

# SENATE STANDING COMMITTEE ON INVESTIGATIONS AND GOVERNMENT OPERATIONS

## REPORT ON THE HEARING HELD ON FEBRUARY 6, 2012 ON EXECUTIVE COMPENSATION AT NOT-FOR-PROFITS

FEBRUARY 16, 2012



**SENATOR CARL L. MARCELLINO, CHAIRMAN**

SENATE STANDING COMMITTEE ON  
INVESTIGATION AND GOVERNMENT OPERATIONS

*COMPILED BY:*

*DEBORAH PECK KELLEHER, COMMITTEE DIRECTOR  
ROBERT PARKER, LEGISLATIVE ANALYST*







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**SENATE STANDING COMMITTEE ON INVESTIGATIONS AND  
GOVERNMENT OPERATIONS**

**Public Hearing on Executive Compensation at Not-For-Profit Organizations**

**Monday, February 6, 2012 11 am**

**Hearing Room A**

**Legislative Office Building**

**State Street**

**Albany, NY 12247**

**WITNESS LIST**

**Michael Cooney**, Partner  
Nixon Peabody, LLP

**Doug Sauer**, Chief Executive Officer  
New York Council of Nonprofits

**James Lytle**, Partner  
Manatt, Phelps & Phillips, LLP  
Testifying on behalf of:

Association For Community Living  
Black Agency Executives  
Catholic Charities of the Archdiocese of New York  
Catholic Charities Neighborhood Services, Diocese of Brooklyn and Queens  
Coalition of Behavioral Health Agencies  
Family Planning Advocates of New York State  
Federation of Protestant Welfare Agencies  
Human Services Council of New York  
Long Island Coalition of Behavioral Health Providers  
Mental Health Association of New York City  
Mental Health Association of Westchester  
New York State Coalition for Children's Mental Health Services  
New York State Council for Community Behavioral Healthcare  
Supportive Housing Network of New York  
UJA/Federation of New York  
United Neighborhood Houses of New York

**Jayne Cammisa**, Registered Nurse  
New York State Nurses Association Union Council Officer  
Westchester County Health Care Corporation





# • Testimony Summary •

**Michael Cooney**  
**Partner**  
**Nixon Peabody, LLP**

Mr. Cooney shared with the Committee his experience working with nonprofits which concentrate on the affairs of tax-exempt organizations, their donors and supporters. Recently, Mr. Cooney served on Attorney General Eric Schneiderman's Leadership Committee for Nonprofit Revitalization.

Mr. Cooney's experience has been that the vast majority of nonprofit executives are undercompensated for the value they bring to their organizations and the communities they serve. He contends there is already a legal structure and practices in place to assure the "reasonableness" of compensation. It is Mr. Cooney's opinion that instead of further regulation, there needs to be a better understanding of this structure and vigorous enforcement of current law.

The Governor's recent executive order limiting the amount of State funding to \$199,000 has left defining the new rules of "compensation" and "executive" to nine different State agencies. Mr. Cooney conveyed to the Committee that it is unclear what the basis is for the \$199,000 figure. He believes that legislative action would bring greater certainty and impact to the State funds.

Mr. Cooney shared with the Committee that Not-for-Profit Corporation Law, Section 202 (a) (12) already imposes on nonprofit corporate governing boards the responsibility to assure executive compensation is "reasonable" and "commensurate with services performed." The Law also provides that salaries must be set by a majority of the board and loans to executives are generally not allowed. Mr. Cooney pointed to a case involving Adelphi University in 2007 which proves this point.

Current law does not delineate procedures to ensure compliance with these requirements, however, organizations defined as public charities by the Federal Internal Revenue Code under Section 501 (c)(3) are already familiar with establishing reasonable compensation under Code Section 4958 by creating a rebuttable presumption that the compensation is reasonable.

Mr. Cooney shared with the committee three core requirements that create a reasonable and efficient rubric for setting executive compensation. These requirements included:

- A board independently reviewing complete compensation packages commonly using a compensation committee of independent, educated board members;

- Board members empowered to consult outside sources to determine comparable pay of other service agencies;
- All actions and steps documented in their minutes and the minutes approved at a subsequent meeting and made available to the full board.

Mr. Cooney shared with the Committee that compensation levels for executives of non-profits is readily available as most charities are required to report, in detail on the IRS Form 990 and is also incorporated in the annual filings with the New York State Attorney General Charities Bureau. As a result, the State and public already have access to compensation information for many of these entities.

Mr. Cooney conveyed to the Committee that without consistent and vigorous enforcement, access to all this information is of little value. He cited a recent case which was the basis for the creation of the Governor's task force last August. In that case, concerns about high levels of compensation were already well-known and it appears there was already a corporate integrity agreement in place with periodic reports on compliance required. Mr. Cooney questioned why these practice were allowed to continue despite the State knowledge and actions.

Mr. Cooney asked the Committee to consider proposals from the nonprofit sector. He believes New York law should supplement and strengthen existing Federal requirements without causing additional burdens and adding new costs. He believes that blanket rules or limits on executive compensation would do more harm than help, to the detriment of all New Yorkers.



**Doug Sauer**  
**Chief Executive Officer**  
**New York Council on Nonprofits, Inc.**

Mr. Sauer, who has served for the past 31 years as Chief Executive Officer of the Council, shared with the Committee the diversity of organizations his council represents and the programs they offer, including being the developer and provider of the State's Board Training Consortium. He also serves on the Attorney General's Committee on Nonprofit Revitalization and is working with Comptroller DiNapoli to reform the State's business practices with nonprofit contractors.

Mr. Sauer shared with the committee that the cases of excessive executive compensation and abuse are few and far between and those cases that do exist need to be eliminated. Rather than over compensation, under-compensation is more prevalent with nonprofits contracting with the State. Mr. Sauer conveyed to the Committee the accessibility that already exists to view nonprofit finances and executive compensation. This information is required by both the Internal Revenue Service and additional information is filed annually with the Attorney General's Office and in most cases, through the procurement and contract reporting processes of State agencies.

Mr. Sauer raised the question of how much it cost the State to collect and analyze the new data the Governor's Task Force requested and how much it cost the nonprofits to respond to the survey. Mr. Sauer pointed out that the time it took nonprofit staff to complete the survey is considered an administrative expense by the State.

Mr. Sauer noted that other organizations and individuals that have business dealings with the State are not coming under the same scrutiny as nonprofits, including State employees. Furthermore, he shared with the Committee that charities in New York State are arguably the most regulated in the country, while many of the current regulations are ineffective and outdated, and the expense to do business in New York State is increasingly cost prohibitive. Laws specific to charities have not been updated for decades, but recommendations are coming soon from the Attorney General's final report.

Mr. Sauer would like to see an effective partnership developed between nonprofits and the State government to tackle problems together. He would like to see the nonprofits have a seat at the table to work with the State instead of being eliminated from the dialogue.

Mr. Sauer asked the Committee to consider the following:

- IRS, State Attorney General and individual New York State agencies already possess compensation oversight mechanisms;
- The proposed Executive Order provides exemptions and waivers which his organization believes will result in exceptions for those organizations whose compensation levels are most likely to "shock the conscience;"
- The proposed system is not consistent and will create new expenses for taxpayers.

Mr. Sauer believes the solution is that New York State needs to better coordinate its efforts, focus resources and streamline its attention to the business relationship with the nonprofit sector. He asked leaders in both the Legislature and Executive Chamber to join nonprofits in committing the attention and resources necessary to developing a cabinet level liaison within the Executive Chamber.



**James W. Lytle**  
**Partner**  
**Manatt, Phelps & Phillips, LLP**

Mr. Lytle testified on behalf of more than a dozen not-for-profit organizations, associations and coalitions. The organizations Mr. Lytle represents believe additional steps should be taken by New York State to hold not-for-profit boards and executives accountable for compliance with reasonable compensation policies and to ensure that State support is directed efficiently and cost-effectively to serve the intended beneficiaries of State funding. However, these organizations feel that arbitrary, inflexible, across-the-board approaches that say they address the abuse that is not widespread and not regulated will only penalize those organizations that are honest and ethical, and the New Yorkers who rely on those services.

Mr. Lytle wanted to remind the committee that these non-profits are providing services, which New York cannot, for those that are in need. Furthermore, although the nonprofit sector has been a contributor to the State's economic activity, these organizations have also been affected by the severe economic downturn, including reductions in government funding and less charitable giving, causing financial distress to these organizations.

Mr. Lytle reminded the Committee that nonprofits are already subject to rigorous Federal and State oversight including regulating excessive compensation and administrative expenses. Since the mid-1990s, the Internal Revenue Service has enforced clear guidelines on executive compensation that must be observed by tax-exempt nonprofit entities. As a result, compensation to board members and executives of the organizations, including anyone with substantial influence over the organizations affairs, are subject to disclosure and IRS scrutiny.

Mr. Lytle shared with the Committee that the IRS reviews information pertaining to similar services by similar organizations to determine whether compensation is reasonable and will presume the reasonableness of the compensation process if the governing board shows and documents the process at which they arrived at their determination.

Mr. Lytle pointed out although the Governor's Task Force on Not-for-Profit Entities was convened last summer which required extensive information from not-for-profits, no analysis of the collected data has been released, nor has a case been made to subject every nonprofit to a "one size fits all" limitation on compensation and administrative expense. The Executive Order does not take into account the unique nature, complexity, size or location of the contracting party or the implications on the recruitment of qualified executive leadership in the not-for-profit sector.

Mr. Lytle believes that neither the proposed legislation nor the Executive Order are fair approaches to the issue and will jeopardize the ability of not-for-profit organizations to meet their missions. Furthermore, it fails to recognize the vast disparities and variations among contracting entities and the services they render, is contrary to State policies that have urged consolidations and affiliations among State-supported contracting entities and is inconsistent with State policies that already seek to contain administrative costs. The proposal also ignores

the specialized expertise and experience that may be required by contracting agencies, will disproportionately impact on the delivery of service to the most disadvantaged New Yorkers and will render nonprofits unable to compete for the best executive leadership. Finally, the proposal is potentially subject to inconsistent application.

Rather than following this approach in the Executive Order, Mr. Lytle and his organizations recommend to the Legislature to strengthen existing laws and rules that will continue to hold contracting organizations themselves accountable for their obligations in setting reasonable compensation and administrative costs.

Strengthening enforcement of existing regulatory requirements could include:

- Amending the Not-for-Profit Corporation Law to required not-for-profit boards to apply the Internal Revenue Service’s (IRS) reasonable compensation standards for tax-exempt organizations;
- Authorizing the Attorney General to enforce these requirements and requiring the organization to produce evidence of its compliance with these standards, upon request;
- Providing sufficient resources to the Attorney General’s Charities Bureau to enforce these requirements;
- Requiring State agencies to adopt reimbursement and contracting practices that ensure that administrative expenses remain within appropriate levels, taking into account the specific services being rendered and other factors that may dictate the appropriate level of “overhead”



**Jayne Cammisa**  
**Registered Nurse**  
**New York State Nurses Association Union Council Officer**  
**Westchester County Health Care Corporation**

Ms. Cammisa shared with the Committee the 2009 salary of Westchester Medical Chief Executive Officer Michael Israel who was paid \$1.2 million and Chief Operating Officer Gary Brudnicki's salary of \$738,800. Thirty-Six other executives were paid between \$128,000 and \$530,000 per year.

During October 2011, the Nurses Association received notices that the facility would be eliminating 250 Registered Nurse positions, of which 139 positions are nurses who work at the patients' bedside. This elimination amounts to a 19% cut in direct-care nursing at Westchester Medical Center. Since the time of these cuts, there are already reports of short-staffing and concerns since studies have linked short staffing with higher incidences of adverse patient outcomes.

Ms. Cammisa also shared with the Committee that management at Westchester Medical Center is aggressively seeking cuts to nurses' benefits and wages during contract negotiations while refusing to commit to management cuts in salaries and benefits.

Ms. Cammisa and her fellow co-workers are extremely concerned that layoffs at Westchester Medical Center will severely impact the safety and delivery of quality care in not only Westchester, but for the entire Hudson Valley area.







# • Recommendations •

The majority of the Not-for-Profits in our State are complying with Internal Revenue Service (IRS) standards for executive compensation. In addition, there are a large number of organization executives that are under-compensated for their dedication and service to our State's residents. It is the intent of this Committee to provide recommendations focusing on those organizations granting excessive compensation to their executives.

## **Executive Order**

- The order should be limited to Not-for-Profit organizations
- Agency guidelines need to be written with a recognition that many organizations have contracts with multiple State agencies, and conflicting regulations routinely create compliance difficulties
- Serious concerns were raised on the across the board administrative cost cap
  - Services, treatments and administrative costs vary based on the type of service and size of provider
- The waiver granting process and the term “showing of good cause” should be defined
  - The order refers to waivers granted for “other related requirements”, which should be defined
- The powers to revoke a contract for failure to comply should be expanded beyond the exclusive right of a Commissioner
- The collection of data from providers to monitor the Executive Order should be limited to just the information needed for compliance

## **Setting Compensation**

- Current Not-For-Profit Corporation Law section 202 (a) (12) allows Not-for-Profit corporations to fix reasonable compensation. The terms “reasonable” and “compensation” are not defined
  - The terms “compensation” and “reasonable” in the Not-For-Profit Corporation Law should be defined with a reference to the Internal Revenue Service (IRS) definitions and guidelines
- Instead of a strict salary or compensation cap, a percentage of an organization's revenues or the value of their State contracts could be utilized
  - Caps could also be set in tiers based on total expenditures, number of employees, geographic location, or the complexity of organization
- NYS should require documentation of the compensation process that mirrors and/or integrates the current IRS guidelines
- Not-for-Profit organizations should be prohibited from giving an “excess benefit transaction” as defined by the IRS, similar to Massachusetts (S.824) legislation

## **Board of Directors**

- Current Not-For-Profit Corporation Law does not restrict employees, family members, or individuals who have business dealings with the organization from sitting on the Board of Directors
  - Boards should have a written policy about employees service on the Board, their voting rights, recusal from Board decisions, and the percentage of a Board that must be independent of the organization
    - Employees should be prohibited from serving as the Board Chair
- The State should offer more training to Board of Directors focusing setting compensation, and the need to set written compensation, nepotism and conflict of interest policies
- Current Education Law section 3016 requires a 2/3 vote to hire relatives of sitting Board members
  - This standard should be added to the Not-For-Profit Corporation Law
- The Department of State and the Attorney General should offer training and “helpful” reviews similar to that offered by New York City

## **Guidelines**

- The State should adopt a number of regulatory and statutory changes in consideration of State contracts with Not-for-Profit organizations
  - The Board of Directors should be required to conduct an evaluation prior to increasing the compensation of any executive and keep documentation of any reviews
- The City of New York requires the submission of a Capacity Building and Oversight Report for continuation of a contract
  - This report focuses on the health of an organization, such as how active the Board of Directors are and staff training
    - The State could require similar submission prior to a contract being signed or renewed
- The current statutory ban on loans to employees and Board members should be expanded
- Based on the IRS standards, guidelines should be set that:
  - Board of Directors must obtain current compensation comparability data
    - Comparability data must be from similar positions in similar organizations
    - Without management influence
    - If a consultant is used, the Board should have policies on their selection and oversight
  - The Board should consider the total compensation including benefits, employee’s qualifications and performance, payments from other related organizations, and the organization’s fiscal resources
  - Each Board member that decides compensation must be disinterested (no employees or family members)
  - Board members with a conflict of interest and the employee whose compensation is being considered may not vote on the compensation
  - Board must document the basis for decision and approve:
    - Terms of arrangement & date approved
    - Names of board members present and the vote

- Description of comparability data & how obtained
  - Explanation of why compensation is reasonable
  - Explanation of action taken by member with a conflict of interest
- This information should be available for review when requested

### **Information Disclosure**

- A written nepotism policy should be required and submitted to the Attorney General or the Department of State
  - Could require that a majority of Board members are not related, as in the current Regents guidelines for Regent Chartered Not-for-Profit organizations
- A written conflict of interest policy covering both business interests and elected officials should be required and submitted to the Attorney General or the Department of State
  - New York City currently requires one that prohibits conflicts with any City elected officials
- A written compensation determination policy should be required and submitted to the Attorney General or the Department of State
- All organizations having a contract with the State should file with the Attorney General including those exempt under Executive Law section 172-a (2)
- IRS 990 forms should be required to be posted on their website

### **Enforcement**

- There should be a consistent and vigorous enforcement of the current laws
- The law should be clarified to allow the State to enforce more sections of the Not-For-Profit Corporation Law, including the provisions covering setting compensation for employees
- The law should be amended to allow for the enforcement by the State of violations of IRS's excess benefit transactions
- Prior to the issuance of a State contract, there should be a review to see if executive compensation is "reasonable", as defined by the IRS







● Attachment A ●

Testimony

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Written Comments Submitted By:

**Michael J. Cooney, Esq.**

**Partner**

**Nixon Peabody LLP**

Before the:

**New York State Senate**

**Committee on Investigations and Government Operations**

**February 6, 2012**

**Albany, New York**

My name is Michael Cooney. I am a partner with the law firm of Nixon Peabody LLP and head of its Higher Education and Exempt Organizations practice.

My practice concentrates on the affairs of nonprofit and tax-exempt organizations, their donors and supporters. I have had the privilege of serving on many nonprofit governing Boards as a volunteer. I recently had the honor of serving on Attorney General Eric Schneiderman's Leadership Committee for Nonprofit Revitalization.

As one who strongly believes in the value of the nonprofit sector to the people of the state of New York, I urge the members of the Committee to evaluate and incorporate in their decision-making the existing processes and structures intended to insure the fidelity of executive compensation in the sector to mission and performance.

In my personal experience, the vast majority of nonprofit executives are undercompensated for the value they bring to their organizations and the communities they serve. Importantly, there is already a legal structure and practices in place to assure the reasonableness of this compensation. What is needed in the State, in my opinion, is a better understanding of this structure and vigorous enforcement of the laws that are already in place.

At the time of this writing, the Governor has promulgated an Executive Order limiting the amount of state funding to the first \$199,000 of compensation to provider executives. The definition of "compensation" and "executive" have been left to the rule-making authority of at least nine different state agencies. The basis for the \$199,000 figure is unclear. The State budget contains similar limitations as a condition of funding. The people of the State of New York and its nonprofit providers deserve a better system. Through legislative action, it would be possible to bring greater certainty and impact to the expenditure of State funds.

### **Existing standards**

New York law imposes on nonprofit corporate governing boards the responsibility to assure that executive compensation is "reasonable" and "commensurate with services performed."<sup>1</sup> New York law generally provides that officer salaries must be fixed by a majority of the entity's governing board.<sup>2</sup> Loans to nonprofit executives are generally prohibited.<sup>3</sup> And, most importantly, as demonstrated in the case of Adelphi University in 2007, the State has the power to remove fiduciaries of nonprofits for, among other things, approving excessive compensation.

Currently, state law does not delineate procedures to ensure compliance with these requirements. But those organizations which are public charities under Section 501(c)(3) of the Internal Revenue Code are already familiar with the decade-old regime under Code Section 4958 for establishing reasonable compensation. That statute sets forth a process, which, if used,

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<sup>1</sup> Not-for-Profit Corporation Law ("N-PCL") Section 202(a)(12).

<sup>2</sup> N-PCL Section 715(f).

<sup>3</sup> N-PCL Section 716.

creates a rebuttable presumption that the compensation approved is reasonable. That rebuttable presumption of reasonableness<sup>4</sup> has three core requirements that create a reasonable and efficient rubric for setting executive compensation:

- Board fiduciaries review the complete compensation packages, independent of any conflicts of interest with those being compensated. The common approach for assuring reasonable executive salaries is to use a compensation committee comprised of independent, educated board members. This delegation is often done pursuant to the organization's by-laws. The charge to the compensation committee should be clear and unambiguous, with committee members having unfettered access to all relevant financial and performance information, which must be complete and comprehensive. The fiduciaries work under a compensation policy declaring that all compensation must be reasonable and setting the percentiles in which compensation may be set.
- Board or committee members must be empowered to consult outside resources to determine what is paid for comparable services by comparable nonprofits. In comparing the board-adopted compensation goals of the institution, the fiduciaries can survey comparable positions at comparable institutions—whether through compensation surveys and salary studies or even from the publicly available IRS Forms 990—in order to establish the bounds of reasonableness. The list of comparables must be reviewed frequently with respect to each position under review. Any outside compensation consultant retained to provide expert advice must report to the compensation committee, free from any taint of management influence.
- Finally, all compensation committee deliberations and actions should be fully documented in minutes, approved at the subsequent committee meeting, and available to the full board.

Well-governed nonprofits have followed these best practices for many years.

## **Transparency**

Compensation levels are not hidden from public view, as one might suspect from news reports. Most charities are required to report, in detail, compensation of board members, officers, key employees, and others on the recently enhanced IRS Form 990, which is also incorporated in annual filings with the New York State Attorney General Charities Bureau. These Form 990 reports must be made available to the public, commonly at the charities' offices and usually online at sites like Guidestar.org. Therefore, state regulators and the public currently have ready access to compensation information for many of these entities.

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<sup>4</sup> 26 CFR 53.4958-6.

## **Enforcement**

All these approval and reporting mechanisms are of little value, however, if the State fails to pursue a consistent and vigorous enforcement path.

The Governor's creation of the task force in August of this past year occurred in the context of serious questions about the million-dollar salaries and benefits paid to two brothers running the Young Adult Institute. Concerns about high levels of compensation at the organization were already well-known.<sup>5</sup> Indeed, it appears that there was already a corporate integrity agreement in place, with the requirement for periodic reports on compliance.<sup>6</sup> Why these compensation practices were allowed to continue is a question not only for your Committee, but for right-minded nonprofits and their boards all across the State. The exception should not provide the rule.

## **Conclusion**

I respectfully ask the Committee to consider the proposals emanating from the nonprofit sector, which is eager for guidance and indeed greater enforcement where appropriate. New York law should supplement and strengthen existing federal requirements without imposing significant new costs and burdens. The nonprofit sector in New York State understands the importance of demonstrating the appropriate use of the scarce and precious resources entrusted to it. The imposition of blanket rules or limitations on executive compensation would do more to harm that process than help it, to the detriment of all New Yorkers.

Thank you for allowing me to comment on this important issue.

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<sup>5</sup> See the editorial on page 4 of the *New York Nonprofit Press*, vol. 10, issue 2 (February 2011) at [http://www.nynp.biz/current/archives/nynparchives/0211\\_February\\_2011%20Edition.pdf](http://www.nynp.biz/current/archives/nynparchives/0211_February_2011%20Edition.pdf)

<sup>6</sup> [http://www.omig.ny.gov/data/images/stories/cia/cia\\_for\\_yai\\_12111.pdf](http://www.omig.ny.gov/data/images/stories/cia/cia_for_yai_12111.pdf)



**TO:** Members of the Senate Committee on Investigations and Government Operations, Chairman – Hon. Carl L. Marcellino

**FROM:** Doug Sauer, *Chief Executive Officer* – New York Council of Nonprofits, Inc.

**ATTACHED:** See Attachment List

## 2-6-2012 Testimony, Nonprofit Executive Compensation

### Introduction

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Good Morning, my name is Doug Sauer, and I am the Chief Executive Officer of the New York Council of Nonprofits (NYCON). I would like to begin my remarks by expressing sincere thanks to Senator Marcellino and the Honorable members of this Committee for affording me the opportunity to speak on behalf of NYCON and the more than 3,100 charitable organizations that make up our membership.

For those of you who may not be familiar with us, NYCON is recognized by the National Council of Nonprofits as *New York's statewide association representing charities of all types* - human services, arts, museums, housing, health, animal welfare, grant makers, etc. Our membership ranges from organizations with no paid staff and annual budgets of less than five thousand dollars to organizations with several hundred staff and annual budgets exceeding one hundred million dollars. NYCON's focus and concern, including in this testimony, is the average everyday charity -small to mid-sized, whose voices are often not represented in these halls. I should note that we don't have hospitals or higher education institutions within our membership.

I have served as the chief executive of NYCON for 31 years and am also past President of the National Council of Nonprofits and currently serve as their Treasurer. Over the years, NYCON has worked extensively with New York State as a partner and contractor in efforts to improve the capacity, performance and accountability of nonprofits and in building a better, mutually beneficial business relationship. For example, for many years, we were the developer and provider for the State's Board Training Consortium (SBTC), a nationally innovative training series for nonprofit boards receiving funding from (5) state agencies. Although the full initiative has ended, two of the state agencies are continuing the efforts to train board members to effectively govern nonprofits.

We are also working with Comptroller Thomas DiNapoli, who has for several years now highlighted the need for reform in the State's business practices with nonprofit contractors, and with Attorney General Eric Schneiderman. I currently serve on his *Committee on Nonprofit Revitalization*.

**Community Focus ♦ Statewide Impact ♦ National Network**

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I wanted to come before this hearing today to try and cut through the sensationalism surrounding this topic, the rhetoric, and misperceptions by laying out for you some simple truths about nonprofits and offering a framework for solutions.

***First, the Truth Is....***The cases of excessive executive compensation and abuse are few and far between and what does exist, needs to be exposed and eliminated.

The very first question I get from the media is, "Do I think there is excessive compensation and abuse in nonprofits?" My answer to that is yes, I agree with Senator Marcellino, the Governor and other key government policy-makers.

***Secondly, the Truth Is...*** Executive compensation and that of other Key Employees is not a secret to the public or the State- the numbers are at your fingertips.

I would like to use the organization I work for, NYCON, to demonstrate how transparent nonprofit finances and executive compensation is to the public – we are just three clicks away. Just go to Guidestar.org and review our publicly available Form 990, filed annually with the Internal Revenue Service. Within moments, you will see that our annual 2010 operating revenue is \$2,475,348. It will also confirm that my direct compensation totals \$110,989. With fringe benefits, my total compensation package is \$130,280.

Disclosure is required by the IRS. And, additional financial information is filed annually with the Attorney General's Office and in most cases, with state agencies through procurement and contract reporting processes.

So the questions have to be raised as to how much money has the State spent to date collecting and analyzing the "new survey" information? How much time and effort did responding nonprofits divert from their mission and services to respond to that survey? How much more taxpayer money do we need to spend to build new bureaucracies to tell us much of what we already know? Ironically, I want to point out that the staff time it took for nonprofits to complete the survey is considered an administrative expense by the State of New York.

***Thirdly, the Truth is...***Under-compensation is a much more prevalent and serious problem with nonprofits that contract with the State than excessive compensation.

Average nonprofits struggle to recruit and retain a qualified and competent workforce, including executive leadership, because our compensation levels are generally not competitive with the public and private sector, there are increasing regulatory and training requirements on staff, and the State rarely pays for the full costs of the services and outcomes it requires.

To give one data example, a 2009 salary study of over 400 community-based nonprofits in New York State conducted by NYCON indicated that the median annual nonprofit executive salary was approximately \$64,000. The story comes into even greater clarity when we consider that the median income of executives at those organizations with a budget under one million dollars was only \$52,000. We are updating that study this year.

***Another truth is...Taxpayers pay for the salaries of many state employees and private, for-profit sector businesses that are not coming under the same scrutiny as charitable organizations.***

When this issue became sensationalized last year, a 2010 salary review by the NYS Division of Budget was (and continues to be) popularly touted. It found that more than 1,926 employees at nonprofits who contract with the State to provide mental hygiene services were paid a salary over \$100,000 with a total cost to taxpayers totaling \$324.6 million. This study fueled the perception that there was something wrong with a nonprofit employee making “six figures.” The Governor’s Executive Order later established a \$199,000 threshold presumably based on the recent survey. The data compiled in this survey still has not been publically released. I do not know where the \$199,000 figure came from.

Just to put things into perspective, a quick review of publicly available data shows that if there are concerns about nonprofit salaries, there should be concerns about “six figure” and “seven figure” earnings in State Government.

During the 2010 fiscal year, the Legislature provided 136 employees at salaries over \$100,000 with a total salary amount over \$16.5 million dollars. A review of the Executive Branch shows an even more compelling result: over 18,000 were employees paid over \$100,000 with an annual cost to taxpayers over \$2.3 billion. This statistic doesn’t include the cost of the generous fringe benefit packages offered to State employees, nor does it take into account the highest compensation to state employees, several of whom make over \$1M. Ironically, included in the top ten is the head basketball coach at SUNY Binghamton, a team that currently has a 0-22 record, making over \$819,000 annually. Clearly that compensation package is not outcome based.

Also, it is important to observe that the State contracts with many for-profit vendors (non-health and human services) and under the guise of “economic development,” provides direct cash subsidy and incentive packages to an increasing number of corporations, such as Global Foundries, with limited or no oversight. Do we know the compensation of these executives and how many of our taxpayer dollars go for that purpose? Is it presumed that these contracted taxpayer dollars are somehow different in value than those that pay for nonprofit services? Do we, as taxpayers, even care? From our perspective, we should.

Our aim is not to malign the compensation levels of the public and private sectors (although I have to question the Coach). The point is that the performance of the nonprofit sector, relied on by the State to produce social and health outcomes in our communities, is dependent, just like other industries, on

recruiting and keeping the best talent to be successful. Fair, reasonable and competitive compensation is an important ingredient in that equation. Nonprofits deserve respect from State Government for the work we do and the leadership and workforce needed to effectively serve our communities.

**Another Truth Is...Charities in New York State, and particularly those that contract with the State, are arguably the most regulated in the Country, and many of these regulations are outdated, piecemealed, and ineffective. Not unlike for-profit businesses, every new regulation, every new reporting requirement, and every new unfunded mandate, comes with a cost.**

The costs for nonprofits to do business with the State of New York are becoming increasingly prohibitive. Administrative costs are rising because of increasing compliance regulations by the State. The administrative expenses of nonprofits who do business with State are driven up by extensive licensing and other standards for mental health, day care and many other services. At the same time, contracting processes and prompt payment problems as pointed out in the aforementioned *2011 Prompt Contracting Report* are chronic and doing serious harm to nonprofits.

As pointed out recently by the New York State Attorney General, the laws specific to charities have not been updated for decades. Recommendations for reform from the Attorney General are forthcoming.

With respect to executive compensation, you will hear or read from the testimony of my respected colleagues, the details of existing IRS regulations for Board's to set executive compensation and federal "intermediate sanctions" currently in place to identify and remedy cases of excessive transactions with nonprofits.

**We propose that a dynamic and effective partnership be developed between nonprofits and State Government so that we can solve the real problems we face, *together*.**

While the current climate is recognized by most all decision-makers and policy-shapers, the truth is that each and every attempt at reforming the nonprofit business relationship with the State of New York has been conducted in a silo. Whether it's legislative initiatives to curb compensation, the Governor's *Medicaid Redesign Task Force and SAGE Commission*, the Attorney General's *Nonprofit Revitalization Committee*, or efforts undertaken by the State Comptroller to reform the contractual relationship.

*In order to protect and enhance our nonprofit community*, the real conversation must be about how we can work together to overcome the challenges facing our State, and actually giving nonprofits a seat at the table.

The State of New York needs to enact comprehensive reform measures and do so in a coordinated fashion. While the Senate has not developed any explicit proposals, a review of the recent proposals from the Executive Chamber will help us identify why a larger reform movement needs to be undertaken in order to protect and enhance New York's nonprofit community.



**We ask that you consider the following:**

1. **The Internal Revenue Service (IRS), State Attorney General, and individual New York State Agencies already possess compensation oversight mechanisms.** The IRS suggests the establishment of a process by which Executive Compensation should be determined, and oversight maintained, by a Nonprofit Board of Directors.

The State Attorney General's annually required submission of a CHAR 500 form requires submission of a current IRS Form 990, as well as an Audit or Review Report for organizations reporting more than \$100,000 in revenue or support.

For many organizations receiving funds from the State of New York, the target of the current Executive Order, executive compensation and administrative overhead rates are already limited in many cases via contractual agreement for services provided. In many cases, the proposed compensation cap and administrative overhead rate are actually *higher* than those already outlined by regulation – how much is that really going to save taxpayers?

**Nonprofit compensation and revenue levels are already available at your fingertips.** As I alluded to in my introduction, just a few clicks of the mouse would allow the State to use already-available data in order to investigate nonprofit compensation levels. This publicly available information includes compensation levels for all key staff of the corporation, as well as any compensation provided to the membership of its Board of Directors. If only we could say the same about the private sector who contract with the State of New York.

2. **The proposed system provides exemptions and waivers which we believe will result in exceptions for those organizations whose compensation levels are most likely to “shock the conscience.”** Let's be honest about why we're sitting here today: taxpayers and lawmakers alike are frustrated with the economic climate, and it's a shock to us all when we see a charitable nonprofit executive making hundreds of thousands of dollars in direct compensation or engaged in nepotism using charitable or taxpayer dollars.

Whether it is a college president making \$2 million in compensation (not including compensation from outside entities for board service) or a nonprofit hospital executive: the nonprofit sector (like its private sector counterparts) has a very small number of highly compensated individuals.

This system, by way of regulations concerning the delineation of State funds vs. privately-generated funding, will generate an environment where those organizations who can afford elaborate accounting and compliance divisions will be able to side-step the original intent of this Executive Order and complimenting budget language, and attempts for carve outs are occurring

as we speak. In my opinion, those with the deepest pockets and most influence will achieve their goal.

- 3. The proposed system is not consistent and will create new expenses for taxpayers.** Under the currently enacted Executive Order, all contracting State Agency heads will have the authority to issue a waiver, though the specifics of why and how that waiver will be granted, along with a specific application process, has not been outlined.

This will undoubtedly create a chaotic situation where nonprofits who do business with more than one State Agency, as many of our members do, may find themselves unable to manage what will be a burdensome and confusing process with separate State Agencies.

We have still not heard from the Executive Chamber what the estimated cost of this program will be, however one can only imagine what the added cost will be of more staff at each State Agency tasked with overseeing, monitoring and evaluating the implementation of the order.

We are confident that neither the Governor, nor other policy-makers, intended to develop a system that will likely cost taxpayers more than it saves and will not provide the desired results.

### **What Is The Solution?**

Whether it's the annual Prompt Contracting Report, the upcoming results of the Attorney General's *Nonprofit Revitalization Committee*, or the inevitable results of the *SAGE Commission* and *Medicaid Redesign Team*; the message is clear: the State of New York needs to better coordinate efforts, focus resources, and streamline its attention to the business relationship with the nonprofit sector. We stand ready to openly and in good faith, to participate.

It is in that spirit that we point to solutions similar to those recently enacted by the State of Connecticut and their decision to hire a cabinet-level appointee whose sole purpose is to help manage the myriad issues related to the State-nonprofit relationship. In addition to appointing former State Representative Deb Heinrich to the cabinet-level position of *Nonprofit Liaison to the Governor*, Governor Dannel Malloy has convened a *Cabinet on Nonprofit Health and Human Services* that is co-chaired by Ms. Heinrich and the President/CEO of The Access Community Action Agency.

**We point to contracting solutions highlighted by our colleagues from the New York City area submitted testimony before this hearing. And, we point to solutions already proposed by the State Comptroller forthcoming from the Attorney General.**

**The time is now** comprehensively reform the state’s contractual and business environment and get on to the business of removing ineffective regulations that prevent nonprofits from delivering services more efficiently to New Yorkers in need.

**The time is now** for us to join in a commitment to move forward together maintaining and building public confidence in the state-nonprofit partnership to achieve results we all desire.

**The time is RIGHT NOW for us to work together to improve and share the truth about nonprofits.**

Today, I am asking leaders in both the Legislature and the Executive Chamber to join us in committing the attention and resources necessary to developing a cabinet-level liaison within the Executive Chamber. If we are to improve the health of New York’s vibrant nonprofit sector, we must enact comprehensive reform efforts and they need to be coordinated by a single entity.

The State truly can save money, and nonprofits can run more effectively, by ensuring a robust dialogue with stakeholders and a coordinated approach to reform that reflects the intelligent approach to policy-making that New Yorkers deserve.

In doing so we will manage more effective and efficient compliance programs as well as remove onerous burdens placed upon nonprofit corporations that don’t add value or result in meaningful oversight. And we will finally achieve the universally desired result: **seeing more dollars spent on vital services that New Yorkers need.**

Again, I thank you for the opportunity to speak today and yield the remainder of my time – and any additional time that the Chairman views necessary – for questions.

**Senate Standing Committee on Investigations and Government Operations**  
**Executive Compensation at Not-for-Profit Organizations**  
**February 6, 2012**

*Overview and Introduction:*

On behalf of the more than a dozen undersigned associations and coalitions of not-for-profit organizations, we understand and appreciate the concern that has arisen over reports of excessive compensation in organizations—not-for-profit or otherwise—that contract with the State. We believe, however, that more effective and targeted approaches could be taken to address any legitimate concerns over compensation and administrative expenses incurred by certain state contractors than have been advanced in the Executive Budget or in the Executive Order and would urge the Legislature to consider the alternative approaches outlined below to address these issues.

It is important to approach the issues of executive compensation and administrative expenses in not-for-profit organizations with an understanding of the important role played by the not-for-profit sector in New York, the complexity and diversity of these organizations, the already extensive regulation that governs not-for-profit corporations and the potential unintended consequence of new, across-the-board state mandates on these organizations.

We do not dispute that some entities contracting with New York State have abused their trust, departed from their mission and failed to abide by the executive compensation standards and procedures that already apply to tax-exempt not-for-profit organizations. We believe additional steps should be taken by New York State to hold not-for-profit boards and executives accountable for compliance with reasonable compensation policies and to ensure that state support is directed efficiently and cost-effectively to serve the intended beneficiaries of state funding. We respectfully submit, however, that arbitrary, inflexible, across-the-board approaches that purport to redress abuses that are neither widespread nor currently unregulated will penalize honest and ethical not-for-profit organizations and the needy New Yorkers who are the ultimate beneficiaries of their services and could do unintended and irreparable harm to the New York not-for-profit sector.

*The role of not-for-profit agencies in New York:*

The not-for-profit providers of health and human services that are members of the undersigned organizations have provided essential services to needy New Yorkers for, in some cases, a century or more. They have done so at the express urging of a State government that recognizes that it cannot provide these services nearly as well or as cost-effectively as these mission-driven organizations. Not-for-profit service providers represent a very significant part of the New York State economy, employ more than a million New Yorkers, provide the lion's share of health and human services to all New Yorkers, and, in particular, are irreplaceable elements of New York's safety net for our most vulnerable citizens.

According to a recent report from the Office of the State Comptroller, New York State has nearly 27,000 registered nonprofits and the State has entered into more than 22,000 active

contracts with these organizations to provide critical services to New Yorkers.<sup>1</sup> According to a just released report from the Center for Civil Society Studies at Johns Hopkins University, 1,246,900 New Yorkers are employed by not-for-profit organizations, representing 18.1% of all private sector employees—and, while the for profit sector has actually declined nationally by an annual rate of .6 percent over the past decade, the nonprofit sector has grown by an average of 2.1% per year.<sup>2</sup> Of the top twenty employers in New York State, nine are not-for-profit organizations, four of which number among the State's top ten employers.<sup>3</sup>

A study by the Long Island Association found that not-for-profits accounted for 11.0 percent of total employment on Long Island in 2010 with an annual payroll of \$6.4 billion in 2010—and that the 132,640 nonprofit jobs on Long Island generated another 88,500 additional jobs in Nassau and Suffolk Counties, accounting for a total payroll of nearly \$11 billion.<sup>4</sup> Independent, non-profit colleges and universities are responsible for generating 174,000 jobs with a payroll exceeding \$10.7 billion and contribute \$54.3 billion to the State's economy.<sup>5</sup> It was likewise estimated that the early child care and education field accounted for nearly 120,000 jobs and \$4.7 billion in economic activity—while enabling 750,000 parents to maintain their employment.<sup>6</sup>

Although the not-for-profit sector has been a vibrant contributor to the State's economic activity, it is also affected by the severe economic downturn: reduced governmental funding at all levels as well as diminished charitable giving have caused considerable financial distress to not-for-profit organizations across the State.

The economic contributions made by the not-for-profit sector in New York are, in any event, only part of the story: without not-for-profit organizations, essential public services—education, health care, and a broad array of other services for disabled, disadvantaged and aging New Yorkers—would either not be provided at all or would be provided by the public sector at substantially greater cost to the taxpayer. Generally speaking, when these services are delivered by the public sector, the overall costs of administration, overhead, salaries and benefits are higher, not lower, than when delivered by not-for-profit organizations. Fringe benefit costs alone for public sector employees are roughly twice what are incurred in the not-for-profit sector. The mission-driven not-for-profit sector has also long been credited, moreover, with providing these services at a level of quality that at least equals, and often exceeds, that of the public sector.

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<sup>1</sup> Office of the New York State Comptroller, *"New York State's Not-for-Profit Sector: Delayed State Contracts and Late Payments Hurt Service Providers,"* November, 2011.

<sup>2</sup> L. Salamon, et al., *"Holding the Fort: Nonprofit Employment During a Decade of Turmoil,"* Johns Hopkins University Center for Civil Society Studies, January, 2012, pp. 3, 5

<sup>3</sup> Center for Governmental Research, *"Economic Impact of the University of Rochester and its Affiliates,"* April, 2010, p. 13.

<sup>4</sup> Long Island Association, *"Long Island's Not-for-Profit Sector: Doing More With Less During a Period of Economic Change,"* June, 2011, pp. 6, 10.

<sup>5</sup> Commission on Independent Colleges and Universities, *"Economic Impact of Independent Colleges and Universities in New York State."*

<sup>6</sup> Cornell University Department of City and Regional Planning, *"Investing in New York: An Economic Analysis of the Early Care and Education Sector,"* April, 2004.

In sum, given the role that not-for-profit entities play in New York—both economically and as the principal safety net service provider for our most vulnerable citizens—it is essential that proposals that might negatively impact on the not-for-profit sector be viewed with caution and we would urge this Committee and the Legislature to approach the issue with these consequences in mind.

***Existing oversight of executive compensation and administrative costs:***

Not-for-profit organizations are already subject to rigorous federal and state oversight that includes regulation of excessive executive compensation and administrative expenses. The Attorney General's Office is authorized by the Not-for-Profit Corporation Law (N-PCL) and the Estates, Powers and Trusts Law (EPTL), as well as by common law, to exercise comprehensive regulatory authority to supervise the operation of the state's not-for-profit corporations, including the reasonableness of compensation.<sup>7</sup> The Attorney General is given explicit authority to seek remedies of wrongdoing by not-for-profit entities, including actions directly against officers and directors that might have engaged in unlawful conduct. The authority includes the right to seek the removal of directors who authorize or acquiesce in payments or practices that are deemed inappropriate.<sup>8</sup> In 1997, the Board of Regents removed 18 of 19 trustees of Adelphi University for neglect of their fiduciary duties relating to an excessive compensation package for their former President and, in 1998, an action brought by the Attorney General against the former trustees for breach of fiduciary duty was upheld.<sup>9</sup>

Since the mid-1990s, the Internal Revenue Service has enforced clear guidelines on executive compensation that must be observed by tax-exempt not-for-profit entities. As a result, excessive compensation paid to board members and the executive leadership of the organization, as well as to anyone else who has substantial influence over the affairs of the corporation, is subject to disclosure and to IRS scrutiny. Very substantial tax penalties are levied on executives that receive excessive compensation—known as an “excess benefit transaction”—and, in appropriate cases, additional substantial liabilities are imposed directly upon members of the board of a not-for-profit entity that approved the compensation package.<sup>10</sup>

In reviewing whether the compensation is reasonable, the IRS reviews what compensation is received for similar services by similar organizations (whether for- or not-for-profit) and under similar circumstances.<sup>11</sup> Entities must demonstrate that the board actually undertook a process to establish the reasonableness of compensation. The IRS will presume the reasonableness of a compensation process if the governing board actually reviews, makes and documents the salary compensation determination, without a conflict of interest, and after obtaining and considering appropriate data and comparability information to make a reasonable fair market determination of an appropriate level of compensation.<sup>12</sup>

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<sup>7</sup> N-PCL §202(a)(12).

<sup>8</sup> EPTL §8-1.4(m) and (n) and N-PCL §112(a)(4), 706(d) and 714(c).

<sup>9</sup> *Committee to Save Adelphi v. Diamandopolous*, Regents of the University of the State of New York, February 10, 1997; *Vacco v. Diamandopolous*, 185 Misc. 2d 724 (Sup.Ct. N.Y.Co., 1998).

<sup>10</sup> IRC §4958.

<sup>11</sup> Treas. Reg. §53.4958-4(b)(1)(ii)(A).

<sup>12</sup> Treas. Reg. § 53.4958-6(a).

In addition, a host of reimbursement and payment rules, adopted by virtually all relevant state agencies, are directed at ensuring that state funding is used primarily to support direct care services and to limit administrative costs. For example, certified home health agencies have, for many years, been subject to a cap on administrative expenses, while other Medicaid-funded providers have had to distinguish between allowable (and reimbursed) and non-reimbursable costs.<sup>13</sup> By statute, the State's Neighborhood-based Initiative program imposes a maximum percentage on administrative costs,<sup>14</sup> and nursing homes, Medicaid-funded clinics and substance abuse programs have also been subject by the Legislature to administrative cost caps<sup>15</sup>—just to name a few. Payments for administrative expenses incurred by Medicaid-funded managed care and coordinated care organizations are limited by contract. Nothing precludes state agencies from tailoring administrative expense limitations to the specific circumstances of their service systems—nor requires an across-the-board approach to containing the costs of administrative overhead.

Despite this extensive regulation, we cannot deny that there have been isolated instances in which excessive compensation has been paid. Nothing we submit here should be construed as either denying that abuses have occurred within the not-for-profit sector or condoning them. It should be noted, however, that no evidence has been advanced that suggests that widespread abuse has occurred in executive compensation or administrative expense in the not-for-profit sector in New York, among either agencies that heavily rely on state support or among those that do not. Although a Task Force on Not-for-Profit Entities was convened last summer that required not-for-profit organizations to submit very substantial information relating to their compensation practices, no analysis of the collected data has yet been released. Nor has the case been made that would support subjecting every entity that receives state support to “one size fits all” limitations on compensation and administrative expense, which do not take into account the unique nature, complexity, size or location of the contracting party or the implications on the recruitment of qualified executive leadership in the not-for-profit sector.

***The Article VII legislative proposal and the Executive Order:***

In the 2012-13 Executive Budget, legislation was proposed that would authorize a broad array of state agencies to limit the extent to which state funds may be used to support administrative, rather than direct care or services, and to preclude state reimbursement for executive compensation in excess of \$199,000 per year. Immediately after the legislation was submitted, Governor Cuomo issued an Executive Order that directs state agencies to implement the same limitations. In both instances, if a contracting entity fails to satisfy the executive compensation and administrative spending caps, the entity's contract could be terminated or not renewed and/or state funding could be terminated.

Specifically, under the Executive Budget and the Executive Order, certain designated state agencies<sup>16</sup> would have the authority “to promulgate regulations or to address by other

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<sup>13</sup> PHL §3614(7).

<sup>14</sup> Exec. L. §548-f(4)(d).

<sup>15</sup> PHL §§2808, 2807(14) and MHL, §25.09

<sup>16</sup> The affected agencies in the legislation include, but are not limited to, the Office for People with Developmental Disabilities (OPWDD), the Office of Mental Health (OMH), the Office of Alcoholism and Substance Abuse

means the extent and nature of a provider's administrative costs and executive compensation which shall be eligible to be reimbursed with state financial assistance or state-authorized payments for operating expenses," as detailed below:

- *Cap on "Administration" Expenses:* At least seventy-five percent of the "state financial assistance or state-authorized payments" for operating expenses of contracting entities must be "directed to provide direct care or services rather than to support the costs of administration"—terms that the applicable state agencies would be authorized to define. The mandated "direct services" percentage would increase by five percent per year until, no later than April 1, 2015, it reaches eighty-five percent, where it would remain thereafter.
- *Cap on Executive Compensation:* The legislation would also provide, "to the extent practicable," that state reimbursement would not be provided for "compensation paid or given to any executive by such provider in an amount greater than \$199,000 per annum." The task of defining "compensation" and "executive" would be left to the applicable state agency. The \$199,000 cap on state-supported compensation could be adjusted annually by state agencies, subject to the approval of DOB, but may not exceed "Level I of the federal government's Rates of Basic Pay for the Executive Schedule promulgated by the United States Office of Personnel Management," which is currently at essentially the same level.<sup>17</sup> In addition, a contracting entity may seek a waiver from compliance with this requirement from the state agency and DOB. Absent such a waiver, non-compliance with this provision may, in the sole discretion of the commissioner of the applicable agency, result in the termination or non-renewal of the state contract or the termination of state support of the contracting entity.

The Executive Order and the legislation would apply the compensation and the administrative cap to "providers of services that receive reimbursements *directly or indirectly*" from the listed state agencies.

***The proposed legislation and the Executive Order are neither effective nor fair approaches to the issue and will jeopardize the ability of not-for-profit organizations to meet their missions.***

Taking a "one-size fits all" approach to addressing the compensation and administrative spending practices of tens of thousands of not-for-profit organizations will not effectively curb excessive compensation by the handful of offending entities and will do harm to an already fragile New York State not-for-profit infrastructure. Rather than focusing scarce enforcement

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Services (OASAS), the Office of Children and Family Services (OCFS), the Office of Temporary and Disability Assistance (OTDA), the Department of Health (DOH), the State Office for the Aging (SOFA), the Division of Criminal Justice Services (DCJS), the Office of Victim Services (OVS) and the State Education Department (SED) The Executive Order applies to the same agencies, except the State Education Department, presumably due to its independent status.

<sup>17</sup> The referenced current salary schedule for such a position is \$199,700 and has been frozen since 2010.



and regulatory resources on the entities that may be the actual wrongdoers, the proposal will, at a minimum, impose significant compliance costs on the vast majority of responsible contractors and will place the not-for-profit sector at a distinct competitive disadvantage as it competes for executive talent.

The proposal fails to recognize the vast disparities and variations among contracting entities and the services they render. The many thousands of not-for-profit entities that contract with State government are a hugely diverse lot, ranging from small not-for-profit entities with total revenues less than the \$199,000 executive compensation cap to entities that administer over one billion dollars in revenue and oversee vast and complex service delivery systems. The notion that a single salary level should be set for each of these diverse entities—including for-profit companies that contract with state agencies—is simply unsupported. Likewise, imposing a single administrative services percentage on a vast array of entirely disparate organizations ignores real differences in how services are rendered across the wide array of state programs that would be subject to the limitation and varying circumstances that might warrant higher or lower expenses in this category.

The proposal ignores the specialized expertise and experience that may be required by contracting entities. Many of the services rendered by contracting not-for-profit entities require uniquely qualified executive leadership to oversee the delivery of highly specialized and complex services. Take, for example, the necessity for medical leadership in certain not-for-profit entities: a large New York City based HIV services organization that requires a medical director to oversee its complex service delivery system will simply not be able to recruit a qualified physician to perform those tasks at the prescribed compensation level. Likewise, services related to care for the elderly, disabled or abused children may require executive leadership with the requisite background, professional licensure or certification, which may not be possible to find at salaries below the cap.

The proposal will render not-for-profit entities unable to compete for the best executive leadership. Leadership matters. An artificial cap on executive compensation will substantially impair the ability of not-for-profit entities to recruit and retain highly capable, experienced and specialized executive leadership—and the quality and cost-effectiveness of the services provided by these entities will suffer as a result. Although the IRS standards focus on the comparability and the reasonableness of the compensation, viewed in the context of the human resources marketplace for executives leading similar organizations, the proposed legislation and Executive Order do not consider what it will actually take to recruit qualified leadership to these organizations. The failure to take into account the considerable geographic differences in the cost of living throughout New York State is just one critical missing element that makes the proposal unrealistic and unworkable.

The proposal will disproportionately impact on the delivery of services to the most disadvantaged New Yorkers. Both the cap on executive compensation and the limit on administrative expenses only apply to expenses financed with “state financial assistance or state-authorized payments.” While the proposal is not entirely clear on this point, for- and not-for-profit contracting entities that receive a substantial amount of their revenue from non-state sources may be able to supplement compensation over the established levels and exceed the

administrative expense limitation, as long as they can demonstrate that these excesses are supported by non-state dollars.<sup>18</sup> Conversely, a contractor that is entirely or virtually dependent upon State support would be fully subject to the caps. Even if that entity's revenues are derived from multiple state sources, the caps on executive compensation and on administrative expenses would be applied to those state revenues in the aggregate. "Safety-net" organizations that devote themselves entirely to serving the most vulnerable New Yorkers are most likely to be those most dependent on State support and would, accordingly, be disproportionately affected by these limitations. These organizations would be unable to compete for the executive leadership against those entities that are effectively exempt from these requirements because of their non-state sources of revenue. Any proposal that disproportionately impacts upon services to the most disadvantaged New Yorkers should be seriously and critically examined.

The proposal is inconsistent with state policies that already seek to contain administrative costs. As noted above, many state agencies already condition—by statute, regulation or contract—the extent to which state funds can reimburse administrative or overhead expenses. The proposed limitations on administrative expenses in the Executive Budget and the Executive Order may be inconsistent with or otherwise complicate these already existing limitations on non-direct service expenditures. The diversity of programs and services makes it impossible and unwise to establish one correct ratio of administrative to direct care expense. Instead of enacting an inflexible, statewide approach to restraining administrative costs, it makes substantially more sense to permit state agencies to address these issues on a program by program basis with percentages or fixed dollar amounts that are tailored to the particular program and service—particularly since most state agencies have already done so.

The proposal is contrary to state policies that have urged consolidations and affiliations among state-supported contracting entities. Governor Cuomo has urged both public and private entities to examine whether consolidation or affiliation among and between entities that provide services to the public may result in the more cost-effective delivery of public services. State agencies, school districts, local governments and health care and human services providers have been encouraged to merge, consolidate or affiliate to become more efficient. While the State would presumably permit four contracting entities, funded by state revenues, to compensate their executives at \$199,000 each, the merger of those four entities into a single, presumably more efficient, provider of service would subject the combined entity to the same compensation limitation. It would be highly unlikely that a qualified executive could be hired who would be willing to lead the much larger and more complex organization for the same salary of the smaller merging entities.

At the same time, the Medicaid Redesign Team (MRT) has emphasized the need to transition the Medicaid program from the current fee-for-service payment system, which reimburses tens of thousands of providers, to an emphasis on coordinated care, which will involve direct state payment to a much smaller number of managed care plans and other care coordination entities. These entities would then be held accountable for administering hundreds of millions of dollars of Medicaid revenues that pay for care rendered to their enrollees, making

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<sup>18</sup> Even these entities would, however, incur additional compliance costs to be able to properly demonstrate that their internal allocation of resources satisfied the provisions of the legislation and the Executive Order, presumably further adding to their administrative costs.

them essentially comparable to some of the large publicly-traded health insurers in the size and scope of their operations. Making these largely state-funded entities subject to an executive compensation cap that completely ignores the actual market for executives in the health care management and insurance marketplace would deprive these entities of the specialized and experienced leadership that these entities require and would seriously undermine the policy direction sought to be advanced by the State of New York.

*The proposal is potentially subject to inconsistent application.* A host of terms used in the legislation and Executive Order are undefined and will require regulatory clarification by the various agencies charged with implementing these new mandates. What, for example, is included within “direct care or services” versus “administrative costs”? Will investments in information technology and other quality improvement expenditures be viewed as “administrative” costs that would be discouraged by the proposal? Which “executives” will be subject to the compensation limitation? What is included in the “compensation” cap of \$199,000: is that just salary or salary and other benefits, including health, disability and retirement benefits? What State funding is encompassed by “State financial assistance or State-authorized payments for operating expenses”? And what is meant by including “providers of services that receive reimbursements directly or indirectly” from state agencies? Would this provision subject any and every sub-contractor of the contracting party since they “indirectly” receive state funds?

The legislation and the Executive Order contemplate that each of the state agencies will promulgate their own regulations to implement these requirements. It is not entirely clear what may be worse: On the one hand, if nine state agencies issue nine different interpretations of these key terms and adopt nine different approaches to the implementation of these mandates, contracting agencies would be particularly challenged if they receive state financial support from more than one state agency. On the other hand, a single set of definitions might be developed by these state agencies that ignores the substantially different services provided by an entity that is funded by, say, the Office for the Aging, as opposed to one supported by the Division of Criminal Justice Services. In short, virtually any approach to the micro-managing of the not-for-profit sector by state agencies runs the risk of doing more harm than good.

#### **An alternative approach:**

We believe there are steps that might be taken to enhance existing requirements relating to state contracting with not-for-profit entities that address these issues in a far more targeted and effective way. Rather than rely on State-issued governmental guidelines that dictate salary and administrative expense levels for thousands of organizations, we recommend that the Legislature instead strengthen existing laws and rules that will continue to hold the contracting organizations themselves accountable for the discharge of their obligations in setting reasonable compensation and administrative costs. In lieu of the Governor’s legislative and Executive Order proposals, we would urge you to substitute proposals that would strengthen enforcement of the already existing regulatory requirements, such as the following:

- *Amend the Not-for-Profit Corporation Law to require not-for-profit boards to apply the Internal Revenue Code's reasonable compensation standards for tax-*

*exempt organizations.* To make absolutely clear that not-for-profit entities in New York are held accountable for compensation determinations they make, legislation should be adopted to mandate compliance with the existing tax-exempt organization requirements. The legislation may specifically require the adoption of compensation policies and procedures that will satisfy compliance with these requirements, including, where appropriate, policies that would require the boards to compile and review sufficient information to support the reasonableness of executive compensation.

- *Authorize the Attorney General to enforce these requirements and to require the corporation to produce evidence of its compliance with these standards, upon request.* The Legislature could authorize the Attorney General to investigate and review compliance by not-for-profit entities with the compensation requirements described above. The legislation could direct contracting state agencies to refer matters involving potentially excessive compensation to the Attorney General's Charities Bureau for further review or the Attorney General might undertake that review, as appropriate, as part of his approval of all state contracts, where excessive compensation may have been alleged. Where a contracting entity is unable to provide adequate justification for the executive compensation it provides and refuses to comply with the existing IRS standards that govern compensation, the Attorney General and/or the state agency should be given enforcement authority to take appropriate action to terminate the state contract and to hold the board of the organization accountable for the excessive compensation. Rather than having these compensation standards enforced in haphazard and inconsistent ways by the various affected state agencies, the office charged with the oversight of not-for-profit organizations in New York would provide a more consistent review of these practices.
- *Provide sufficient resources to the Attorney General's Charities Bureau to enforce these requirements:* It has been suggested that the Attorney General's Charities Bureau may not have sufficient legal or investigative resources to fulfill either its existing responsibilities or an expanded mission. While we would defer to the Attorney General's office as to the level of resources that might be necessary, we would support consideration of dedicating appropriate fee increases or other resources to ensure that the Bureau has the resources that it needs to meet its public protection responsibilities.
- *Require State agencies to adopt reimbursement and contracting practices that ensure that administrative expenses remain within appropriate levels, taking into account the specific services being rendered and other factors that may dictate the appropriate level of "overhead."* As also noted above, many state agencies already have adopted reimbursement and contracting policies aimed at limiting the extent to which state funds are utilized for administrative expenses. The Legislature could require all state agencies to promulgate regulations or to adopt contracting policies that would ensure that services are being rendered as efficiently as possible. Rather than imposing a statewide and program-wide

administrative cost mandate, state agencies should be required to tailor their reimbursement and contracting policies to minimize administrative expenses, without being saddled with an across the board and potentially arbitrary administrative cost limitation that may be either too generous or too limiting for any particular program or service.

We appreciate your consideration of these alternative approaches and would be prepared, along with our colleagues in the not-for-profit sector, to work with you in the development of sound policies to address these issues that recognize the importance of the not-for-profit sector and the complexity and diversity of the services and programs that they deliver.

Respectfully submitted,

**Association For Community Living  
Black Agency Executives  
Catholic Charities of the Archdiocese of New York  
Catholic Charities Neighborhood Services, Diocese of Brooklyn and Queens  
Coalition of Behavioral Health Agencies  
Family Planning Advocates of New York State  
Federation of Protestant Welfare Agencies  
Human Services Council of New York  
Long Island Coalition of Behavioral Health Providers  
Mental Health Association of New York City  
Mental Health Association of Westchester  
New York State Coalition for Children's Mental Health Services  
New York State Council for Community Behavioral Healthcare  
Supportive Housing Network of New York  
UJA/Federation of New York  
United Neighborhood Houses of New York**

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**Testimony of the  
New York State Nurses Association  
Before the  
Senate Standing Committee on Investigations and  
Government Operations on Compensation Levels  
of Executives at Not-For-Profit Organizations**

**February 6, 2012**



**11 Cornell Rd, Latham, NY 12110  
Governmental Affairs Department  
PH: 518-782-9400, ext. 283  
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## **Testimony for Compensation Levels of Executives at Not-For-Profit Organizations**

Good Morning/Good Afternoon, my name is Jayne Cammisa, and I am a registered nurse at Westchester Medical Center. I am also a member of the New York State Nurses Association. Thank you for letting me speak today in regards to the exorbitant executive salaries in some of New York's hospitals and nursing homes.

According to 2009 financial reports, Westchester Medical Chief Executive Officer Michael Israel was paid \$1.2 million. Our Chief Operating Officer Gary Brudnicki was paid \$738,800, while 36 other executives were paid between \$128,000 and \$530,000. Wouldn't some of this money be better spent on cultivating a stable RN workforce to provide quality patient care?

In the middle of contract negotiations this past October, the Nurses Association received notice that the facility would be eliminating 250 RN positions. An estimated 139 of these positions are nurses who work at the patients' bedside. Other planned layoffs will affect direct-care providers such as nurse practitioners, clinicians, specialists, and positions that provide support, such as managers, supervisors, coordinators, and the entire Education Department of this Level 1 trauma teaching hospital. This staggering 19% cut in the direct-care nursing workforce at Westchester Medical Center is simply too much for the remaining staff to bear. RNs are already reporting that they are working short-staffed, and many have been doing so since layoffs at the medical center in 2003 and 2004. Staffing levels are an issue of concern because studies have linked poor staffing with higher incidences of adverse patient outcomes. My colleagues and I cannot comprehend why those at the bedside are being sacrificed while some executives continue to line their pockets at the taxpayer's expense. The executives at our facility need to do the right thing. Cuts should begin with executive salaries, not caregivers at the bedside. What kind of message does this send not only to the other staff, but to the patients we serve, and the community, as a whole?

Even in current contract negotiations, Westchester Medical Center management is aggressively seeking cuts to nurses' benefits and wages, while refusing to commit to severe cuts in management salaries and benefits or discuss the millions spent on outside contracts. Our negotiating committee offered \$9 million in various givebacks to our employer only to be told that we didn't work hard enough on our proposal. Westchester Medical Center faces the same dilemma as other healthcare facilities in New York State, yet others haven't made cuts of such magnitude.

Westchester Medical Center has the highest case mix index in the country, and is the only burn unit between New York City and the Canadian border. It's also the only level one trauma center

between New York City and Albany, supporting patients from seven counties. Having committed, high quality, highly credible nurses at the bedside is vital to the survival of patients and to Westchester Medical Center. The layoffs at my facility will severely impact the safety and delivery of quality care not only in Westchester, but for the entire Hudson Valley area. This will not be world class medicine.

Recently, Governor Cuomo said that not-for-profits that provide services to the poor and needy must work to prevent public funds from being diverted to excessive compensation and unnecessary administrative costs. The Governor issued an executive order that would cap both executive compensation and administrative costs paid by the state to not-for-profit and for-profit service providers.

My colleagues and I at Westchester Medical Center and the New York State Nurses Association applaud the Governor and this committee for working to keep non-profit executives accountable for their salaries and better aligned with their not-for-profit missions.

Thank you for letting me speak today.



● Attachment B ●

Submitted Written Testimony



**TESTIMONY BEFORE THE SENATE COMMITTEE  
ON INVESTIGATIONS AND GOVERNMENT OPERATIONS**

**Executive Compensation at Not-for-Profit Organizations  
Receiving State Funding**

**February 6, 2012  
Hearing Room A, Legislative Office Building**

**Testimony of:**

**NEW YORK STATE REHABILITATION ASSOCIATION**

**By:**

**Jeff Wise, JD  
President / CEO  
New York State Rehabilitation Association  
155 Washington Avenue, Suite 410  
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**Senator Marcellino and Committee Members: NYSRA greatly appreciates your invitation to appear in person to deliver testimony at this hearing on an important topic. Unfortunately, because of the change in date of the hearing, we are unable to personally appear. We are grateful for the opportunity to submit the following written testimony and apologize for our being unavoidably unable to attend.**

## **INTRODUCTION**

NYSRA, formed more than 30 years ago, is a statewide trade association of not-for-profit providers of services to New Yorkers of differing abilities. Our providers and their direct-care staff are key components of the state's delivery system of services to people with developmental disabilities, mental health diagnoses, learning disabilities, and other conditions. Our approximately 100 provider agencies deliver myriad services to New Yorkers, including vocational rehabilitation, residential care, day programs, clinical services, and other supports.

In recent months, questions have surfaced in New York State around the compensation of executives at not-for-profit organizations that receive funding from State revenue sources. Notably, news articles focusing on a small number of such agencies licensed by and funded through the Office for People With Developmental Disabilities (OPWDD) have been published and served as the foundation for public discourse on the matter of compensation of executives.

In January, Governor Cuomo, through his submitted Executive Budget for the 2012-2013 State Fiscal Year as well as in a separate, virtually identical Executive Order, has further focused attention on compensation and operations of agencies (both for- and not-for-profit) that provide services under contract with the State. The Governor proposes certain limitations on state reimbursement of executive salaries at such agencies and also prescribes the percentage of state funds that must be used for services, rather than administration, of the agencies.

NYSRA agrees that such issues are pertinent. It does not condone wasteful spending by any entity with which the State contracts to provide services and supports to New Yorkers who need them. We understand both the concerns of the Governor and this Committee with regard to appropriate spending and service delivery. As outlined below, however, we believe there are ways to protect the taxpayer, ensure effective and efficient service delivery to people in need, and guarantee the integrity of the systems in issue without further legislation or policy change.

## **EXISTING STATE MECHANISMS**

The not-for-profit agencies that constitute NYSRA's membership are community, mission-driven organizations governed by volunteer Boards of Directors. These Boards are populated by community-minded citizens and taxpayers who work to ensure that services and supports are delivered to New Yorkers who need them by responsible not-for-profit agencies. These agencies are subject – as they should be – to close regulation by the State government, whose interest lies

both in the guarantee of service delivery to people in need as well as in protecting the public purse.

Our agencies operate under myriad rules, regulations, licensing requirements and statutes. Among these are the Not-for-Profit Corporations Law, the Estate Powers & Trusts Law, various Public Health statutes, the Mental Hygiene Law, Medicaid rules and regulations, and statutory and common-law provisions regarding fraud. State oversight of our agencies is seated in the Attorney General, the Office for People with Developmental Disabilities, the Office of Mental Health, and the Office of the Medicaid Inspector General. In various ways and to varying degrees, all of these State agencies prescribe – and proscribe – practices with regard to the operation of community-based agencies that provide services to people they serve.

These controls and this oversight regarding service providers are substantial. Not-for-profit organizations delivering service to needy New Yorkers are subject to audits from multiple agencies, quality assurance guidelines, and oversight that is designed to ensure both the efficacy of their services and their integrity of their operations.

Aside from the notable exceptions that have been the subject of recent publicity and attention, we are not aware that there is widespread abuse of the public trust by our agencies. We believe the abuses that have been reported – which are very few – are, in fact, extraordinary exceptions, newsworthy for their rarity. Existing mechanisms work to make this so. We believe it should be noted that one exception, publicized last summer, was itself the result of an investigation by the Office of the Attorney General that resulted in the departure of executives from the not-for-profit being examined. Existing protections do, in fact, work to identify and resolve such situations – as they should.

## **FEDERAL IRS APPROACH**

Given the significant role played by Medicaid in New York's systems of services and supports for people with disabilities, a great deal of federal oversight of provider operations is present on a regular basis. Providers are subject to a considerable federal, as well as State, scrutiny.

For the purposes of this hearing, however, perhaps the most pertinent requirements are those of the Internal Revenue Service (IRS) and its governing powers relating to not-for-profit status of our community service providers. For many years the IRS has applied an executive compensation analysis that focuses attention on not-for-profit boards, their governance principles and the integrity of their operations with regard to setting salaries of agency executives. This is done both through statute and regulation.

Internal Revenue Code §4958 identifies highly specific requirements imposed on governing boards of not-for-profit corporations and their oversight. Moreover, Treasury Regulation 53-4958-6, read in conjunction with the authority in the above-cited statute, sets out a process regarding necessary and proper practices when establishing executive compensation for Internal Revenue purposes such as maintaining or revoking not-for-profit status. We advocate very

strongly with our members to see that all boards of directors follow the statute and regulation closely.

Those that do comply – and such compliance must now be attested annually through submission by each agency of IRS Form 9990 – have a pathway that secures them in the knowledge that they are setting compensation amounts that the IRS will consider presumptively reasonable and not excessive.

It is our strong belief that community providers' boards are following these provisions very closely through board governance principles that align with the spirit and the letter of the IRS provisions. After all, it hardly needs to be stated that loss of not-for-profit status would be catastrophic for these providers. (DD providers in New York, for example are required to be not-for-profit entities if they are to provide services under license from the state OPWDD.)

The IRS approach has several virtues that more rigid provisions lack. Boards must exercise due diligence in studying comparative data that assists them in setting salaries. This ensures that executives are compensated after adjustments – up or down – that are consonant with the data the boards gather from similarly situated providers with similarly experienced, educated, and credentialed executives. This comparative data approach thus indirectly, but effectively, takes into account geographic factors, education levels of similar executives, other credentials, longevity of service, and the market value of such individuals. And, by requiring a board to take pains to document the comparative data study, the IRS thus has easily analyzed data in which to make a determination of reasonableness and to help ensure that boards do not act arbitrarily, in secret, or without proper basis for the compensation level it approves.

It should be noted that, much as state-imposed compensation limits are designed to protect the public purse, the IRS approach is designed in the same spirit. The IRS in this case polices whether not-for-profits are abusing a status that confers a social subsidy on them. We think it is significant that the IRS has chosen a path that balances many factors – among them, the protection of taxpayers.

This approach also comports with a New York State manual of best practices that was recently prepared. The April 2010 “Report on Executive Compensation” published by the New York State Commission on Quality of Care and Advocacy for Persons with Disabilities (CQCAPD), speaks approvingly of governing boards' reliance upon data from IRS Form 990 when setting compensation levels, as it is the most common public source of compensation data. The report also recommends comparing “similar jobs, at agencies of similar purpose, revenue size and geographic area.” The report reiterates these values by citing three key factors that influence executive compensation: size of agency budget, geographic region and “personal factors” such as education and an individual's years of experience. Thus, the report endorses the same sorts of factors that the IRS expressly notes as criteria under its reasonableness tests.

NYSRA and its member agencies feel quite strongly that the State has a significant interest in ensuring its fiscal investment in provision of services and supports is protected. All of our member agencies, as well as our association itself, operate with missions that are service-related and centered on the individuals who are served, not the welfare of provider agency executives.

At the same time, providers, like all other effective businesses, must contend with challenges of recruitment and retention of talented, qualified and effective individuals to help ensure that services of the highest quality are made available to New Yorkers. Any limitations must be viewed from a perspective of whether they will ultimately drive quality people from the provider systems.

While we recognize the intent of proposals such as those advanced by the Governor, we caution against policies or legislation that, while they appear to be effective responses to a problem – in this case, a problem we can only conclude is isolated to a very few instances – may in fact instigate other problems. Flat limits, for instance, could conceivably drive up salaries that are already lower than the prescribed restriction. Rigid provisions can work injustices because they lack the capacity to be applied equitably. Caps on state reimbursement of salaries can mean that talented, innovative, and truly effective leaders leave our systems behind once they become so valuable as to be too expensive for our community providers to retain them.

Efficient government and taxpayer protection are, as we noted, important priorities for policymakers. However, we must also be mindful of our shared goal of ensuring that quality services and supports play a major role in shaping our system as we move forward. That is why we endorse the IRS approach. It protects taxpayers while it remains sensitive to the various real-world factors that well-meaning governing boards deal with when finding and compensating leaders. We believe it is far more effective than a “one-size” approach when seeking to balance the varied interests implicated by this issue.

NYSRA sincerely thanks Senator Marcellino, this Committee and the Senate leadership for the opportunity to air our views on this significant and important issue.

Executive Compensation-January 11, 2012

Respectfully submitted by Daniel Lukens, Executive Director of Camp Venture Inc.

New York State faces perhaps its most important challenge in a generation as the Medicaid cost sharing agreement that has underwritten the generous array of services that we offer to our citizens with developmental disabilities in this state will sunset in April of this year. And, contrary to the assertions otherwise, the fact is that our current system is among the best. Nonetheless, at this pivotal time the system is under threat from a loss of public confidence related primarily to its failure to address the excesses of a few individual executives.

Greed is not good especially when it exploits our most vulnerable citizens and abuses our state community's most noble and altruist aspirations. At a time when we are compelled as a state to consider hard choices and reexamine our priorities in order to maintain essential services and restore economic stability, what the public needs most is confidence in our public endeavors especially those that support the most essential aspects of the social safety net. The question is not simply what represents adequate compensation but what do those compensation number say about our priorities and the values we espouse?

As an Executive Director of a medium size not-for-profit organization serving adults and children with developmental disabilities, I am fully aware of the need to attract and retain fully qualified executive staff to run what has become a highly diverse and complex organization. As a former direct care worker and as the brother of man with Autism who has been a part of this service system for more than 30 years, however, I appreciate as well that compensation is as much about values and the example that I set as a leader as it is about a supply and demand equation for executive talent. In a service system that relies on workers who start at \$11-\$13 per hour and who often make great personal sacrifice to serve their fellow man, my own concept of what I am worth is assuaged by the value I see demonstrated in their dedication to the people they serve.

As it stands, executive compensation decisions are the purview of boards and the state's governance expectations have been focused on board oversight. With all due respect to boards, the result of this approach I believe is self-evident. An examination of good agencies with modest executive compensation I believe would reveal that the reasonableness in executive compensation is guided more by the discretion of the executive than by the board. I would further suggest that in a greed-driven culture, corporate style boards sometimes do not afford respect to executives who are too modest in their salary demands. Executives mostly get the money that they ask for.

With all of that said, the bottom line is this: What does it take to get someone to accept a 24/7 responsibility for the lives of nearly 200 vulnerable people and a service responsibility for about 1000 more? Consider a workforce of nearly 600 and a budget of about \$32M. Then compare that to similar public and not-for-profit endeavors and jobs and remember

that the not-for-profit sector does not have the kinds of pensions that the public sector does. In my case that brings you about \$130K per annum in salary plus health benefits and some modest retirement contribution from the organization (which is the same benefits offered to all employees). It is compensation that I believe puts me among the great majority of my colleagues and if it seems excessive I would be more that willing to discuss that in an open dialogue about reform, as I believe most of my colleagues would as well.

The commitment of the voluntary service providers, by and large, is to the people we serve and to the public trust. Senate action on executive compensation I believe should focus on promoting the good and not grandstanding on the bad. It should recognize that what vulnerable people need most is a public dialogue that promotes the noblest altruistic intent of the people. A caring community is one that sacrifices for the least of its citizens with confidence that they will not be abused for their good intent. My hope is that Senate leadership will act decisively and publicly to restore that confidence.

Thank you!



February 6, 2012

**Joint Testimony**

**New York State Senate Committee on Investigations and Government Operations**  
**Hearing on Executive Compensation at Not-for-Profit Organizations**

**Submitted on behalf of the following organizations:**

The Human Services Council of New York City  
Lawyers Alliance for New York  
Nonprofit Coordinating Committee of New York  
UJA-Federation of New York  
United Way of New York State

We appreciate the opportunity to submit written testimony to the Committee on behalf of our respective organizations. As you know there are thousands of nonprofits that have historically provided services to New Yorkers across a wide array of needs. This partnership of public and nonprofit services is a longstanding one, and highly successful.

Based on our extensive history and experience with nonprofit organizations in New York State, we offer our perspective and recommendations on this issue for your consideration:

**1. Enforcement of existing state and federal oversight and reporting of nonprofit compensation is essential.**

We note that all charitable organizations, whether they have contracts with New York State or not, face an almost unprecedented and recently increased level of regulation through required registration and annual reporting. These documents are already available for public and government review, including:

- Annual reports to the Office of the Attorney General (CHAR 500), which must include the agency's independent audit or financial review (depending on the amount of annual revenue). We note that the New York Attorney General is already charged in state law with the registration and reporting for all nonprofit organizations, however the reports to his office are currently submitted only as paper copies via regular mail.
- Applications to the federal government to become a tax exempt charity or "501(c)(3)," which requires extensive documentation and are acted on only after a lengthy and detailed review process.

- Annual reports to the IRS (Form 990), only recently revised and expanded, which are also lengthy and are *required* to include not only complete financial data, but also a description of programs, major revenue sources, a list of Board members, salary data for top staff, and a required description of how executive compensation is established – annually. These reports must be made available to the public upon request and many organizations post them on their web sites.
- The procurement review process in New York State, which involves a multi-layered process for issuing Requests for Proposals, reviewing contracts and approving payments for nonprofit agencies, including a review by the state agency, the Division of the Budget, the Office of the Attorney General and the Office of the State Comptroller. For a multi-year contract, there continues to be review each year of the organization’s budget and scope of work, by these state agencies.

These multiple state jurisdictions (state agencies, DOB, OAG and OSC) already have the authority to ask questions and call a halt to contracts in which the work is not being performed satisfactorily, the program objectives are not being met, or state funds are not being used for the purpose intended.

**2. Electronic filing should be implemented to enable the Attorney General to identify agencies not in compliance with state law or regulation so that their actions can be investigated and remedial action, where appropriate, may be undertaken.** The New York Attorney General is charged with the regulation of all nonprofit organizations, and any solution must involve that central role. Reports generated by the system would also be available to state agencies for their own compliance reviews and to the public to strengthen accountability with donors.

**3. Electronic filing of all state RFP and contract documents and supporting documentation should also be implemented.** Electronic filing would make it easier for the state to identify questionable contracts, investigate and take action where needed. In addition, the opportunity that electronic filing would have for increased transparency to the public, to the Legislature, as well as to state regulators, would only serve to increase public trust and benefit the entire system.

**4. Additional education of the nonprofit sector, including staff and Board members, is always helpful.** The Attorney General, as well as voluntary organizations and their federations, can play a more active role in continuing education for the nonprofit sector as to the federally required procedures for review and setting of executive compensation. The current best practices of a number of organizations can also be used as a basis for further outreach and education.

**5. Efforts to make the public aware of the existing regulatory and reporting requirements and enforcement efforts is also recommended, as that, in itself, is a powerful educational and compliance-inducing tool.** However, that publicity should take care to not taint the entire sector.

**6. We recommend that the Attorney General interpret New York law in a manner consistent with the current federal “intermediate sanctions” standards for nonprofit executive compensation.** This would include use of market-based analysis comparing like organizations, and following the voluntary “safe harbor” procedures set forth in the IRS regulations for setting compensation. These existing requirements should be recognized by the state to simplify and expand enforcement, and also to provide protection to nonprofits that follow them from challenge under New York law.

Before closing we would like to comment on the Governor’s proposals with respect to not for profit executive compensation. These were first proposed in budget language on January 17 and were the subject of an Executive Order for executive agencies on January 18. The state agencies are directed to develop regulations and take other actions to implement the order within 90 days.

We are troubled about how this issue has been handled and are concerned about its implementation. More specifically:

- A Task Force, chaired by Benjamin Lawskey, was appointed in the summer of 2011. Senator Marcellino is of course a member. Their initial action was to send nearly a thousand detailed questionnaires to not for profit agencies requesting compensation and benefit data. The public and the Legislature should be able to review the compilation of this data and an analysis of the findings, prior to proposals being put forth and discussed, and certainly before any action is taken.
- We are also concerned that there has been no process for the not for profit sector to be “at the table” to give its input into this issue. We note that other major issues dealt with in the past year have begun with the creation of a task force or committee to engage in study and dialogue. These committees included state representatives and members of the sectors which would be affected. This was followed by detailed study, public hearings, and dialogue, prior to reports with recommendations. Some examples of these include the Medicaid Redesign Task Force, the Mandate Relief Task Force and the SAGE Commission. These steps have not been taken with the Compensation Task Force prior to proposals in the budget and the Executive Order being made public.
- News stories in 2011 reported on nonprofit agencies that apparently used public dollars in an irresponsible and possibly illegal way. We do not support the actions of those agencies. Certainly, however, the state already has the legal tools to demand restitution, if that is the case, and the existing oversight authority, as outlined above, to prevent a re-occurrence. New restrictions or reporting for the entire sector have not yet been demonstrated as necessary and could further add to administrative costs that are themselves a target for savings.

- What has not been demonstrated is that the problem is widespread and persistent. In the meantime, the not for profit sector has been unfairly portrayed as “lining their pockets at taxpayer expense”, thus doing irreparable harm to the reputations and good work of thousands of these agencies and their staff. This will surely hurt the private fundraising of these agencies at the very time when demands for their help have increased and while state and federal governments are cutting programs.
- The state is already an outlier itself when it comes to processing contracts with not for profit agencies. The State Comptroller’s annual reports on prompt contracting show that the state has been late between 70%-90% of the time in approving these contracts between 2008 and 2010, and the record was no better before that. This, despite a law that has been on the books for over 20 years, passed by the State Legislature.
- State agencies already have different determinations for “administrative” or “overhead” expenses, as well as different allowable costs accepted as components.

To suggest that the state agencies take time to develop guidelines on compensation prior to this delay prone process being fixed, will needlessly add to the financial distress of the majority of not for profits who serve your constituents, as they spend time and money complying with new regulations and procedures.

We urge your committee and the legislature to proceed with caution in formulating new measures to deal with a problem that has been the subject of considerable reform over many decades, and for which there is extensive law and regulation already on the books. Excessive compensation paid to a few nonprofit executives, particularly when paid from limited state dollars, represents a waste of resources that could be devoted to program services and creates a stain on the nonprofit sector. However, we believe that an extensive set of tools in state and federal law and regulation already enables New York State to identify those cases and address them.

We are confident that your committee will give extremely thoughtful consideration to the issues raised here. To summarize, we urge the state to focus on: (1) enforcement of existing laws and regulations as to wrongdoers; (2) education of the public and nonprofits as to those laws and rules; and (3) confirmation that New York State will follow the comprehensive federal rules and procedures for determining whether compensation is excessive. The time and money that will be wasted by imposing a new system will not remotely, in our view, be offset by benefits to New York State finances, to those served by New York State nonprofits or to nonprofits themselves.

Again we appreciate the opportunity to submit this testimony and we are willing to meet to discuss these recommendations.

Michael Stoller, Executive Director

**The Human Services Council of New York City (HSC)** is a coalition of nearly 200 nonprofits strengthening the human services sector's ability to serve New Yorkers in need. As a non-partisan intermediary between government agencies and member organizations, we passionately champion the sector. We proactively negotiate with State and City government for mutually beneficial, solutions-based budget, policy, and legislative reform that improve our constituents' work and the lives of the individuals they serve.

Sean Delany, Executive Director

**Lawyers Alliance for New York** is the leading provider of business and transactional legal services for nonprofit organizations that are improving the quality of life in New York City neighborhoods. Lawyers Alliance represents hundreds of small and community-based nonprofits that contract with New York State to provide vital services in low-income neighborhoods.

Michael Clark, President

**Nonprofit Coordinating Committee of New York (NPCC)**, is an "umbrella" organization representing and serving nearly 1,500 member nonprofit 501(c)(3) organizations in the New York City area. Established in 1984, NPCC informs and connects nonprofit leaders, saves nonprofits money, and strengthens the nonprofit sector's relations with government.

Ronald Soloway, Managing Director, Government & External Relations

**UJA-Federation of New York** is a major Jewish philanthropy that provides funding support to a network of 100 health and human service agencies in New York City, Long Island and Westchester County. Our network of agencies assist the poor and vulnerable in both the Jewish and broader community.

Susan K. Hager, President

**United Way of New York State** is a statewide association which works to strengthen the capacity of local United Ways to be leaders in achieving results that improve the lives of all New Yorkers.

February 6, 2012

Senate Standing Committee on Investigations and Government Operations  
Executive Compensation at Not-for-Profit Organizations

**I. Introduction**

My name is Gerald J. Archibald. I am a Certified Public Accountant in the State of New York. For 38 years, beginning in 1974, I have specialized in serving the accounting, tax, and cost reporting needs of Not-for-Profit Organizations in New York. I worked with the international accounting firm of Arthur Andersen until 1986, and then joined The Bonadio Group where I am now the partner in charge of the Firm's Tax Exempt Organizations Practice for Central New York. The Bonadio Group is a Top 100 Accounting Firm in the United States (#70) and employs approximately 350 individuals in our seven offices. Our firm currently provides services to more than 300 Not-for-Profit organizations in New York State. Our tax exempt practice includes the entire spectrum of Not-for-Profit organizations including hospitals, nursing homes, colleges / universities, and human service and arts / cultural service providers. As a result, a majority of our clients in these service sectors receive State funding from DOH, OMH, OASAS, OPWDD, SED, OCFS, etc. These organizations are subject to the provisions of the recent Executive Order regarding Executive Compensation and Administrative Costs.

I am currently the editor for two Thomson Reuters publications, *The Non-Profit Controller's Manual* and *The Controller's Manual*. For the past 16 years, I have written a monthly column on Not-for-Profit Management Issues for the *Rochester Business Journal* and more recently the *Central New York Business Journal*. I am also a Fellow in the Healthcare Financial Management Association, an organization of healthcare finance managers with more than 30,000 members nationwide.

This submission is respectfully provided to the Committee from the perspective of a professional CPA who has also served on many Not-for-Profit Boards, including Board Chair in several cases. I am also active in supporting the philanthropic and volunteer needs Not-for-Profit Organizations.

I have recognized and observed throughout my career that there have always been and will continue to be opportunities for improving the cost effectiveness of Not-for-Profit organizations that serve as a vital component of the New York State infrastructure supporting all New York residents. The observations and recommendations that follow are provided for the Committee's consideration. I believe the Governor's Executive Order on Executive Compensation and Administrative Costs must be modified. If not modified, I believe that these two requirements, improperly implemented by State Agencies, could very well result in the chaotic dismantling of the Not-for-Profit service infrastructure built by this great State over the past 60 years.

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## II. Executive Compensation

The proposed salary cap of \$199,000 on Executive Compensation for Not-for-Profit Organizations contracting with New York State is both arbitrary and dangerous, if implemented incorrectly. I suggest that the Committee consider the following facts and suggestions as important to the implementation of regulations and requirements related to the Governor's Executive Order:

- 1) Not-for-Profit Organizations are already subject to the requirements of the Internal Revenue Service Code Section 4958. These requirements, which are reported each year on the IRS Form 990 by each Not-for-Profit organization in the country, specifically address the procedures that must be followed by the organization to ensure reasonable and fair compensation for nonprofit CEOs. If Section 4958 requirements are not met, the organization, its Board Members, and its CEO can be subjected to penalties and fines for what is referred to as an Excess Benefit Transaction. The Section 4958 "Intermediate Sanctions" requirements have been in effect since 2002. In my opinion, these regulations properly address in a systematic manner the requirements for Not-for-Profit organizations to ensure that total CEO compensation is both fair and reasonable.
- 2) However, as Committee members and the Governor know, the existence of regulations does not guarantee 100% compliance. There will always be a certain number of organizations subject to any regulation that will choose to ignore, manipulate, or abuse the specific intent of the regulation. I, therefore, agree with the Governor that something must be done to identify the CEO compensation outliers in a systematic and rational manner that is reasonable and manageable for all Not-for-Profit organizations to implement.
- 3) Executive Compensation is impacted by many factors including, but not limited to, size of organization, complexity of the responsibilities of the position, number of employees, geographic cost of living, number of senior management team members, experience and background of the individual CEO, market competition, CEO performance, and annual evaluation of the CEO's achievement of Board established goals and objectives. A statewide CEO salary cap of \$199,000, without proper implementation guidance, could seriously disrupt many Not-for-Profit organizations and their ability to continue to provide services to New York State residents in fulfillment of their individual charitable missions.
- 4) I fully expect that many other parties will be submitting their suggestions, objections, and recommendations to the Committee. While my submission may not be lengthy or detailed in terms of background support and statistics, I do believe that my journalistic limit of 1200 words should be 1500 words for purposes of Business Journal publication will serve as an advantage in this situation. In a nutshell, implementation guidance by the Governor and the Legislature to the State Agencies responsible for implementing the CEO compensation salary cap is critical to achieving an effective result.
- 5) I recommend that the Committee appoint a Task Force or charge the current Not-for-Profit Executive Compensation Task Force with the responsibility of developing specific guidance and regulations related to State funding of Not-for-Profit CEO compensation. In assigning this responsibility, it should be recognized that all stakeholders be represented in accomplishing the task. My specific recommendation in this regard is rather simple and straightforward, which will ensure that compliance and enforcement of the regulation can be monitored effectively.
- 6) Therefore, I recommend that the implementation regulations, recognizing that the IRS has already established comprehensive requirements for Not-for-Profit organizations in the area of Board oversight of CEO Compensation, include the following provisions:
  - A) CEO compensation caps or guidelines should be established at various dollar levels based primarily on the size of the organization's total annual expenditures, number of employees, and geographic location (Upstate and Downstate). Other factors may be considered in the assessment of reasonable compensation caps; however, the size and, therefore, complexity of the organization should be the primary basis for implementation guidance.

- B) CEO compensation salary caps should be established at the following thresholds based on the total annual expenditures of the individual Not-for-Profit organization:
- i) Less than \$5,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - ii) From \$5,000,001 to \$10,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - iii) From \$10,000,001 to \$20,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - iv) From \$20,000,001 to \$30,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - v) From \$30,000,001 to \$50,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - vi) From \$50,000,001 to \$100,000,000 in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$XXX,XXX.
  - vii) \$100,000,001 and above in total annual expenditures in the preceding fiscal year would have a CEO salary cap of \$X,XXX,XXX.
- C) Additional thresholds and/or narrower bands for purposes of implementation can be considered.

### **III. Administrative and Direct Service Cost Percentage Caps**

The Governor's Executive Order directs state agencies to implement "...regulations or to address by other means the extent and nature of a provider's administrative costs and executive compensation which shall be eligible to be reimbursed with state financial assistance or state-authorized payments for operating expenses..." Consistent with the recommendation above with respect to CEO compensation, the implementation of the Governor's administrative cost thresholds (decreasing from 25% to 15% over a two year period) to be fully implemented by April 1, 2015 will require careful consideration and specificity related to the following areas.

- 1) Administrative costs must be clearly defined with specificity and practical examples of proper cost classifications. This will be extremely difficult since, depending on the nature of an organization's programs and services, certain costs can be direct service costs for one organization while the same type of cost may be an administrative cost for another organization (e.g., information technology costs, regulatory compliance costs, CEO and Senior Management personnel with direct program service responsibilities, etc.).
- 2) Individual percentage target thresholds for administrative and direct program service costs, respectively, without regard to the size and nature of an organization's services, cannot be applied fairly across the broad spectrum of Not-for-Profit service providers.
- 3) If the primary objective of this provision is to "weed out" those providers who cannot demonstrate cost effective delivery of services funded by State agencies", then the implementation approach should focus on identifying those providers who have excessive administrative costs and or service unit costs, as defined. The provider organizations identified should be informed that their administrative costs and/or service unit costs are excessive based on an independent review of cost reports filed with the State of New York and the Form 990 filed with the Internal Revenue Service and the New York State Charities Registration Bureau.
- 4) New York State clearly has excess capacity in certain Not-for-Profit service areas while other areas are underserved in terms of provider capacity. The State initiative, known as the "Berger Commission", was effective in its analysis and review of the State's health service capacity in the acute care hospital sector. In addition, recent State-sponsored analysis led to a targeted reduction of 6,000 skilled nursing facility beds in the long-term care service sector. These are just two of many examples where State-initiated analysis, with provider involvement, has resulted in an orderly assessment of the State's provider capacity to deliver sufficient health and human services to its residents.



- 5) There are many ways to achieve improvements in cost effective delivery of Not-for-Profit services. Assessment of excess capacity, too many providers involved in service delivery and quality of service are a few examples of the many approaches available to the State for purposes of demonstrating cost effective delivery of Not-for-Profit services. The application of the administrative cost threshold, without appropriate consideration of other factors influencing the cost effective delivery of services, may result in service delivery interruptions, access to care issues, bankruptcy / financial failure, etc. for many New York State Not-for-Profits. In many cases, the providers most seriously damaged by an arbitrary assessment of administrative cost inefficiency, may represent those providers who are providing the highest quality of care to the most vulnerable and needy residents of New York State. I strongly encourage the Committee to establish a structured approach to implementing the Governor's Executive Order, with the active involvement of provider representatives, associations of providers, volunteer Board members, State representatives and other key stakeholders.
- 6) If a percentage approach is deemed appropriate for assessment of cost efficiency by New York State Not-for-Profit service providers, then the approach described in Section II, Item 6 above with regard to executive compensation should be applied to the percentage limitation on administrative costs for organizations. Administrative costs, as well as CEO compensation, will vary based on the size and complexity of an organization's programs and services. A statewide percentage for administrative costs for every Not-for-Profit in New York would not be fair and reasonable to apply to each and every organization in the State.

I appreciate the opportunity to submit these observations and recommendations for the Committee's consideration. I am more than willing to provide further input in the development of the implementing regulations of the Governor's Executive Order on a pro bono basis. Thank you for your attention and deliberations related to developing appropriate implementation guidance for these extremely important areas that will clearly impact on the future viability and stability of New York State Not-for-Profit organizations.

Respectfully submitted,



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