the reasonableness of the compensation, all items of compensation provided by the tax-exempt entity in exchange for the performance of services are taken into account. These may include:

- All forms of cash and noncash compensation, including salary, bonuses, fees, severance payments, and deferred compensation;
- The payment of liability insurance premiums, or reimbursement of taxes or certain other expenses, and fringe benefits (such as club memberships) unless excludable from income as de minimis fringe benefits;
- Payments to medical welfare benefit plans (medical, dental, vision, etc.);
- Expense allowances (except those under an accountable plan);[1] and
- Foregone interest on below-market loans.

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[1] An expense reimbursement process that describes the business connection of the expense and requires expense substantiation and the return of all amounts in excess of documented expenses that satisfy the requirements of section 62(c) of the IRS code

As mentioned earlier, the IRS provides guidance as to what steps employers should take to ensure that the executive compensation package will be presumed reasonable according to the IRS code. Under the IRS code, an organization will have established a "rebuttable presumption" of reasonableness if three conditions are met:

Condition (1): The compensation arrangement has been approved in advance by an authorized body of the applicable tax-exempt organization. The authorized body must be composed entirely of individuals who have no conflict of interest with respect to the compensation arrangement. In a Girl Scout council, this body would be the board of directors.

Under the regulations, a conflict of interest would exist if a member of the decision-making body were related to, had an employment relationship under the control of, or received compensation subject to the approval of the disqualified person (executive). Take note that in meeting Condition 1, it is not sufficient to have a conflict of interest policy on file or to have a policy which requires that potential or actual conflicts of interest be disclosed. In order to comply with Condition 1, there must be a complete absence of conflict of interest within the decision-making body. Any member who has a conflict of interest must recuse herself/himself from voting.

Condition (2): The authorized body (board of directors) has obtained and relied upon appropriate comparable data in making its determination. GSUSA's Human Resources Consulting and Compensation staff can assist the council in data gathering.

In determining whether the authorized body obtained and relied upon appropriate comparable data, the IRS considers:

- The knowledge and expertise of each of the voting members of the authorized body as to the particular proposed transaction under consideration (in other words, do the board members making the decision have the competencies and skill sets necessary for effective decision making around executive compensation); and
- Whether the authorized body had sufficient information and data to determine whether the compensation arrangement (in its entirety) was reasonable. Relevant information would include:
    - Compensation levels paid by similarly situated organizations, both profit and nonprofit, for functionally comparable positions;
    - The availability of services similar to those performed by the disqualified person (executive) in the geographic area of the applicable tax-exempt organization;
    - Current compensation survey data compiled by independent firm(s); and
    - Actual written offers from similar institutions competing for the services of the disqualified person.

Condition (3): The authorized body adequately documented the basis for its determination concurrent with making that determination. The written documentation should include the terms of the transaction under review, the date of its approval, the members of the authorized body present during the debate and vote, the comparability data obtained and relied upon in decision making, the actions of any member of the authorized body having a conflict of interest, and the reasons/basis for the determination. If the conditions are met, the IRS can refute the presumption of reasonableness only if it develops sufficient contrary evidence to rebut or refute the value of the data relied upon by the authorized body.

Excess Benefit Treatment

Note that unless the applicable tax-exempt organization providing the benefit clearly indicates its intent to treat the benefit as compensation when the benefit is paid, the economic benefits are treated as "excess benefits" under the regulations. This compensation designation requirement can be satisfied by:

- The organization reporting the benefit as compensation on an original federal tax information return (Form W-2, Form 1099, or Form 990), or on an amended federal tax information return filed before the start of an IRS examination;
- The disqualified person (executive) reporting the benefit as income on his or her original or amended Form 1040, filed before the start of an IRS examination; or
- The organization producing a signed, written contract between the executive and an authorized organization representative.

Should a nonprofit fail to meet the requirements outlined above, the entity and the executive may be subject to the following penalties for "excess benefit transactions":

- Reversal of the transaction by means of the executive repaying the excess amount to the nonprofit entity, along with interest;
- Imposition of a 25-percent tax on the disqualified person's excess benefit;
- If the prior actions are not executed within 90 days of receiving an IRS deficiency notice, the disqualified person may incur a liability of an additional 200-percent tax on the excess benefit;
- If an organization's managers knowingly and willfully participate in an excess benefit transaction, they may be subject to a 10-percent tax on the excess benefit, up to $10,000 per transaction (if the disqualified person receiving the benefit is also the manager, he or she may be subject to both the 10- and 25-percent tax; managers may include CEOs, officers, directors, employees, or others with similar powers); and/or
- IRS revocation of the nonprofit's 501(c)(3) designation.

Recommendations

In light of the above, GSUSA recommends that councils put the following practices in place:

- Identify all disqualified persons and organizational managers.
- Set up a system for independent review of compensation and performance systems.
- Conduct a review of executive compensation plans vis-à-vis the current economic climate and council financial circumstances. Considerations include:
    - Checking to ensure that the design of any "incentive program" is in keeping with the organization's mission and resources
    - Reviewing severance arrangements relative to size, length, and precipitating need
    - Examining the controls for review and approval of executive and board travel and other expenses
    - Evaluating the affordability and appropriateness of executive perquisites (such as club memberships, automobile allowances, etc.)
    - Regularly briefing the full board on the executive-level pay philosophy, program, and its various components
- Form an independent compensation task group of the board of directors. Ensure that the members of the task group have the requisite skills, experience, and knowledge to render appropriate recommendations and decisions.
- Review or develop a conflict of interest policy and ensure it is appropriately executed within the context of executive compensation; assess the transparency and integrity of the decision-making process; check for perceived as well as actual conflicts of interest.
- Revisit the organization's overall compensation philosophy; test the consistency of executive-level pay decisions vis-à-vis this philosophy; test for internal equity as well as external competitiveness. Ensure the board reviews, understands, and supports the total compensation package through its decision-making process. Since the information is public and reported on Form 990, the board should understand and be able to articulate a rationale for the compensation decision.
- Enlist the support of independent compensation professionals in compiling and analyzing data; ensure the data set used is representative of "comparably situated" organizations and positions. (GSUSA's Compensation Unit can assist here.)
- Distribute worksheets to ensure board and task group members understand the full scope and cost of executive pay packages.
- Assess the transparency and integrity of the decision-making process; check for perceived as well as actual conflicts of interest.
- Ensure that responsibility for handling related media or governmental inquiries is assigned to appropriately trained and informed designated representatives.
- Consult with the council's tax accountant and employment counsel when developing and implementing your process.

Assistance from GSUSA

Several departments at GSUSA stand ready to assist you in this endeavor. They include Council Governance, Council Finance, HR Consulting, and Compensation. Contact information for each department follows:

- Compensation—Almesha Pegues, Director (apegues@girlscouts.org)
- Council Finance Consulting—Cheryl Olson, Director (colson@girlscouts.org)
- Council Governance—Liz Swanson, Director (lswanson@girlscouts.org)
- HR Consulting—Sharon Czebotar, Director (sczebotar@girlscouts.org)

In order to assist you in getting started, we have attached a worksheet template. Please feel free to adapt and customize it to your individual council's needs.

Human Resources Consulting
September 2009

Executive Compensation Worksheet

Position	
Incumbent (disqualified person)	
Contract Term (if applicable)	

Elements of Compensation Package

Component	Description	Amount
Salary Amount		
Bonus Amount		
Welfare Benefit Plans		
Fringe Benefits		
Perquisites		
Deferred Compensation		
Below-Market Interest Loans		
Expense Allowances Outside Accountable Plan		
Severance		
Other		

Listing and Description of Comparability Data Utilized **(surveys, reports, etc., including full documentation of data sources)**

Data Source	Description of Source

Comparability Table by Type and Source

	Source A	Source B	Source C	Source D
Type				
Salary				
Bonus				
Welfare Benefits				
Fringe Benefits				
Perquisite				
Deferred Compensation				
Interest Loan				
Expense Allowance				
Severance				
Other				

Executive Compensation Worksheet

Location of Source Data File

Total Compensation Package Proposed (all elements)			Maximum Total Compensation Package Per Comparable Data (all elements)			Approved Total Compensation Package (all elements)	
Type	**Amount**		**Type**	**Amount**		**Type**	**Amount**
Salary			Salary			Salary	
Bonus			Bonus			Bonus	
Welfare Benefits			Welfare Benefits			Welfare Benefits	
Fringe Benefits			Fringe Benefits			Fringe Benefits	
Perquisite			Perquisite			Perquisite	
Deferred Comp			Deferred Comp			Deferred Comp	
Below Market Interest Loan			Below Market Interest Loan			Below Market Interest Loan	
Expense Allowance			Expense Allowance			Expense Allowance	
Severance			Severance			Severance	
Other			Other			Other	

Date Approved	

Members and Others Present for Voting

Member Name	Title or Position

Others Present	Title or Position

Executive Compensation Worksheet

Comparability Data Relied upon by Approving Body and Source

	Source A	Source B	Source C	Source D
Type				
Salary				
Bonus				
Welfare Benefits				
Fringe Benefits				
Perquisite				
Deferred Comp				
Below Market Interest Loan				
Expense Allowance				
Severance				
Other				

If Applicable, Members with Conflict of Interest and Nature of Conflict

Name	Description of Issue and Action Taken

Documentation Prepared By and Date	
Date of Board Approval	
Location of Minutes	

Executive Compensation

February, 2010

Girl Scouts

Legal Framework

- **501(c)(3) Organizations: law requires that "no part of the net earnings of [the exempt organization] inure to the benefit of any private shareholder or individual..."**

- **This means that a tax-exempt charitable organization may not improperly transfer financial resources to any insider.**

Executive Compensation: Board Roles and Responsibilities

Board's Role in Setting Executive Compensation:

- Current environment
- Board's responsibility for determining executive comp
  - ➢Mission and strategy
  - ➢Fiduciary stewardship
  - ➢Legal responsibilities

Executive Compensation: Board Structure

Structuring Your Board to Determine Executive Comp:

- Task group
- Full board
- Composition
  - ➢Knowledge/Skills
  - ➢Disinterested members
- Role of staff

Executive Compensation: Board Process

Formal Process for Determining Executive Compensation:

- Appoint task group and determine charge
- Compensation philosophy
- Determine who is likely to be treated by IRS as "disqualified person"
- Align with annual review process
- Marketplace
- Legal requirements
- Community and public scrutiny
- Providing rationale and documenting process

Executive Compensation: Drafting a Compensation Philosophy

- **Compensation philosophy: guiding principal and critical foundation of a council's values; drives compensation decision-making**
- **Important to identify and document council position on:**
  - **Total compensation package**
    - **Base pay**
    - **Benefits**
    - **Incentives**
  - **Peer group**
    - **Non-profit**
    - **For-profit**
    - **Local area**
  - **Pay-for-performance position**
- **Guidelines and policies should be created to complement the philosophy (e.g., merit increases and promotional guidelines)**

Executive Compensation: Creating a Compensation Program

When establishing a compensation program for your council:

•First step

- Develop philosophy
  - Based on the council's mission, core business strategy and future goals
  - Including the council's market position (e.g. middle of the market)

•Second step

- Go to the marketplace
  - Compare council pay to defined peer group

Executive Compensation: Customized Analyses

- Focus on pay trends in the Girl Scout world and non-profit arena
- Take a customized approach looking at other organizations of comparable:
- Budget size
- Membership size
- Geographic area
- Ensure both market competitiveness and compatibility with the council's budget
- Update regularly

Executive Compensation: External Market Sources

Market Sources include:

- Council Benchmark Compensation Survey (CBCS)
- Surveys conducted by well established consulting firms
- Other non-profits
- General industry
- Surveys sponsored & conducted by other employers

GSUSA Compensation Resources

The compensation team consults to councils in the following areas:

- Creation of a compensation philosophy
- Development of customized salary structures
- Guidance through job slotting (e.g., internal equity evaluations)
- Development of hiring ranges
- Guidance in making exemption status determinations
- Development of compensation administration guidelines
- Creation and administration of customized surveys

Board Action Needed

Motion:

That the board approve the Executive Compensation Philosophy and Executive Compensation Task Group Charges as presented.

The following slides provide additional information to support the Executive Compensation Philosophy

“Excess Benefit Transactions”

- Excess Benefit Transaction: excessive economic benefit to an organization insider (aka “Disqualified Person”)
  - Occurs when value of benefit exceeds value of what Disqualified Person provides to organization in return
  - All forms of cash and non-cash compensation can qualify
    - May include sale/transfer of property, loans, etc.

“Disqualified Person”

- Disqualified Person: individual who is, or in the 5 years before the transaction has been, in a position to exercise *substantial influence* over the organization’s affairs
  - Includes:
    - Voting board members
    - Individuals responsible for implementing decisions of board
    - Individuals responsible for organization’s finances
  - Also includes the Disqualified Person’s family members and entities controlled by a Disqualified Person

Creating a Presumption of Reasonableness

- An organization can create a *rebuttable presumption* that compensation is reasonable if all 3 conditions are met:
  - Condition 1: Comp package is approved in advance by an authorized body
    - Task Groups
    - Avoid conflicts of interest
  - Condition 2: The task group (or other authorized decision-makers) rely on appropriate information
  - Condition 3: Comp decisions are adequately documented

Designating Benefits as Compensation

- Failure to designate benefits as compensation will result in treatment as an excess benefits
- Compensation can be designated in a variety of ways:
  - Organization may report the benefit as compensation on its tax return
  - The Disqualified Person may report the benefit as compensation on his/her return; or
  - The parties can produce a signed employment agreement detailing the individual's compensation

Possible Penalties for Excess Benefit Transactions

- Reversal of the transaction to the extent possible
- 25% tax on the excess benefit; possibility of additional 200% tax if excess benefit is not corrected
- Possible 10% tax on individual managers who *knowingly/willfully* participate in transaction
  - $10k max. penalty (in aggregate)
  - Reliance on professional advice may insulate from liability
  - If meet 3 conditions above, ordinarily no knowing/willful participation
- Ultimately, possible revocation of 501(c)(3) designation

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United Way Agency Partner

DRAFT

Girl Scouts of Western Ohio Compensation Philosophy: Principles, Strategy, Process

Compensation Philosophy:

Girl Scouts of Western Ohio is committed to attracting, rewarding, motivating, and retaining the highest quality candidates and employees possible, needed to accomplish the council's underlying mission and core business strategy. In meeting this objective, the council is committed to offering competitive cash compensation levels and health and welfare benefits that meet the basic needs of its employees. The package targets the median or 50% percentile of remuneration offered by an appropriate and comparable peer group of non-profit and for-profit organizations located within a reasonable distance of the council's headquarters and/or regional offices and with whom the council competes for talent.

While this is the council's philosophy, it is predicated on the council's economic realities and its ability to ensure its short and long-term financial stability. The council is committed to staying in compliance with applicable federal and state laws and regulations. The council will review this philosophy on a regular basis to ensure alignment with ongoing council goals, objectives, and financial situation

Principles

The following principles apply to the implementation of Girl Scouts of Western Ohio's compensation philosophy:

1. Girl Scouts of Western Ohio will develop and communicate a compensation philosophy that attracts, motivates, and retains a workforce that helps achieve the council's overall goals and objectives.
2. Girl Scouts of Western Ohio will link individual and/or group performance and rewards in a fair and equitable manner.
3. Girl Scouts of Western Ohio will recognize and comply with applicable federal and state laws and regulations.
4. Girl Scouts of Western Ohio will ensure short and long-term financial stability of council salaries and rewards.
5. Girl Scouts of Western Ohio will review compensation policies and strategies to ensure alignment with ongoing council goals, objectives, and financial situation.

Strategy

Girl Scouts of Western Ohio's management of compensation seeks to achieve balance and flexibility in determining employee pay by ensuring:

1. External competitiveness: The council's salaries are competitive with not-for-profit and appropriate for-profit organizations of comparable size, job responsibilities, and in geographic areas in which the council operates.
2. Internal equity: The council's positions are evaluated using the required knowledge, skills, duties, and responsibilities to position them in the salary structure alongside other jobs of comparable impact to council operations.
3. New hire pay: A candidate's experience and accomplishments are evaluated in setting a target hiring salary within the salary range.
4. Progression through the salary range: Employee job performance is evaluated as a primary factor in determining salary increases, progress through the salary range, and career advancement. Note that other factors may impact movement through the range.
5. Budgetary Priority: Annual pay increases are sustainable within the council's short and long-term financial situation.

Process

The following process will be used in the administration of the compensation philosophy:

1. Job descriptions are developed and reviewed regularly for all positions.
2. External salary survey data from not-for-profits and appropriate for-profit organizations of comparable size, job responsibilities, and within appropriate geographic areas for the position are acquired regularly.
3. Appropriate fiscal year merit increases are determined that can be supported by the operating budget.
4. Performance management guidelines are developed for staff on an annual basis. Merit guidelines are developed for staff when merit increases can be supported by the operating budget.

Sources for Benchmarking:

The following sources will be used in the benchmarking of salary ranges and merit increases:

1. GSUSA salary schedule
2. Clark, Shaffer, Hackett Annual Compensation and Benefits Survey
3. Barnes Dennig Compensation and Benefits Study of Not-for-Profits Organizations
4. Employers Resources Association Compensation Survey for Non-Profits
5. United Way Compensation Survey(this is not done annually)