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Enough is Enough!

The Ins and Outs of Board Compensation

Board compensation is sometimes a touchy subject among cooperative members. Why are board members compensated? Is it possible to pay too much or too little for their service? The roles of cooperative members as customers and owners complicate the issue.

A recent article appeared in the *Austin American-Statesman* recounting the controversy surrounding Pedernales Electric Cooperative, Inc. At the heart of the controversy lies the issue of board compensation, giving many cooperative members and professionals reason for some serious thinking and consideration.

Pedernales Electric seems to be at the top of its game. The cooperative serves more than 211,000 members spread over 8,100 square miles in the Texas Hill Country making it the largest electric cooperative in the United States. Above that, Pedernales Electric Cooperative ranks number one in customer satisfaction of utilities in the state of Texas, and number three in the nation according to a J.D. Powers and Associates survey. The cooperative has lowered residential rates by 17% since June of 2006... and they have some very unhappy members. Consider some of the facts that have recently come to light:

- * Although it holds millions in surplus revenues, the cooperative has never paid out dividends.
- * Board members are paid over \$35,000 annually—the highest rate of compensation among Texas' 10 largest cooperatives.
- * The board president is paid nearly \$190,000 annually to handle external relations for the cooperative, and will have been on the board of directors for 40 years in February 2008.
- * The general manager was reportedly paid nearly \$400,000, not including a signing bonus of over \$350,000 a few years back.

- * The board selects the nominating committee who then chooses which names are on the voting ballot. Members complain that this makes it hard for “outsiders” to be placed on the voting ballot and with mail out proxy voting, the “outsiders” situation seems to be further hindered.

Granted, Pedernales Electric has some explaining to do, but our purpose is not to criticize or pass judgement on this cooperative. In fact, it is easily argued that this cooperative has provided a much needed service since its inception in 1938.

However, the larger issue of board compensation deserves our attention.

Why do we compensate cooperative directors? How much should they be compensated? Are there other board practices that need to be evaluated before members say “enough is enough”?

Why Compensation?

A cooperative business is owned by its customers who elect a governing board from amongst themselves to represent their interests in directing the company. Thus, directors are member-owners that have been given the rights of ownership and control of the business by their peers through democratic voice. All this is done in adherence to established bylaws. This form of governance is a common feature of a corporation and is an efficient means for control of an investor (or member) owned business.

The board of directors for any corporation are said to be its backbone. The directors act as agents on behalf of the owners with the responsibility to protect investments, grow the business, and improve profitability. In regards to a cooperative business,



the directors have the added responsibility to serve the needs of the members.

In carrying out these duties, directors meet on a regular basis to discuss the performance of their business and the challenges that could hamper its future success. Directors in corporate America are often chosen for their expertise and proven experience that can aid the growth of the business. Personal expense can accrue as a director invests his or her time in studying, meeting, or travel on behalf of the business. It is only reasonable that compensation should be made for this necessary service to the business.

Cooperatives also choose directors for their expertise. An often unrecognized strength of a cooperative business is its powerful connection to the customer through their representation on the board of directors. However, because of this dual nature of the cooperative board member to be both customer and owner, paid compensation is typically lower for cooperative boards than what you see in other business forms. Regardless, the directors are responsible for the performance of the business and it may seem fitting to provide them with comparable benefits.

Board duties don't stop there. Cooperative directors are also responsible for the following:

- * Abiding by the guidelines set forth in the articles of incorporation and bylaws.
- * Hiring and evaluating management.
- * Informing members of cooperative affairs.
- * Providing leadership and foster the development of future leaders.
- * Maintaining the cooperative mission and promoting its values.
- * Establishing long-term plans that preserve the cooperative assets and equity.
- * Establishing and enforcing cooperative policies.
- * Overseeing board elections and recruiting new talent to the board.
- * Overseeing the annual financial and physical audit.
- * Allocating savings to members.
- * Planning and approving large capital expenditures.
- * Planning and oversight of member meetings.
- * Being informed about the financial well-being of the cooperative.
- * Seeing that the cooperative complies with state and federal cooperative statutes.
- * And much more...

How Much is Enough?

Obviously this is a large responsibility. Cooperative directors provide a great service to the members that they represent. In compensation, directors are typically reimbursed for expenses in attending board meetings in the form of a per diem allowance that is authorized by the membership. Most cooperative bylaws disallow any form of direct payment to directors. The question then lies...How much compensation is enough and how much is too much? The practical answer to this lies in the status of the budget. Many newly started cooperatives lack the funds for any form of compensation. Later, as these organizations grow, they may re-evaluate their ability to compensate the board of directors. Ultimately, the answer will depend on various factors that will differ from one cooperative to the next.

For example, you might consider the amount of time and other work expected of your directors. Time away from the farm can be costly and should be treated as valuable. Also, consider your ability to attract members to serve on the board. It may be that the size and composition of your membership will require greater compensation to attract the service that you need. Don't be too hard on younger members for their seeming lack of indifference; attending to a relatively young farm and family may take limit the amount of time they are willing to share. Finally, your cooperative membership is likely to look to the past policies on compensation when asked to evaluate a new one. Drastic changes in compensation might not go over too well with members.

Its an Investment

If you are not sure about your current compensation policy, consider this: many cooperative directors are overseeing millions of dollars of assets with very little in return. The compensation of directors is an investment in the organization. Are you investing in your directors in a reasonable proportion to your assets? Suppose your cooperative owns \$2,000,000 worth of assets and you pay each board member \$38 per meeting (the average reported in our 2006 State of the Industry Survey) and you take your board to the annual TACC meeting. That's roughly \$1,500 per board member per year in compensation. This equates to about 0.07% of the value of your assets being invested in directing the business for each board member. That's not even one-tenth of one percent of your assets being invested in protecting those assets.

In this light we can see how directors of a large corporation like Pedernales Electric could expect greater compensation beyond what seems typical to members. However, cooperatives seeking to properly compensate directors must consider their expectations of directors, the available pool for recruitment, and the expectations of members in making this decision.