



Compensation for Nonprofit Health Care Board Members: The Right Path or a Minefield?

REPRINT OF *INQUIRY* ARTICLE, SPRING 2012

In summer 2011, Massachusetts Attorney General Martha Coakley publicly challenged the appropriateness of the board compensation practices of the state's four major nonprofit health plans, and promised to seek legislation that would grant her the authority to approve or deny future board compensation practices of these plans. In response, the board of one of those plans, Blue Cross Blue Shield of Massachusetts, considered seeking a change in its ownership status from a public charity to a member-owned mutual company to avoid such regulatory intervention in the future. It ultimately decided against seeking such a change because of more pressing issues, and it indefinitely suspended board compensation. At about this same time, down the Atlantic Coast, local media were questioning the board compensation practices of the nonprofit Blue Cross Blue Shield of South Carolina.

In fall 2011, the Governance Institute released the results of its most recent compensation survey showing that 15 percent of the 660 nonprofit hospital and system respondents were compensating some or all of their board members, up from 10 percent in 2009. Government-sponsored respondents were found to be the most likely to compensate some or all of their board members, and nonprofit health system respondents were found to compensate their board chairs more than others (25 percent at \$30,000 to \$50,000 and 25 percent at more than \$50,000).

Are there circumstances under which it is appropriate for a nonprofit health care organization to compensate, or to consider compensating, some or all of its board members? Would board members receiving some level of compensation tend to take their board assignments more seriously? If compensation is deemed appropriate for some board members, should all be compensated to at least some degree? Where a board decides that all its members should receive some compensation, should individual board members be permitted to opt out?

These are among the issues explored in the following discussion, another in *Inquiry's* ongoing Dialogue series, co-sponsored by the Alliance for Advancing Nonprofit Health Care to provide a variety of voices on important nonprofit health care issues. The panelists for this discussion, held on September 27, 2011, were: **Kenneth (Ken) Ackerman**, chairman of Integrated Healthcare Strategies in Minneapolis, Minnesota; **Douglas (Doug) Clark**, retired president and CEO of Excelsa Health (Pennsylvania), now residing in Greensburg, Pennsylvania; **Michael (Mike) Cascone**, retired president and CEO of Blue Cross Blue Shield of Florida, now residing in Jacksonville, Florida; and **William (Bill) Kreykes**, former board chair of the Trinity Health System (Michigan) and retired president and CEO of the Lifespan Health System (Rhode Island), now residing on Cape Cod in Massachusetts. **Bruce McPherson**, president and CEO of the Alliance for Advancing Nonprofit Health Care in Washington, D.C., moderated the discussion.

Bruce McPherson: *Under what circumstances, if any, do you feel it is appropriate for a nonprofit health organization to compensate—or at least to consider compensating—some or all of its board members? Let's assume that the organization has the financial resources to do so.*

Bill Kreykes: I think it depends very much on the nature of the organization and what that organization is trying to accomplish with its board. If it is a large health care system, for example, with hospitals across the country and with a well-developed plan and formal search process to recruit on a national basis board members with different types of expertise or other talents, then I think it is very appropriate for that kind of a board to fully consider compensating all of its members.

Another factor to be considered is the amount of time that a board member needs to spend to be fully and effectively performing in his or her role. I've been on a board that met quarterly, in the central part of the country, with meetings generally lasting a day and a half each, starting in the afternoon and going through the next day. Some board members from other parts of the country were literally devoting two if not three days for each of the board meetings—much more than is required for a board meeting of a local community hospital.

Mike Cascone: I am not generally supportive of board compensation. The only circumstance where I can see board compensation warranted is where a certain talent is required on the board that is not readily available on a volunteer basis. In my view, such a circumstance will be very rare, because most communities that are big enough to have a nonprofit health care institution or nonprofit health plan should have available all the talents it needs. Where such a circumstance does arise, I think that a relatively small amount of compensation would be appropriate, but just for the individual filling that void.

One of my major concerns is that for those nonprofit health care organizations that compensate members and enjoy tax exemptions, the opponents of such exemptions will use board compensation as one more illustration of how the distinction between not-for-profit and for-profit has become blurred and why those exemptions are no longer warranted. Moreover, when those tax-exempt organizations that compensate board members seek donations, they may not see every potential donor refuse to give, but a large portion of them are likely to give less.

Also, if a nonprofit health care organization is using some of its resources to pay board members, a portion of those resources will be lost to the community because that compensation will be taxed as income to those board members by federal and state governments.

Ken Ackerman: As I've thought about this subject over the last 15 years, I've come full circle and tend to lean toward Bill's view—that it depends on the culture and circumstances of the organization and the community or communities it serves. I don't think there is any right or wrong answer for all nonprofit health care organizations.

But I feel strongly that any board that wants to consider it should do so very carefully, through a very deliberate decision-making process. It needs to start with a reputational risk assessment. Is the board willing and able to take the heat if there are any challenges from the media, the state attorney general, or other sources?

Doug Clark: I think you can make a case for board compensation in very large, multistate or national nonprofit health care organizations, as Bill has suggested, but there are relatively few of them. You can make a case for some compensation in other situations as well, where the time commitments of the chair of a board are substantially greater than those of other members of the board.

However, most of the board members I have talked to in medium- and large-sized hospitals and health systems about this issue were even somewhat offended by the question. Most view the time they spend on a board matters as a philanthropic gift. They say they don't need the money, would probably give it back anyway, and that's not why they serve. Moreover, back to Ken's point about reputational risk assessment, it may be very difficult to defend any board compensation, particularly if many of the board members are well-to-do and/or if the organization is simultaneously sending out seemingly conflicting messages to the public about other initiatives, such as fundraising or employee layoffs. In the local environment, particularly for a charitable organization, it can be a very slippery slope in terms of government relations, public relations, employee relations, and fundraising. Each board must ask itself if compensation is really worth the risks.

Ackerman: Information is very sketchy right now on the nature and extent of board compensation and on how much time is spent by board members of various types of nonprofit health care organizations. At least for nonprofit health care institutions, there will be better data for analyzing trends because of recent modifications in the governance and compensation reporting requirements on the Form 990.

There is little doubt, however, that the prevalence of board compensation in hospitals is skewed to the larger organizations—the type that Bill is describing—above \$2 billion in revenue and 2,000 beds. They are tending to recruit

the best in governance from around the country and are moving towards compensation. When you consider the enormous amount of time that some spend on their governance duties, their compensation would translate to a very low hourly rate.

On the other hand, there are a number of prestigious organizations that have national boards and do not compensate other than reimbursement of travel expenses. Will that change? Who knows?

Cascone: Substantial time commitments are required on the five to 10 boards I have served on at any one time—primarily boards of charitable and other nonprofit organizations. What I have found most time consuming are the committee assignments. You may end up on three committees of a particular board that each require more homework and meeting time. Committee assignments can consume up to three to four days a month if meetings are monthly.

Let me iterate, however, that my concerns with board compensation are unrelated to how much time is involved.

Kreykes: I know a number of boards that factor in the amounts of time consumed during and outside the meetings of the board, standing committees, ad hoc committees, as well as the time consumed in leadership roles in determining whether and how to compensate board members. When I chaired the Trinity Health board for three years, I probably spent 10 percent to 20 percent of my time on some activity related to that system.

McPherson: *Do you feel that a board member of a nonprofit health care organization who receives some level of compensation will tend to take his or her board assignments more seriously than one who does not?*

Clark: That may depend on the individual, because as a CEO I always had one or two board members who would bring up the issue from time to time; however, I don't think it is true as a general rule. In my experience, most take their assignments very seriously, whether because of the prestige involved, personal ethics, and/or their passion for the organization and its mission. Of course, those who serve in the leadership positions on the board tend to be the most committed of all.

Ackerman: Bruce, I think there is truth in what Doug is saying, but anecdotally, I have not ever talked to a CEO whose board is compensated who would want to stop it. They feel that there have been more up sides than down sides to board compensation. For instance, one told me that he felt less reluctant to call on his board members for more help because they were compensated.

Kreykes: On almost every board I've served, I have generally found my fellow board members to be very dedicated and committed individuals, and compensating them or not compensating them was not a major factor in their level of commitment. I do believe, however, as Ken suggested, that compensation can provide a little added comfort to the CEO in calling on board members for some extra help. And it may cause at least some board members to think twice about missing a board meeting.

But the primary benefit I see in compensating board members is to give them a tangible expression of appreciation for their time and hard work—a tangible recognition of the value they bring to the organization.

Cascone: As productive human beings, I believe we all have a responsibility to give something back to our communities, however defined. Of the total population of board members serving nonprofit health care organizations, I would expect that more than 90 percent of them are doing it as a community service and are getting a lot of self-satisfaction from it. Those I've talked to would be insulted if anyone were to imply that their level of attentiveness would be improved with compensation.

Kreykes: I don't disagree with that perspective, Mike, but I think a distinction can be made between a board member serving a community-based organization and one serving an organization that is not part of a community—a national or multistate enterprise. I served on the board of the local hospice, and in no way would I consider being compensated for that role. As you said, Mike, that was part of my community service. On the other hand, I was recruited to serve on the board of a nonprofit hospital in another state before it merged with Trinity Health, and I had no affiliation with that community whatsoever. Similarly, the majority of the board members who were recruited

at Trinity Health had no previous relationship with any of the Trinity Health institutions or communities. They were recruited for specific expertise or other talents to serve on the system board, and I don't consider their service on that board to have been community service.

McPherson: *Where compensation is deemed appropriate for some board members, should all be compensated to at least some degree?*

Cascone: I would not support compensation to everyone. As I noted earlier, I think it would be a very rare situation where any board member compensation is needed. That said, I'm aware of a few instances where selective compensation is happening, and in those cases it is well understood and well accepted by the other board members. For instance, the treasurer of a board I know about had many administrative duties not normally handled by a board, and that board member was compensated—but not a very significant amount—as a token of appreciation for his extra duties.

Kreykes: If you compensate selectively, you have to have very clear criteria and a solid rationale. Is it fair not to compensate a housewife with young children who has to pay babysitters, while compensating a lawyer for time away from practice? It can get very sticky.

Clark: It sure can. As nonprofit hospitals add more physicians to their boards, who have to take time away from their practices, I envision increased pressure from them to be compensated. But if you get above one or two being selectively compensated, then the board politics get tricky and I think you would have to compensate all of them.

Ackerman: If you have decided to be selective about it, you'd better be very careful to avoid a slippery slope that takes you to a bad place. I would be in favor of all or nothing when it comes to board compensation. Where there is compensation, the amount might vary for the reasons mentioned earlier.

McPherson: *Where a board decides that all of its members should receive some amount of compensation, should individual board members be permitted to opt out?*

Cascone: In organizations I'm familiar with that compensate all board members, they are not allowed to individually opt out.

Clark: I think that board members not wanting the compensation should just donate it back into the organization in some way rather than opt out. An "opt out" only serves to exacerbate any potential public relations problems with board compensation.

Ackerman: Good point, Doug. I am aware of board members in some organizations who donate their director compensation back to the organization.

Kreykes: I haven't been confronted with this issue, but my gut reaction is in line with the thinking of all of you on this.

McPherson: *Where there is compensation, what form or forms do you think it should take?*

Clark: From a public perspective, it would be advantageous to stick as closely as possible to a flat fee. It's simple and likely to be better understood and received externally.

Kreykes: I experienced one approach that I felt was very effective. All board members received a flat fee, as Doug suggests, but the board chair and the standing committee chairs received an add-on amount for their extra work. Everyone understood the plan and felt it was fair and appropriate.

Ackerman: I agree. The simpler the compensation approach, the better. When you get into additional features, like per-meeting fees, you create the potential for some board members to try to "game the system," such as by trying to persuade the rest of the board to have more meetings to discuss issues.

Cascone: In those rare instances where I think compensation might be appropriate, I think a flat fee makes sense. However, I'm aware of a number of organizations that favor both a flat fee and meeting fees; those organizations only compensate the board chair and committee chairs.

McPherson: *How does a board go about determining what is reasonable compensation, once a decision has been made to compensate some or all of its members?*

Kreykes: First, I think you need to engage a compensation consultant who has surveyed, or who will survey, comparable organizations' board compensation practices. If the organization is a nonprofit, I recommend that it stay within the norm of what other comparable nonprofits are doing so that it has a defensible methodology and database, should the compensation come under public scrutiny.

Ackerman: I agree, Bill. The board should follow the same steps of the "rebuttable presumption of reasonableness" process that the Internal Revenue Service recommends for the governance of executive compensation: engagement of an independent third party that gathers peer comparator data; independent synthesis and presentation of the data; and careful, timely documentation of the decision and rationale.

Cascone: Even with the use of an independent third party consultant and an accurate database, my experience suggests that such a practice is inflationary over time. Nobody wants to say they're in the lower 50th percentile, much less the lowest quartile. People will naturally want to be paid at least at the median, if not more.

More importantly, at least with executive compensation you have the board providing oversight. Who provides the oversight over board compensation? The board will be perceived by the public as having an inherent conflict of interest, exercising self-dealing rather than good governance.

Maybe there should be an independent national group, a neutral third party such as the Alliance for Advancing Nonprofit Health Care, to serve as an oversight group.

Kreykes: My experience with this has been different, Mike. In the years I served on compensated boards, we did not experience the kind of board compensation "creep" you are talking about. The level of compensation was stable, with no pressures within the board to change it.

Clark: I would still be concerned that, over a period of time—maybe five to ten years—a psychology could come into play where board members who are working hard or even harder would want more compensation.

Ackerman: Our firm has seen some boards use an independent group, composed of representatives of the community, to advise them on whether and how much to compensate board members. That's an interesting concept.

McPherson: *Setting aside the structure and process issues surrounding determination of the reasonableness of board compensation, can any of you provide a ballpark range of compensation that you think would be considered reasonable and defensible?*

Ackerman: The survey data I've seen, Bruce, suggests that for those nonprofit health care organizations with less than \$500 million of revenue that are compensating board members, the compensation ranges anywhere from a few thousand dollars all the way up to \$20,000 a year per member, with the latter being very unusual. For larger organizations, the range is typically \$25,000 to \$50,000 and higher, with add-ons for the board and committee chairs. Some also pay meeting fees.

These kinds of figures are modest in comparison to what for-profit health care companies are paying their board members, which is reassuring. Whether that will change over time, however, is a reasonable question.

Kreykes: I have not seen any survey data over the past several years, but my recollections are along the lines of the ranges that Ken just cited.

Cascone: I don't have any hard data, but if the annual level of compensation is as much as or more than what lower-paid employees in the organization are making, then I think you have a very difficult sell within your organization. While in most cases employees are unlikely to visibly protest in those situations, in a few cases I have witnessed one or more employees raising the issue with the media.

Clark: Building on Mike's point, I talked to a board member of a health system who served there for 50 years. He told me that he opposed board compensation because, with his income, he wouldn't otherwise be able to look a housekeeper or a dietary worker in the eye.

Ackerman: I think those are very valid concerns, especially for community-based nonprofit health care organizations. The dynamics are very different for a large regional or national organization.

McPherson: *As you look ahead, taking into account both the heavy demands being placed on the boards of nonprofit health care organizations and greater public access to data on board compensation, do you see the prevalence of board compensation by nonprofit health care organizations increasing, decreasing, or staying about the same?*

Cascone: I certainly don't see it decreasing. How many boards or executives would want to reverse themselves, openly admitting to a mistake? If they succumb to public pressures to change their policy, they will come across more negatively than if they were able to defend it. Moreover, if they admit it was a mistake, are they going to require everyone to return all of the past compensation?

Clark: As the demands on system boards continue to mount, I think more will gravitate to board compensation, especially for those experts whom they feel they need to attract from outside their locales.

Ackerman: We're seeing more and more consolidation, especially of nonprofit hospitals and systems, and as that occurs I think that we will continue to see some increase in the prevalence of board compensation in large systems. According to a recent Modern Healthcare survey, there is already some up-tick in board compensation in the multibillion-dollar systems, although it's too early to call it a trend.

Kreykes: I agree. I think we will see growth in system size and the larger ones will do more national recruiting to secure the kind of expertise they need to achieve their missions. To attract the expertise they need, compensation will be a factor.