

# An Examination of Issues Surrounding Nonprofit Executive Salaries: 2010-2017

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## Abstract

This paper examines issues related to executive compensation in the nonprofit sector for the period since the last recession, 2010-2017. We explain why nonprofit executive compensation matters in terms of charitable giving in the United States. We discuss what is meant by the terms “nonprofit” and “tax-exempt”; the requirements that an entity must meet in order to achieve each respective designation; and why the two terms are not interchangeable. We examine different types of tax-exempt entities and how tax-exempt status aids organizations in raising funds from the donating public. We focus on the requirements for obtaining, and maintaining that status as a regulatory tool. We review the significant expenses for a tax-exempt non-profit and note how commercial entities face similar expenses. We illustrate how the particular expense of executive compensation is inherently different for a tax-exempt non-profit than for profit-making enterprises. We explain the factors that determine executive salaries in the former and the components of this compensation. We review the federal and state regulations governing tax-exempt nonprofit executive salaries and guidelines offered by non-governmental entities. We note that research (Balsam and Harris 2014) indicates a negative correlation between the level of disclosed executive compensation and the percentage of donations that a tax-exempt nonprofit receives. We discuss and analyze the compensation for chief executives at certain such nonprofits which have been highlighted by the mainstream media, the source of nonprofit information most easily accessible to the vast majority of donors to such entities. We conclude by highlighting why donors should have a voice in the determination of a tax exempt’s nonprofit executive compensation.

## 1. Introduction

Non-profits are a multi-billion dollar sector of the United States economy and employ over 10% of the U.S. workforce. Yet many people do not know the nuances of how this industry functions. In fact, there are perhaps few other areas about which the general public has such a high level of misconception as non-profit organizations. The lack of knowledge ranges from the types of organizations that can be called “non-profits” to the activities in which such entities engage. It is, however, important for the public to have a strong understanding about such groups because they exist in many different industries and impact many aspects of the daily lives of people in the United States.

For example, many people think all non-profits are what are commonly referred to as charities. While these type of “mission-based” entities are often the most obvious in terms of their fundraising particularly during the holiday season, they are far from the only type of non- profits in existence. Many people might be surprised to know that fraternal organizations, political action committees, labor unions and even condominium boards are also considered non-profits.

Nonprofit organizations are given favorable tax status by the federal government and by many state and local jurisdictions because they serve “the public good”. Unlike commercial corporations, these entities should not, in theory, benefit a select group of owners but rather a broader base who have no ownership interest in the organization itself and who do not influence its activities. In other words, the work of these groups should be “selfless”. That is why at every stage of a nonprofit’s existence, the subject of its executives’ compensation is a critical issue both for the organizations themselves and also for government entities and the donating public.

Due to the nature of their work, many nonprofits receive large government, state and local grants to carry on their missions. In addition, many people donate their personal funds to these entities; as do many commercial enterprises.

Donations made to some of these entities can sometimes be fully deductible on the federal income tax returns of the respective individual donors or commercial entities which make them.

It is because nonprofits receive such funding from a variety of public and private non-owner sources that how they spend their funds is closely monitored by the government and the public. The issue of what are termed “general and administrative” expenses is an area of particular interest. For many non-profits, a large portion, if not the largest portion, of these so called “G/A” expenses are related to employee salaries, and chief among them executive compensation. Executive compensation can be thought of as an ethical issue when salaries reach levels that the public would deem “excessive” because it has implications for the organization’s culture and its integrity in allocating resources. In general, an executive salary of \$1M or above would be in the category the public might deem “excessive”.

This paper examines the issues surrounding compensation for executives of nonprofit entities organized under section 501© (3) of the federal Internal Revenue Code and why it is an important subject to comprehend and examine. It begins by stressing the importance of this sector to the U.S economy and reviewing what is meant by the terms “nonprofit” and “tax-exempt” and what entities are included in each group. We then proceed to look at the factors necessary for an entity to become a tax-exempt nonprofit. This is followed by a review of the sources of funding these groups receive and the issues that are of concern to the public related to these funding sources. Next, we examine how these issues influence the discussion of pay and benefits for non-profit executives; who determines a nonprofit executive’s salary; and why it is a necessary examination for anyone who is associated with nonprofit organizations or who would like to donate to a nonprofit. Lastly, we provide some examples of nonprofits which give their executives large salary and benefit packages during the period 2010 to 2017, the timeframe after the last recession. .

## 2. Why Nonprofit Executive Compensation Matters

In 2016, the last year for which there are available statistics, charitable giving grew to an estimated \$390 billion, the third year in a row that total giving increased to a record level (Charity Navigator). This shows the substantial role that charities play in our society, a role which shows every indication of growing.

Charitable giving in 2016 represents an increase of 2.7% in current dollars (1.4% in inflation adjusted dollars) over 2015 levels and represents 2.1% of U.S. GDP. In fact, charitable giving has increased in the United States in all but three years (1987, 2008 and 2009) in the 40 years since

1976. During that time, the average year-to-year change in total donations was an increase of \$8.96 billion (in current dollars). That makes the 2015-2016 current-dollar change in total giving much larger than the 40-year average. Total giving as a percentage of GDP was 2.1% for three of the four years, 2013–2016.

As astounding as the magnitude of these numbers might be, it is perhaps more surprising that majority of these donations came from individuals. Specifically, individuals gave \$281.86 billion in 2016, accounting for 72% of all giving and representing a 3.9% increase over 2015. This is in keeping with multi-year trends because historically, donations from individuals account for over two-thirds of all charitable giving. If you add in gifts from bequests, then the category accounts for nearly 80% of all donations. In other words, the vast majority of annual charitable giving is neither generated by corporations nor large foundations but by individuals.

These 2016 donations were disseminated among various charities as follows:

- Giving to Education charities was up 3.6% to \$59.77 billion (15% of all donations).
- Donations to Human Services charities were up 4.0% to \$46.8 billion (12% of all donations).
- Foundations saw an increase of 3.1% to \$40.56 billion (10% of all donations).
- Health charities experienced an increase of 5.7% to \$33.14 billion (8% of all donations).

As nonprofits generate more funds, so also does the compensation their executives receive increase. The Nonprofit Quarterly, reports that during the year 2014, 2,700 employees of charities received an annual compensation of more than a million dollars (Wyland 2017). Also during that year, five of these nonprofits (four of which were healthcare organizations) paid their CEOs salaries of \$10 million or more (Wyland 2017). The issue of nonprofit executive compensation is particularly controversial, according to Charity Navigator because the top 1% of the charity executives run organizations which receive 86% of donated funds.

The general public has a vested interest in knowing how much charity executives receive in compensation because they are the primary source of these charities’ funding. Due to the various benefits that are given to nonprofits to aid them in completing their missions, nonprofit executive salaries should not be viewed the same as those of commercial enterprise executives. In the end, when it comes to nonprofits, the public has “the power of the purse” and as such should be made aware of how much of their monies are spent in creating a very good quality of life for nonprofit executives.

### 3. Terminology Related to Nonprofits

When most people refer to an organization as a ‘non-profit’, they usually mean an entity such as the well-known American Red Cross, American Museum of Natural History, or American Cancer Society. These entities are charitable organizations to which people can donate money and that donation will be deductible on the donor’s federal income tax returns. While it is true that the definition of “non-profit” does apply to each of these entities, that definition does not by itself encompass all these characteristics. That is why it is erroneous to automatically label a non-profit entity a “501©” or a “tax-exempt” organization although many charitable organizations are organized as both a non-profit corporation and tax-exempt entity as is each of the entities mentioned above.

#### *Meaning of the term “Nonprofit”*

The term “non-profit” is a concept found within state law and refers to how a specific entity is incorporated in the state of its incorporation. This term is used to describe an organization that does not generate funds to benefit a particular entity individual or corporation but rather works to serve a public purpose. There are several examples of non-profits which would not be considered charities by the general public such as unincorporated associations, nonprofit corporations, charitable trusts and certain limited liability corporations (LLCs). All nonprofits are organized to serve a community need, further a mission, or promote a cause. Specific examples of such entities would be condominium associations, Memorial Sloan Kettering Cancer Center, and the National Organization for Women, respectively. The form (unincorporated association, nonprofit corporation, etc.) the organization takes depends on its purposed and is a decision to be made by the governing members of the particular non-profit.

Any group which decided to form a non-profit can do so in any state in which it chooses, not just the state in which its main offices are located. The formation is usually done under the auspices of the Secretary of State of the state of incorporation. It is usually accomplished by filing articles of incorporation or a certificate of formation. The date of approval by the Secretary of State’s office is the “birthdate” of the non-profit.

#### *Meaning of the term “Tax-Exempt”*

The term “tax-exempt” unlike “non-profit” is a concept found within federal law although there is an aspect to organizations that are tax-exempt which affects their taxation under state law. The exempt status releases or “frees” a non-profit from paying corporate income tax on any income which is generated from the activities that are substantially related to the stated purposes for which the group was organized. A “tax-exempt” entity is, therefore, a specific type of nonprofit which pays no federal income taxes for revenues generated as a result of activities which are in line with its exempt purpose.

This favorable tax status is granted in theory so that the entity can devote a maximum amount of its funds to furthering its purpose which the government believes to be for the good of its citizenry, not for the enrichment of a few. In fact, the IRS defines a non-profit as “an entity whose income is not used for the benefit or private gain of stockholders, directors, or any other persons with an interest in the organization” (Gaver and Im 2014). In some sense, these entities are granted this tax freedom so that they can carry on work that the government might have had to do if the nonprofits did not exist. In return, such nonprofits are expected to comply with government laws and regulations. The idea of excessive executive compensation can be thought of a violation of the “private gain” principle because it is enrichment of an employee who has an interest in the organization

### 4. Types of Tax-Exempt Organizations

Tax exempt organizations are granted their exemption under Section 501© of the Internal Revenue Code. This section has several subsections which enumerate the various types of nonprofits that achieve this beneficial tax position. For example, Section 501© (3) governs charitable, educational, and scientific organizations. This section also governs the activities of recreational clubs, civic leagues, credit unions, and small insurance companies. Section 501© (4), on the other hand, applies to advocacy groups and Section 501© (6) relates to boards of trade and business leagues. The majority of tax-exempt organizations are organized as the first designation and are informally called “501© (3)'s”.

For each type of 501© entity, there are additional requirements on how the group can operate and in what kinds of activities the organization can engage. For 501© (3) entities, the IRS exemption guidelines require the following:

An organization must be organized and operated exclusively for exempt purposes set forth in section 501© (3), and none of its earnings may inure to any private shareholder and individual. In addition, it may not be an action organization, i.e. it may not attempt to influence legislation as a substantial part of its activities and it may not participate in any campaign activity for or against political candidates.

The favorable tax status granted to these entities by the federal government is not the only tax-related benefit they receive - many states grant them some form of tax freedom under state law. Nonprofit organizations with 501© (3) tax-exempt status automatically receive tax freedom from paying state taxes in twenty states. These are: Alaska,

Colorado, Connecticut, Hawaii, Idaho, Illinois, Kansas, Louisiana, Michigan, Mississippi, Missouri, Nebraska, New Mexico, North Dakota, Oklahoma, Oregon, South Carolina, Virginia, West Virginia, and Wisconsin. Many other states make achieving tax-exemption in their respective states relatively simple to obtain. Federally tax-exempt charities in New York, for example, need only notify and provide the appropriate documents from the Internal Revenue Service to New York State Attorney General's Office and they will receive tax-exempt status in New York State.

The IRS further bestows upon 501© 3 organizations a built-in fundraising tool – donations to 501© (3) tax-exempt organizations are fully deductible from the donor's federal income tax return up to 50% of the donor's Adjusted Gross Income (AGI). This is what is commonly referred to as "charitable giving". This is done to give people an incentive to donate money to these charities so that they charity will be able to continue providing for the "public good". Many states also exempt such donations from the taxpayer's state tax returns as well.

This public purpose of these entities and the benefits given to these groups to further such goals come with a set of reporting and filing requirements that show both government agencies and the donating public that the entity is keeping in line with its exempt purpose. Failure to either file the appropriate documentation, failure to make the mandatory disclosures on a timely basis or failure to make them at all can result in the nonprofit losing its exempt status at least temporarily.

### **5. Achieving Tax-Exempt Status**

As noted above, because the tax-exempt status is such a boon to nonprofits, their operations are subject to a high level of oversight. The Form 1023 is one such example – it is required to be filed within the charity's first 27 months after the nonprofit's inception. Failure to do so would require additional paperwork to be filed by the entity and might result in the IRS denying the entity's application.

A nonprofit organization begins the process of achieving tax-exempt status by filling this Form 1023 which is comprised of 11 sections. Certain nonprofits such as churches and religious organizations which are not also private foundations and which have less than \$5,000 in gross receipts do not need to file this form. Churches and religious organizations in general have less filing requirements than other types of nonprofits. These sections enumerate the documentation, policies and practices that an entity must undertake in order to qualify for tax-exemption. These are required to give the various levels of government and the general public assurance that the non-profit is adhering to its expressed charitable purpose and also provide mechanisms by which any external party can review that adherence.

The 11 sections of Form 1023 include noting the compensation and other financial arrangements with officers, directors, trustees, employees and independent contractors. Additional information sought by the IRS on this form includes specific activities in which the nonprofits engages; its history; and certain financial data. Again we see that the idea of how much money a nonprofit executive receives from the nonprofit is an area of interest for parties which are involved in the entity's functions. Although the tax exemption is granted after an organization is formed, once the status is achieved, it is effective as of the date of the organization's inception.

It should be noted that although a nonprofit only needs to apply for tax exempt status only once, in some sense, needs to, in essence, "actively" maintain that status by following the reporting and disclosure guidelines prescribed by the Internal Revenue Service. As with information required to apply for tax-exempt status, failure to provide the IRS with the required information by the required deadline can result in penalties for the nonprofit.

### **6. Maintaining Exempt Status**

As noted above, the granting of tax-exempt status to a nonprofit is only done after that entity has proven it will promote the public good and it is not something that is done lightly by the federal government. In order to continue to receive this favorable tax status, these charities need to adhere to certain rules and laws and report on their activities at least annually in order to maintain this status. This is done as a way to provide continual oversight both formally by government officials and informally by donors who contribute their own funds to the nonprofit that the entity is engaged in the activities for which it was given its tax-exempt status.

Equally important is a review of the organization's activities to determine that it did not engage any activities which the IRS deems prohibited for such entities. For example, activities such as supporting political candidates is a lifetime prohibition for 501© (3) charities. Certain organizations which have violated this ban have had their tax exempt status rescinded by the Internal Revenue Service.

The primary vehicle used to disseminate information about a nonprofit's activities on a fiscal year basis as well as adhere to the level of reporting and public disclosure that the IRS deems appropriate is the IRS Form 990. This is the nonprofit's tax return and is called an "informational return". Certain elements within this return are the subject of particular focus, one of which is the private benefit rule. Because nonprofits receive favorable tax treatment because they are in existence for "the public good", these entities must provide data that shows no one associated with the group

reaped a benefit exclusively for themselves. In the minds of many, the issue of excessive executive compensation can be thought of as a private benefit for executives at nonprofits.

These strict reporting guidelines help to demonstrate that the nonprofit is fulfilling its obligation in serving the public good. However, not every aspect of the nonprofit's activities is heavily regulated. Despite these rules, however, there exists a great deal of latitude in how the entity spends the funds it generates.

### **7. Significant Expenses for A Nonprofit**

One of the most significant misconceptions about nonprofits is that they function in ways dissimilar from how commercial businesses operate. While it is true that nonprofits and commercial entities differ in the area of ownership, each type of enterprises need to generate funds in order to further its set of respective goals. As Dan Summers, president of the Child Advocacy Center's board once noted. "I think there's a misconception that everybody in 'nonprofits is giving away their time and it's not like a business. But believe me, it's every bit of a business." (Section I)

For example, nonprofit organizations, like their counterparts in the commercial world face a myriad of similar expenses such as rent, electricity, telephone and salaries. Each group needs to achieve efficiency in the expending of funds to attain its respective goals. What resources are allocated to which areas is one that has to be accomplished by considering both external and internal factors. One area in which this is particularly true is the area of executive compensation.

It is true that both nonprofits and commercial enterprises need to pay their respective executives as compensation for the work these individuals do in furthering the entity's goals and ensuring its continued existence into the future. Very often, nonprofits that give their executives compensation packages which are thought to be excessive, they compare their organization to a for-profit entity and use the similarities between the two as justification for the nonprofit executive's high compensation. However, this argument is rational and has merit if we believe that for-profit and nonprofit are comparable when it comes to revenue generation. A strong argument can be made that they are not.

When a commercial company generates wealth, that money goes back to the shareholders who invested in the company with the hope of recouping and exceeding their initial investment. When a nonprofit generates funds, the people or entities providing those funds are interested in helping others not generating a profit for themselves. In fact, those funds are given to the nonprofit to be used for the betterment of the population which the nonprofit serves.

For example, a medical institution such as the Icahn School of Medicine, the CEO of which receives over \$1M in annual compensation could use some of those monies to perform a complicated surgery on a patient who might otherwise not be able to afford the operation. The same holds true of an educational institution which pays its President close to a million dollars a year. Part of that salary could be used to pay for the tuition of students who might not otherwise afford to attend that college despite having good grades.

In a time when healthcare costs are rising along with student debt, much of the donating public might agree that this strategy bears merit. And research indicates this approach might be the case as donations to some nonprofits with highly paid executives drop when the media reports on the level of its executive compensation. (Wyland)

### **8. Determination of Executive Salaries in Nonprofits**

When the CEO of a publicly-traded company receives a pay increase or an added postretirement benefit or another "perk" that decision is usually made by the company's Board of Directors or a subgroup therein. The Directors who sit on that Board are voted into office by the shareholders to represent their interest. In effect, increase in the salary and other benefits for the CEO of the company is coming from the owners of the company. That leads to a related question for nonprofits: Since nonprofits do not have owners, how would the CEO receive a pay increase. The answer is simple: From the Board of Directors. However, in the case of nonprofits, these Directors are often picked by the CEO or Executive Director of the entity and he or she has the ability to remove those Directors. Such was the case at Young Adults Institute (see below), a nonprofit which gave its executives exorbitant compensation packages and the actions of which led to some nonprofits in New York state being restricted in how much their executives can be paid from funds provided by the state.

### **9. Components of Executive Compensation**

It is important to bear in mind that when a nonprofit executive's "compensation package" is discussed, this term refers to more than just the executive's salary. Grant Thornton, the public accounting and advisory firm noted in 2010 that the trend in the constitution of such packages included items that were designed to offer nonprofit executives a high quality of life beyond just financial gain. The firm noted the following items in such packages for executives of educational institutions such as universities and colleges:

- Bonus plans, including many discretionary plans

- Housing and auto allowance or use
- Loans with forgiveness or below market rate features spousal or first-class travel
- Split-dollar life insurance
- Deferred compensation programs

In addition, Grant Thornton pointed that among all type of nonprofits, standard executive benefit plans may often provide two or more of the following supplemental (i.e. in addition to salary) benefits:

- Retention incentive (457(f))
- Supplemental Executive Retirement Plan (457(f))
- Employer funded 457(b)
- Supplemental life insurance
- Supplemental disability
- Post-retirement health care Supplemental long-term care.

The firm noted that the following comprised the most common non-salary benefits and perquisites provided by non-profit organizations for the top executive:

- Car/car allowance
- Additional vacation days
- Excess life insurance
- Reserved parking
- Private club membership
- Supplemental retirement and disability plans

Returning for a moment to the concept of donor intent, we can ask ourselves: At a time when many Americans are not saving enough for their retirement and dealing with increasing healthcare costs, do donors want their charitable dollars to go toward funding executives' postretirement benefits and healthcare?

#### **10. Federal Rules Governing Non-Profit Executive Compensation**

Despite the filing requirements outlined above, the IRS does not mandate specific governance policies regarding the structure of tax exempt organizations. And even though executive compensation is reviewed by the IRS when an entity completes its Form 1120, the government does not mandate the amount of compensation a nonprofit entity's executives should receive but does offer tax-exempt entities some guidance on the issue in Section 4958 of the Internal Revenue Code (IRC).

According to the IRC, a charity may not pay more than reasonable compensation for services rendered to a tax-exempt entity by its staff or its directors. Specifically, Section 4958 prohibits a tax-exempt organization from applying an "excess benefit transaction" with a "disqualified person". The excess benefit transaction would be deemed unreasonable.

A disqualified person is defined as any person having the power to exercise significant influence over the affairs of a tax-exempt, non-profit organization anytime during a five-year period following the date of the transaction that includes the compensation. Again, the principle driving this concept is the idea of personal enrichment; that is, a person of influence should not be able to generate excessive compensation for him or herself. The list of such people enumerated by the IRS include the following: voting members of the non-profit organization 's Board of Directors; its President; Chief Executive Officer or family members of the preceding disqualified persons. The term "family member" includes spouses, siblings, in-laws, children, grandchildren and their spouses. Additional rules apply to corporations and partnerships, as well as donor advised funds and supporting organizations, in which the above persons have an interest and which have dealings with the tax-exempt entity.

The word "reasonable" grants a great deal of latitude to the members of a nonprofit's Board of Directors. Under U.S. federal law, a "reasonable amount" is an amount that would ordinarily be paid for comparable services, by similar enterprises, under comparable circumstances. This definition does not limit the tax-exempt entity to merely comparing itself with other nonprofits, but allows the Board to evaluate its executives' compensations in terms of what for-profit groups are paying. Ultimately, the Board of Directors of a tax-exempt entity bears the responsibility of determining what is a reasonable compensation for each of its executives. The IRS does not prescribe the procedure by which this compensation will be determined, but it does regulate the persons who must comprise the Board of Directors. The main focus of the IRS with regard to executive compensation for nonprofits is the Board of Directors exercises a sufficient

degree of due diligence in deciding on this compensation.

### **11. Federal penalties for Excessive Nonprofit Executive Compensation**

Just as the Enron, WorldCom and Tyco scandals of the early 2000s ushered in the era of Sarbanes-Oxley, several scandals in the nonprofit world brought about increased government oversight in this area. The main vehicle for this increased level of review was the redesigned Form 990 first released in 2009. Executive compensation was one of the main areas of this scrutiny.

In addition to redesigning the nonprofit tax return, the IRS imposed greater penalties for Boards of Directors that gave their executives compensation deemed to be excessive. Beginning January 1, 2010, board members who knowingly and willfully approved excess benefit transactions are joint and severally liable for a 10 percent tax. The tax is limited to \$20,000 per transaction. This law applies to certain insiders of the nonprofit who are deemed to have a substantial influence over the organization's affairs. This group includes: The Board, CEO and CFO, and can be extended to others who are determined to have such influence. This definition includes not only the individuals who exert significant influence over the nonprofit but also their family members and any controlled businesses they own

If any of these individuals or entities is found by the IRS to have engaged in an excess benefit transaction and the IRS imposes penalties, the details of this penalty, including names and amounts must be shown on the publicly-available Form 990 filings. Automatic violations are triggered by failure of the nonprofit to properly document and report compensation and benefits; and any benefits paid or provided which are not properly reported and disclosed are considered automatic excess benefits, regardless of the amounts.

### **12. State Regulations Governing Nonprofit Executive Salaries**

The federal government is not the only regulatory authority that has the ability to create guidelines for nonprofit executive compensation. Since many nonprofits receive substantial funding from state governments, these entities can exercise some form of control over these groups. As with many new laws and regulations, they develop in response to some form of scandal.

For example, in June of 2011, it was revealed that the Nellie Mae Foundation compensated each of its 15 directors between \$19,000 and \$32,000. In response, Massachusetts officials, led by then Attorney General Martha Coakley moved to ban compensation for nonprofit trustees. In 2012, New York Governor Andrew Cuomo proposed a new regulation designed to reduce state funds being used by non-profits for their executives' salaries and overhead.

Governor Cuomo's rule limits to \$199,000 the amount of state funds that any nonprofit which receives at least 30% of its overall funding from the state would be allowed to put toward a nonprofit executive's compensation package. The executive order does not limit the executive's total salary, but any organization wishing to pay an executive more than the \$199,000 amount would have to find non-state funding sources to bring the compensation above that level and also obtain special permission. Additional aspects of the regulation initially required a minimum of 75% of a provider's state funding go to program services rather than administrative costs; that percentage rose to 85% by 2015. Also, the order mandates that the salaries--no matter the source of its funding fall no higher than the 75th percentile for that field in order for an organization to qualify for state funding.

The Cuomo executive order came about when the salary and benefits packages of executives at YAI became publicized. This mental health organization was operated by two brothers, Philip and Joel Levy, each of whom earned approximately \$1M each. They each had multiple luxury home and automobiles. The tuition for their children's college education was also paid for by YAI and the nonprofit's funds were used to help buy one of Philip Levy's children a co-op apartment in Greenwich Village.

### **13. Guidelines Provided Non-Governmental Entities**

Information on a variety of nonprofits is readily available to donors and Boards of Directors who wish to learn about their governance policies and finances. Several entities also offer guidance to any Board of Directors in exercising its due diligence with regard to managing its expenses.

For example, [smallbusiness.chron.com](http://smallbusiness.chron.com), a website specializing in advising small businesses, also offers non-profits budgetary advice. The site recommends that nonprofits use the following outline: 80 percent of the nonprofits' funds should go to the non-profit's mission and purpose; 10 percent for administration costs and 10 percent for fundraising expenses. It further recommends that investment funds in a savings account should not be considered a part of these percentages; and that using volunteer labor can be a way the entities to save on administrative costs, most notably salaries."

Another organization, the Better Business Bureau (BBB), on which consumers rely for business recommendations, also offers advice for nonprofits. According to the BBB, "not more than one or 10% (whichever is greater) directly or indirectly compensated person(s) serving as voting member(s) of the board. Compensated members shall not serve as

the board's chair or treasurer.” The Bureau also recommends that charitable organizations should spend at least 65% of their total expenses on program activities which are defined as total program service expenses over total expenses. It further notes that nonprofit organizations should not spend more than 35% of related contributions on fund raising and defines “related contributions” as those which include “donations, legacies, and other gifts received as a result of fund raising efforts.” The fundraising percentage is calculated by dividing total fund raising expenses over total related contributions.

Other sources do not offer recommendation for the amount of monies that should be spent in the nonprofit’s various expenses but does show how particular nonprofits use their funds. Two such groups are Charity Navigator .com and Guidestar.org, itself a nonprofit.

Since its founding in 2001, Charity Navigator has provided the public with ratings of charities designed to provide donors unbiased evaluations of these groups. In carrying out its goal of disseminating this information, Charity Navigator analysts note that they have examined tens of thousands of non-profit financial documents to assess over 9,000 American charities. . The end result is a numbers-based ratings system. This system analyzes two main areas of a charity's performance; their Financial Health and their Accountability & Transparency. The goal is to provide donors with an idea of how efficiently Charity Navigators’ analysts believe a charity will use its funds currently; how well it has sustained its programs and services over time; and its level of commitment to good governance, best practices and openness with information.

Guidestar offers its users information on every single IRS-registered nonprofit organization, specifically each nonprofit’s nonprofit's mission, legitimacy, impact, reputation, finances, programs, transparency, governance, in addition to other information. Guidestar’s website lists the latest available 990 returns for the majority of non-religious nonprofits in its database.

It should be noted that while neither of these resources gives advice on how much money a nonprofit should allocate to its executive compensation, they both offer advice to nonprofits on how to justify to the IRS such salary and benefit packages.

Other organizations which offer similar information to the general public are The Foundation Center, Giving USA and The National Center for Charitable Statistics.

#### **14. Examples of Non-Profit Executive Salaries: Analysis and Discussion**

As noted earlier, the topic of nonprofit executive compensation is a crucial one in the discussion of charitable giving. Since the recession of 2008 and 2009, media attention has increased greatly regarding high executive pay at both for-profit and NFP organizations. Public concern has grown along with this media attention. When information about a nonprofit executive’s high compensation package is reported in the media, public confidence in the organization decreases, as does the amount of donor contributions.

It is worthwhile to note that while a nonprofit’s Form 990 is a public document and provides a tool for donors to access information regarding executive compensation, research conducted by Balsam and Harris (2014), discovered that, there is no association between the amount of compensation disclosed in a nonprofit’s tax return and a change in the percentage of donations the nonprofit receives. A correlation appears when excess executive compensation is reported by the media. Their research found that donations are reduced by "five percent for every \$100,000 of executive compensation disclosed by the media" (Balsam and Harris, 2014). They also found that organizations which were the subject of this kind of media scrutiny experienced approximately 15 percent less growth in donations in the two year period following such publicity.

The following examples obtained from media reports over the past five years show that the topic of excessive nonprofit executive compensation is not merely a theoretical discussion, but one that is based on real world occurrences.

In a The Nonprofit Times Charity Guide & Watchdog Report, published in May and June 2013, reported the following compensation packages for nonprofit healthcare executives were culled from each organization’s respective Form 990. The information is provided in order from greatest compensation to least:

1. Memorial Sloan Kettering Cancer Center paid its Chairman and Attending Surgeon, Peter T. Scardino, M.D., compensation and other benefits of \$2,207, 147.
2. City of Hope gave its President and CEO, Michael Friedman, \$1,434, 148 in compensation and benefits.
3. Shriners Hospitals for Children provided its Chief of Staff, Kenneth Guidera, with compensation of \$1,347,996.
4. The Dana- Farber Cancer Institute/Jimmy Fund paid their president and CEO, Edward J. Benz, Jr. M.D., \$1,245,790 in compensation and other benefits.



5. Smile Train provided their organization's past president, Brian Mullaney, with total compensation of \$1,178,571.
6. The Heritage Foundation's president, Edwin J. Feulner, Jr., was provided total compensation of \$1,172,321.
7. The Cystic Fibrosis Foundation' president and CEO, Robert J Beall, was provided with a total compensation package of \$1,073,725.
8. Te United Way Worldwide organization's president and CEO, Brian Gallagher, was paid \$999,574 in salary and other benefits.
9. The Alzheimer's Association- N.O's president and CEO, Harry Johns, was awarded a total compensation package of \$996,824.
10. The Boy Scouts of America-N.O.'s past chief scout executive, Robert J. Mazzuca, was awarded total compensation of \$987,412.

When reviewing seven figure salaries for nonprofit executives, the donating public should always ask itself: How many services could the nonprofit provide with the funds paid to these executives?

Data from 2012 gives additional insight into the compensation packages of the highest paid university presidents. It should be noted that these chief executives received these salaries at time when the New York Times reported that 1 of 4 students cannot finish college and university because they cannot afford the tuition. As we look at the top 10 paid presidents in public universities in the United States provided below we see salaries ranging from almost \$3 million to \$1 million. It should also be pointed out that in 2010, one of the highest salaries paid to a private university president was paid to Bob Kerrey of the New School in New York City. His compensation that year was \$3,047,703.

Here is information on the top 10 public university presidents' compensation packages paid in the United States during the 2012 fiscal year.

1. The Pennsylvania State University at University Park, paid Graham B. Spanier total compensation of \$2,906,721. He assumed office in September 1995 and left under a cloud in November 2011 due to the Sandusky scandal that produced negative publicity for the university.
2. Auburn University paid Jay Gogue total compensation of \$2, 542, 86. He assumed office July 2007.
3. E. Gordon Gee from Ohio State University-Main Campus assumed office in October 2007 and his total compensation was \$1,899,420.
4. George Mason University paid Alan Merten with a total compensation package of \$1,869,369. He has been president since July 1996.
5. Jo Ann M. Gora from Ball State University was provided with a total compensation package of \$984,647. She assumed office August 2004.
6. Mary Sue Coleman of the University of Michigan, was awarded total compensation of \$918,783. She assumes office in September 2002.
7. Charles W. Steger from Virginia Tech received total compensation of \$857,749. He assumed office June 2008.
8. Mark G Yudof from University of California system was awarded total compensation of \$847,149. He assumed office January 2000.
9. Bernard J. Machen from University of Florida assumed office in December 2003 and received total compensation of \$843,562,
10. Francisco G. Cigarroa from the University of Texas system received a total compensation package of \$815,833. He assumed office February 2009.

## 15. Conclusion

The subject of excessive compensation for nonprofit executives is a controversial one and is a subject that has been the source of discussion in the media. Many proponents of large compensation packages for nonprofit executives argue that these institutions should pay "market rate" for their chief executives. This is a tenet of executive compensation in the for-profit world.

However, the non-profit sector is so inherently different from the commercial sphere that this logic does not hold true in the universe of mission-based entities.

With their favorable tax status and preferential tax treatment of donation, nonprofits are depended on the donating public and the government to survive. This means that the public should have a say in whether the compensation package for a

nonprofit executive is excessive. And the research indicates that this compensation is a factor in whether donors contribute their personal funds to charities. At its core, the issue of such compensation packages rests with the idea of donor-intent: Do donors want the funds they contribute to mission-based organizations to go to paying the organizations' executives large compensation packages or do they want those monies to go to activities that further the mission of the organizations. The research would indicate the latter.

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