

CEO UPDATE

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1220 L Street NW, Suite 850, Washington, DC 20005

Executive Employment Agreements

By David Goch and James Zaniello

It is often said that the law is not static, nor does it exist in a vacuum; that is no more obvious than in the area of nonprofit CEO agreements.

Nonprofit executive's agreements have begun to mirror contracts for their counterparts in the for-profit world with executive perks such as automobiles and club dues, compensation packages with deferred income and working remotely, while still under the umbrella of the nonprofit organization and the watchful eye of the IRS. On the other side of the equation is typically a savvy Board, acting on advice from professionals, with the goal of retaining the executive but under terms most favorable to the organization.

Preparing to negotiate your first executive employment agreement can be a smooth process if you have educated yourself in advance. First and foremost look at the resources that are immediately available to you – the sample employment agreement of the American Society of Association Executives as well as information

contained in salary surveys. Consult close colleagues who have already negotiated their first contract.

If the hiring organization has a savvy human resources executive or an executive search firm is involved, the search committee is likely knowledgeable of what an employment agreement entails. However, if the organization is managing the search on its own, it may be unclear to you whether it is offering an employment agreement or how well it has thought through this process.

Consulting an attorney is also an important part of this process – particularly if you are not familiar with employment law or the laws of the state in which the organization making the offer is located. The attorney retained by the organization you are negotiating with represents the organization, not you.

Key Elements

Salary: Often the first consideration but not necessarily the most important. Is there a possibility of severance for any early termination? For highly compensated individuals, is there the possibility of setting-up a deferred compensation plan so that realization of the income can be deferred to a time when you are likely to be in a lower income tax bracket?

Clearly, the amount is of concern. As stated above, numerous benchmarking resources exist. Furthermore, salary is rarely ever a flat amount anymore. Percentages, bonuses, and other creative formulas are more common than ever.

Term: A common error is the assumption that every contract is for a term of years, which provides the executive with a desired level of job security. For general discussion, written contracts come in three forms: “at-will” open ended agreements that, while setting forth with specificity the exec’s relationship with the organization during the employment relationship, still clearly states that the relationship is “at-will” and can be terminated by either party for any or no reason (without consequence). The second contract can have the same result but is a little more deceptive in how it is presented. This agreement acknowledges a term, e.g., a three-year agreement which automatically renews for additional one-year terms..., but, placed in the separate termination provision is language that allows a Board to terminate the agreement on, e.g., three months notice “without cause”. In this case, the exec’s “three year deal” is at best a 90-day contract. The third option is a contract that provides the exec security in that it is a multi-year deal and the only way it can be terminated by the organization is for cause; “cause” typically being defined as a “substantial breach of a material aspect of the agreement”.

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David Goch is a Partner with Webster, Chamberlain & Bean, a law firm specializing in providing full legal service to nonprofit organizations of sizes.

James Zaniello serves as Vice President of Association Strategies Inc., an organization development and executive search firm serving the association/nonprofit community.

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Bonus Opportunity: With a frugal Board, or a financially challenged organization, often a bonus can be the exec's financial savior. An important aspect of a bonus, however, is the means by which it is awarded. Is it based purely a subjective determination by the Board or a more objective analysis of meeting performance goals.

Benefits: In addition to the traditional benefits, the sky can be the limit, including country clubs, continuing education, expense budget (business vs. coach class), car allowance, moving expenses, companion travel, home office expenses, etc. But keep in mind all benefits are not "free". Many can result in taxable events to the exec.

Deferred Comp: Deferred compensation is one of the benefits available to nonprofit executives, but there are significant limits under federal tax laws. Still, whatever options exist should be considered.

Termination: Although addressed previously, it bears repeating, an exec's job security is dependant upon the termination language and its clarity. First, prior to termination, an exec's job duties should be set forth with specificity. Thus, a contract that only allows for termination "for cause" will provide an exec a blue print for success.

Ambiguous, incomplete, or catchall language, could be detrimental to an exec. The

contract should also spell out who must approve termination.

Severance: Negotiating severance at the outset of a contract can, at times, be a very difficult task (e.g., the prospective employer's prior exec left under less than favorable circumstances and the Board feels "burned") or can be an easy term to settle. An industry standard is one month for every one year of service to the organization. But this standard is not always clearly understood. Does it apply only at the end of the natural term? How do you deal with early termination without cause? With cause? Generally, the stated standard would apply to a "natural" term end (a contract not to be renewed). Early termination without cause should warrant payment for the balance of the contract AND possibly some additional severance.

Noncompete Clause: Execs should be cognizant of how long they will be barred from competing, what is defined parameters of competition, are there any geographical restrictions. Suffice it to say, that the narrowest drawn non-compete provision, in terms of professional scope, time and geography, is preferred.

Performance Measures and Job Duties: It is not coincidental that these two areas come last

in the list and also serve as the summary for a successful agreement. Having clearly articulated job duties, as well as closely aligned performance measures, will allow an exec to understand his/her job and the tasks and direction of the organization and the staff. While salary and perks are the direct benefits of the job, some of the more unpleasant aspects we have discussed (termination, non-

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compete) can be avoided by negotiating with the Board on these elements. Similar to the termination procedure, performance measures should be evaluated by the body most familiar with the exec and be passed by a super majority. An exec should be diligent seeking out a review in order to remain informed as to the Board's expectations.

Tax Issues

The exec and his lawyer need to understand clearly what elements of the compensation package are taxable, and which are not. This is particularly important when considering various kinds of fringe benefits, such as companion travel, or nonqualified deferred compensation. Properly structured, these are tax-free or tax-deferred. Otherwise, they can present an unexpected tax bill for both the employer and the exec. ■

EXECUTIVE PROFILE

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A. My sense is that in CEO association market compensation is increasingly tied toward clear objectives. We are all using strategic plans as management tools to get clarity from the board, and we have agreement on the priorities and what we are going to do here. That gives the board tools to evaluate their CEO. So, I think compensation is tied to that.

I think it varies according to associations. CEO compensation is going up for association CEOs as it is for corporate CEOs. Increasingly organizations are looking for people with the professional skill that is unique enough that a certain compensation is in order to get that skill set.

Q. Once you were close on a deal, did you use an attorney or agent to help you negotiate the terms of your contract? If so, what are the lessons learned?

A. I negotiated directly with my Chairman. I used an employment lawyer to review the contract and make sure that the documents were laid out in an appropriate and fair way. It didn't

feel intrusive in terms of my relationship with the Chairman or in the good faith way we were approaching this. He made some edits in the document that gave me some protections that were appropriate based on what he knew other CEOs had in their contract and what seemed fair to the organization.

Q. When you are in that place of being offered a position but not yet having a deal, what are the most important things you need to think about? How do you achieve the best deal without creating a negative atmosphere?

A. I had in my mind several things that were the most important to me, and I find it an advantage to have a search firm between you and the perspective employer. They are hired by the employer, but it is in their interest to have a collegial, constructive arrangement negotiated. I can be pretty upfront early on with things that I want in terms of compensation, a contract, and I expect X-Y-Z.

By the time the Chairman and I had a breakfast for him to make a formal offer to me, we knew what was important to both of us. If you get a good search firm who really is

interested in making a right match, not just pushing the job, it makes all the difference.

Q. You have managed to create a positive public persona with your volunteer activities and boards. You are President of the University Club and have been active in a number of organizations. Is there a good way or strategy to this that makes sense?

A. It is important to do things because you like to do them, and I do. I was destined to be an association executive because I actually like serving on committees, I like leading committees, I like being on boards; not everyone has an appetite for that kind of work, but I find it enjoyable.

Then there is obviously visibility that comes from it and good experience. Working in the volunteer capacity chairing a committee is good experience for ultimately chairing a board, and you can further develop some of those kinds of consensus building and leadership skills through your volunteer work.

Also, it is good to get out of your sector niche for the diversity it gives you and exposure to other players. The things that I have done in the Rotary, University Club, and Public Affairs Council have all been helpful to my growth as a person and as a professional because they give me other dimensions. ■