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Your Accounting for a New Economy

Paying by the Rules: Compensation for NFP Executives

Many not-for-profit organizations have a fiscal year ending December 31, which means they've already begun planning their budgets for 2011. Overpaying the executives in your organization can lead to costly and grave penalties up to and including the loss of your organization's status as a not-for-profit. With increased governmental scrutiny and severe penalties in place, there has never been a better time to become reacquainted with the rules and regulations regarding the determination of executive compensation for an exempt entity.

Ground Rules

- Not-for-profit executives may be paid at "Market Rate".
- "Market Rate" can be determined by looking at the compensation for a similar position in an organization of comparable size and mission or field of activity.
- For-profit companies may be used when determining "Market Rate" as long as the company in question is of equivalent size and has an analogous mission.
- The IRS does not have a formula (such as a percentage of revenue or expenses) for determining acceptable NFP executive compensation.

Penalties

If an exempt organization is found to have overpaid an executive:

- A fine can be assessed for both the executive in question as well as the board members who approved the overpayment.

- The organization's tax exempt status may also be revoked if:
 - The board has not based its decision on appropriate research
 - And the board has not documented the process of making its decision at the time compensation was approved.

The severity of the penalties involved emphasizes the importance of proper research when it comes to determining the executive compensation for not-for-profit organizations. If you have any questions concerning the requirements or guidelines do not hesitate to contact your trusted LGT advisor or David Ovesen, the partner in charge of LGT's not-for-profit group at 214-461-1443 or by email at dovesen@lgt-cpa.com.