

# Communicating Compensation to the Board REMDC May 2011

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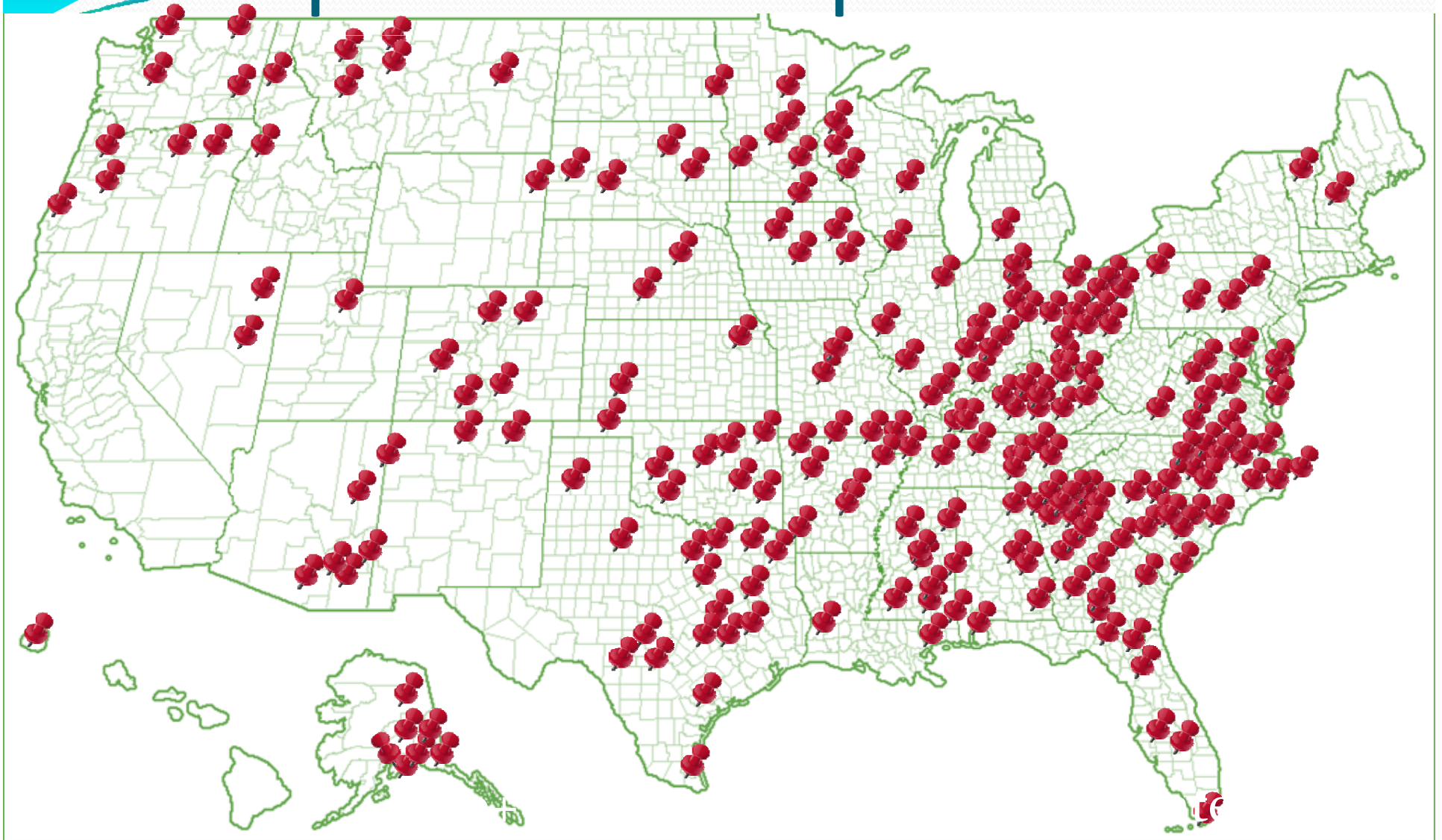
**MDF HR  
Consulting**



# Who I am

- 20+ years professional Human Resources Experience
- Full time consultant for 13 years
  - Sample Clients
    - Internal Revenue Service
    - Department of Defense
    - US Customs Service
    - UK Ministry of Defense
    - Cooperatives Nationwide for the last decade

# Cooperative Perspective



# Topics

- Strategic Value of Compensation
- The labor market
- Board Perceptions
- Best Practices



# Strategic Value of Compensation

- Compensation Plans Contributes to Vital Business Objectives:
  - Attract Qualified Employees to the Cooperative
  - Retain Qualified Employees
  - Motivate Qualified Employees
- Properly Maintained Plan
  - Pays Employees Competitively
  - Controls Salary Costs

# Retention Value for Executives

- Do you have a productive and competent Sr. Staff
  - Then they are worth fair market value
- Do you have the bench strength to replace our Sr. Staff with internal candidates
- Replacing the Sr. Staff
  - Costly search for replacement
  - Disruption in the smooth operation of the Cooperative
  - Board will have to break in new ones



# Value of Executives

- Salaries should not be thought of in terms of cost, but rather as investment
- Management Employee's make the decisions and take the risks that allow the Cooperative to be viable as a business
- Effective employees create worth much greater than salaries received through:
  - Reducing Costs
  - Increasing revenue
  - Increasing Value to the member



# Management Responsibility

- If you want to maintain a competitive salary system you must continually educate the board
  - Value of employees
  - Our Labor Market





# Communicating our value

- We are our own worst enemies here
- Commonly heard in board meetings (highly simplified):

*“we are planning some system improvements. They will cost us \$3 million dollars. Please vote on this so we can put it into the budget”*

- When you communicate in this manner
  - Board only sees you and your staff in terms of cost
  - When compensation issues come up, just one more cost to add to the list.

# Communicating our value, a better way

- Train yourself and your executive staff, any time you come before the board
  - Reinforce your value
  - Talk about benefits and outcomes
- The \$3 million we want to spend will
  - Enables us to better serve our members
  - Increases system reliability by x%
  - Will reduce maintenance costs by %
  - Save us \$xxx within X years

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# Cooperative CEO Labor Market

- Is a national market
- Has some “local flavor”
- It is not driven by “cost of living”
- Cooperative CEO’s could make more in the private sector
- Best Sources of Data
  - NRECA National Compensation Survey, G&T, and RESMA
  - 990 Filings available on [Guidestar.org](http://Guidestar.org)

# CEO Pay Compared to Other Industries

- Average Ratio of CEO Pay to employees
  - 250 to 1
- Normally found ratio in Cooperatives
  - 4-5 to 1

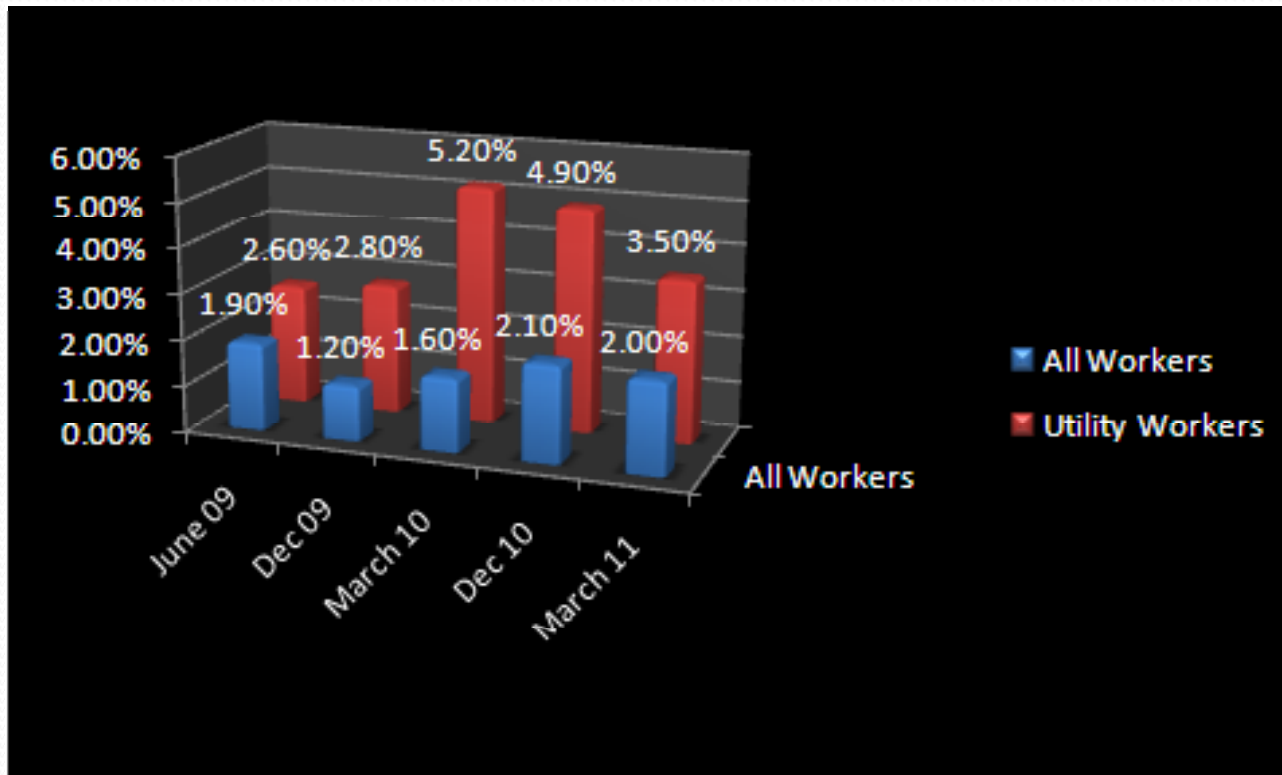


# Investor Owned Compensation

- Allegheny Energy \$12,589,731 379/1
- Duke Energy \$ 8,815,181 265/1
- Exelon Corp \$9,418,399 283/1
- Entergy \$8,280,067 249/1
- El Paso Electric \$2,141,247 64/1
- Portland Gen Electric \$1,728,845 52/1

# Outlook in Base Compensation

- The Utility sector continues to be strong
- Employment Cost Index Change
  - Utility Vs. All Workers



Source: US  
Bureau of  
Labor  
Statistics,  
Economic  
News  
Release

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# Board Members perception on pay

- Most willing to pay market value
  - Unsure of what that is
  - Afraid of excessive compensation
  - If they are comfortable with the analysis, willing to pay what is fair
- Some have a tendency to gauge executive compensation against personal compensation
- Some opposed everything as a general rule
  - They are only one vote



# Arguments I hear constantly

- Nobody makes that kind of money around here!
- The farmers are having a hard time!
- This will impact rates!
- The guy at the Cooperative next door does not make that much!
- That's an awful big jump!
- The labor market is tight, they are not going anywhere!

# No one makes that kind of money around here!

- May seem that way, but not usually true.
- Unless you are the only employer in your territory
  - Other executives are being compensated at similar rates
- Although the labor market is entirely different, these positions are usually compensated at comparable rates:
  - Hospital Administrators
  - School Superintendents
  - College Administrators
- Random sampling of “not for profits” in client territories reveals the following:



# Not for Profit Hospitals

- Moundview Memorial Hospital, Friendship WI
  - \$188,204
- North Valley Hospital, Whitefish, Montana
  - \$180,642
- Rockingham Memorial Hospital, Harrisonburg, VA
  - \$681,526
- Knox Community Hospital, Mt. Vernon, OH
  - \$1,177,583
- Community Hospital of Anaconda, MT
  - \$244,709
- Marcus Daily Memorial, Hamilton, MT
  - \$304,848



# Private Colleges

- Lee University, Cleveland, TN
  - \$186,232
- Santa Fe Community College, Gainesville, FL
  - \$246,329
- Washington & Lee University, Lexington, VA
  - \$344,654
- Hendrix College, Conway, AR
  - \$235,935



# Charities

- Crossroads Youth & Family Svcs, Norman, OK
  - \$102,344
- Landsun Homes, (Retirement Home), Carlsbad, NM
  - \$124,800
- Hospice of the Piedmont, High Point, NC
  - \$130,000
- Hospice of Central PA, Enola, PA
  - \$123,685

# The farmers are having a hard time!

- We are not insensitive to our members, however unless your Sr. Staff is setting fire to the crops
  - It is not fair to punish them
- We are working hard to keep that farmers rates reasonable
- He would be having a harder time without affordable, and reliable electricity

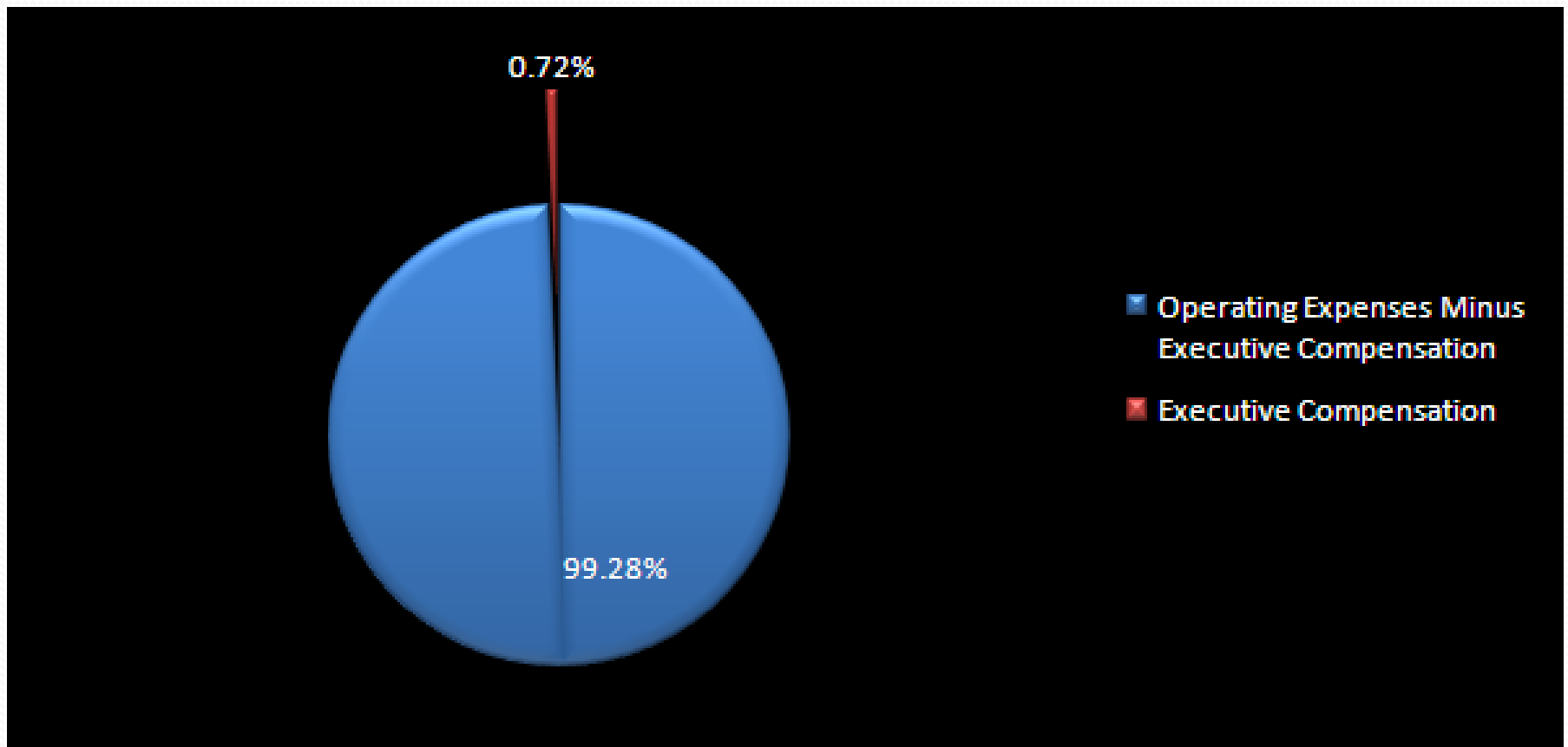


# This will impact rates!

- For this to be true
  - Consumption must remain stable, or decline
  - You have no margin now, and don't expect any
  - Your current rates already don't support your expenses



# Cooperative Executive pay in perspective



Real world example, client in Mid Missouri



# Real Effect on Customers

- 20,000 member Cooperative
- Average base CEO pay for that size \$155,234
- Average cost per KWH \$0.1151
- Average KWH Consumption per year 12,000
- Assume consumption is even
  - If we could only get the CEO to work for free
- We could give our consumers:
  - An annual rebate of \$7.76
  - Or 4 minutes and 27 seconds of electricity per day for an entire year
  - Or two large coffees at Starbucks at the end of the year
- Members would see greater savings by switching to CFLs
  - That we provide to them at no cost

# The guy at the Cooperative next door does not make that much!

- First, Basing compensation on one “guy next door”
  - Violation of Federal Anti-Trust laws
  - Could result in criminal penalties
- Senior staff compensation is a National Market, not local
- Is the cooperative next door really a fair comparison to you?
- Are the managers at the same point in their career?
- Do they have the same background and skill sets?



# That's an awful big jump!

- If it's a big jump, you have been getting your CEO at a discount for quite a while
- If you don't make attempts to bridge the gap, you send a clear message:
  - We value you, but not enough to pay you what you are worth.
- Underpaid executives in my experience retire early or move on.

# The labor market is tight, they are not going anywhere!

- Unemployment is high, but not for the people we need
- Keyword search for CareerBuilder.com Open Positions
  - Electrical Engineer 7,583
  - Electrical Utility Manager 881
  - Electric Utility Accounting 1,502
  - Public Relations Manager 5,675
  - Electric Utility 6,037
- Cooperative.com
  - 11 Senior Management positions advertised

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# Best Practices in Executive Compensation

- Establish a compensation philosophy
- Have a compensation committee, with clearly defined responsibilities
- Educate the Board on legal requirements for governance of compensation
- Use an independent third party to assist in the analysis
- Anticipate criticisms of the compensation package, develop responses



# Compensations Philosophy

- Define where the cooperative should be positioned in the market place
- Do we
  - Lead
  - Meet
  - Lag
- Who do we see as our labor market?





# Compensation Committee

- Establish a committee to work out the details of executive compensation
- Clearly defined responsibilities
  - Managing the CEO appraisal process
  - Establishing the base compensation for the CEO
- Have the committee present findings and recommendations to the full board
  - Prevents the board from being bogged down in minutia
  - Entire board may be more accepting, if they trust the work of the committee



# Educate the Board

- All board members need to be clear with regards to compensation
  - What is board responsibility, and what is management responsibility
  - If you have a policy in place, remind them of the need to follow it
  - Continually reinforce your value, and that of your staff



# Use a Third Party

- Use a consultant to gather data on competitive practices
- Do not rely on Cooperative Staff
- Have the compensation committee engage the consultant directly
- Have the consultant report directly to the board
- Supports a transparent process
- More defensible if challenges arise



# Anticipate Criticism

- In today's environment it is very common for the local media to beat up on executive compensation
- Disgruntled members will try to make it a “wedge” issue in Board elections
- Prepare your response to this criticism, and make sure:
  - The message is consistent
  - Only authorized personnel relay the message
  - The message is defensible to begin with



## Summing Up

- Establish your philosophy
- Continually educate the board
- Communicate your value
- Adopt best practices



Questions?

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