Chief Executive Officer Compensation in Federally-Qualified Health Centers Highlights of the 2011 Edition

Data Collected May-August, 2011
Published October, 2011

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April, 2012

This “highlights” report provides a selection of information from our first annual analysis of Chief Executive Officer compensation in Federally-Qualified Health Centers. More than 100 FQHCs submitted data in time to be included in the study.

The participants represent a broad range of organizations, in terms of their size, location and services. Geographically, the participants come from every region in the US, including Alaska and Hawai’i. About half of the participants have revenues in excess of $10 million, and roughly 40% serve primarily rural areas.

The results of the study do not show any surprising compensation differences from our previous research, but illustrate more clearly the impact of revenue as a predictor of pay – something not always covered in sufficient detail in other studies. The data supports our hypotheses that management pay in the industry is much more equitable than is generally considered to be the case in the market overall. With women managing large FQHCs as often as men, and earning as much or more than men across the board, health centers present a model for gender pay equity.

Our major concern is that FQHCs do not have sufficient governance processes in place to respond to growing scrutiny of executive compensation from the government, media and community. It is not enough to simply “pay right” – organizations must ensure that their processes and documentation are sufficient to withstand question.

More extensive information is found in the full report; those who complete a copy of the 2012 questionnaire will receive a copy of the full 2011 report for their use while the 2012 analysis is in progress. For more information on “best practice” Chief Executive Officer compensation methods and processes, visit our website, or contact us by phone or email (ebura@mercesconsulting.com).

Sincerely,

Edmund B. Ura

Edmund B. Ura, MAIR, JD
President

“merces” - (mur’sez) Lat.: pay, reward, recompense, compensation

SUMMARY

One hundred and one (101) FQHCs participated in this first edition of Merces' Chief Executive Officer Compensation in Federally Qualified Health Centers Survey. The average reported base salary for a Chief Executive Officer is just less than $141,000, while average "total cash compensation" (base salary plus most recent bonus) is about $144,500. Compensation increases directly with FQHC revenue, with average salaries for the largest revenue group ($186,500) roughly twice as much (97% higher) than average salaries for the smallest revenue group ($94,600).

Unlike common assumptions about the general market, salaries for female Chief Executives in Federally Qualified Health Centers equal or exceed those of male Chief Executives, a trend which continues through the largest organizations. Incentive compensation does not constitute a significant part of total cash compensation, representing about 2.4% of base pay for all CEOs, and about 6.4% when considering only bonus-eligible CEOs. Most of the participants do not have formal incentive programs, although about one third are eligible to receive bonuses.

There are a number of elements that we consider essential to a "best practice" compensation program. These include:

- A descriptive, Board-adopted compensation philosophy
- Formal Board processes for governance of CEO compensation
- A thorough and accurate job description for the role of CEO
- A CEO salary range based on the compensation philosophy and competitive market
- Formal structured performance appraisal methodologies with results tied to discrete segments of the salary range

The governance practices of most of the participants do not reach "best practice" standards, and should be cause for concern for the industry. About two-thirds maintain a formal compensation committee, but only a third have a formal, Board-adopted compensation philosophy. Only half of the participants reported a pre-established salary range for the salary for the Chief Executive Officer position.

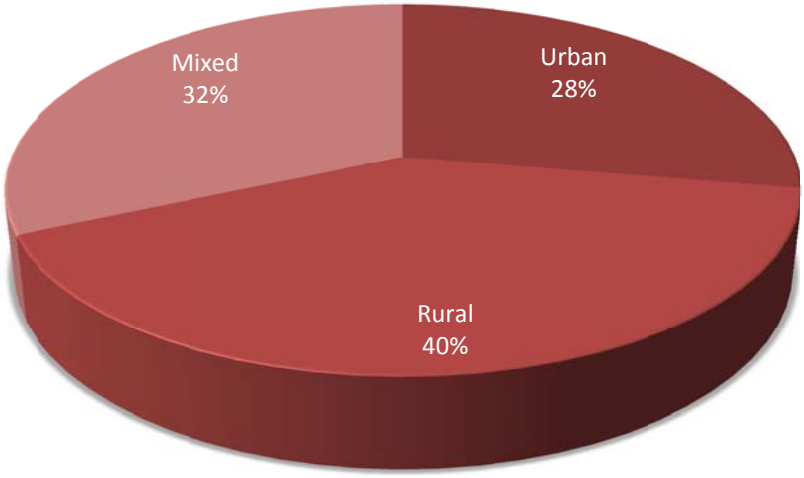
Most health centers use some type of competitive data to set CEO compensation levels, although much of this data is collected by individual Board members or internal staff. The inherent conflict of interest (either real or perceived) when internal staff provides information about the pay of their own managers should be a concern for the more than 40% of FQHCs who use this method of compensation research. Only about one in five of the participants use an outside advisor, and few of those are aware of whether their advisor is qualified as an Independent Compensation Consultant.

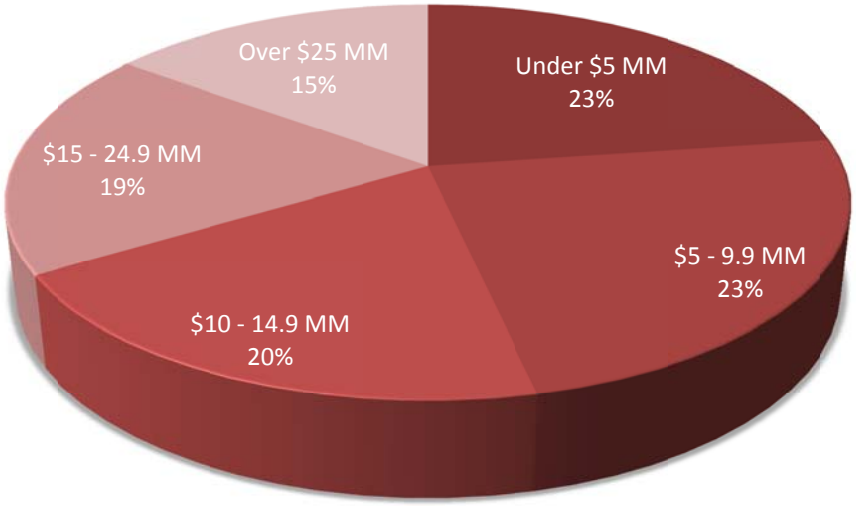
METHODOLOGY

Questionnaires were sent to Chief Executive Officers at more than 1100 Federally Qualified Health Centers (FQHCs) in late May of 2011, with an initial deadline of July 1. The deadline was later extended and all questionnaires received by August 31, 2011 were included in the analysis.

ABOUT THE PARTICIPANTS

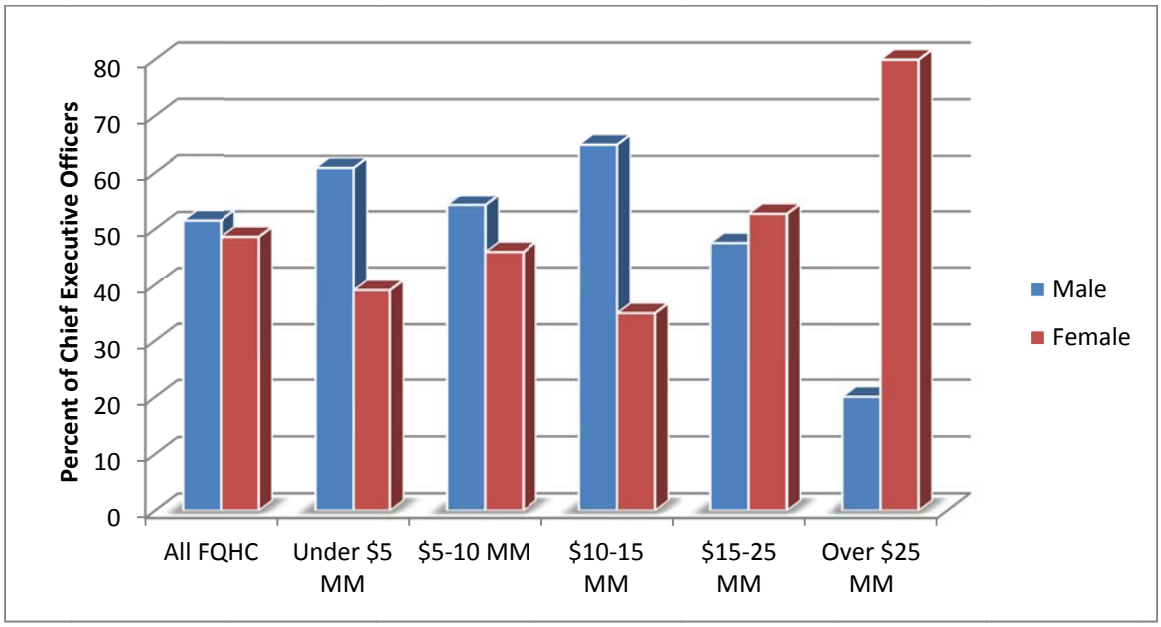
The 101 participants, a sample of roughly 8% of Federally Qualified Health Centers nationwide, have combined revenues of just under $1.4 billion dollars, and serve roughly 2.3 million patients in service areas with a total population of nearly 40 million. These organizations had more than 7.8 million encounters in the last year, of which approximately 5.5% were related to migrant workers.





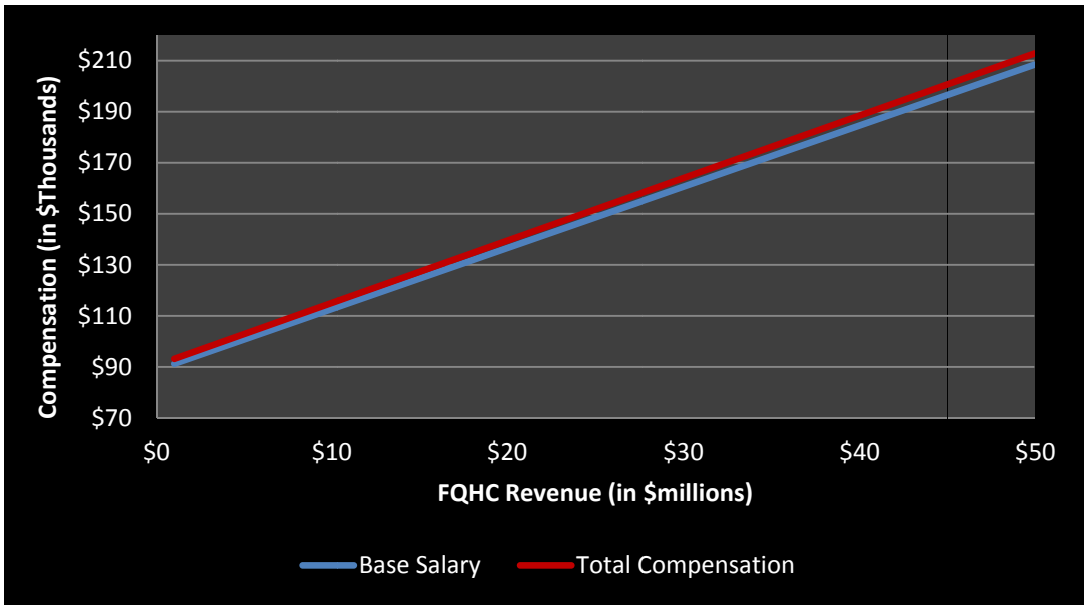
ABOUT THE CHIEF EXECUTIVE OFFICERS

The "typical" health center Chief Executive Officer is 55 years old, with half between the ages of 55 and 61, and has been holding his or her current job for 12 years. Half of the participants report their CEOs are male, half female. As revenue increases, it is more likely that the Chief Executive Officer will be a female; of the largest health centers represented in the survey, 80% are run by women.



CHIEF EXECUTIVE OFFICER COMPENSATION

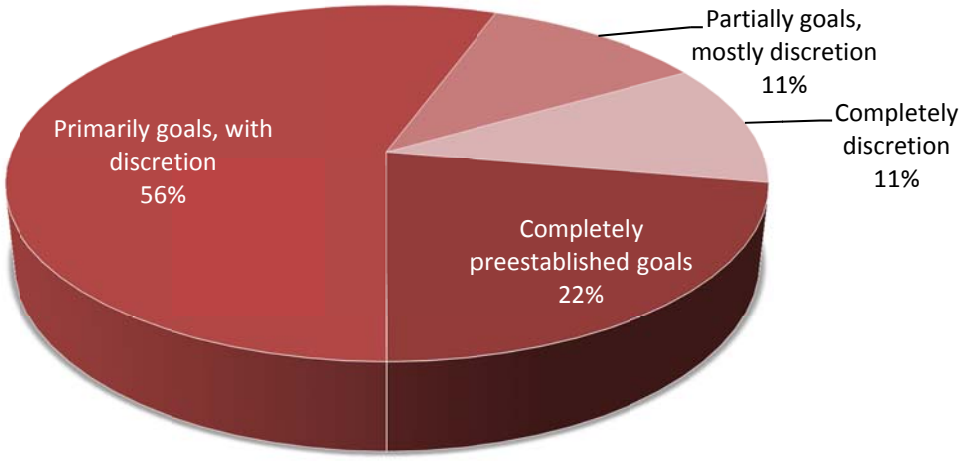
The average reported CEO base salary for the entire survey population is just less than $141,000. An average bonus of less than three percent (2.8%) of base salary brings total cash compensation to about $144,500. As is typical with any industry pay increases with size, measured by health center revenue.



Incentive Compensation

More than a third of the CEOs (37%) among the participants are eligible to receive an incentive or bonus. Incentive compensation is much more likely in the largest health centers (53%) than the rest of the participants (35%). An interesting finding is that within the larger health centers ($15 mm revenue and up), salaries for "incentive eligible" CEOs are about the same as those who are not eligible. In the smaller organizations (as well as the total sample), salaries for CEOs who are "incentive eligible" are about ten percent higher than those not receiving bonuses. The average bonus, where paid, is about 6.5% of base pay, thus about 5% of the total cash compensation package. Across the entire population, incentives average about 2.4% of base pay.

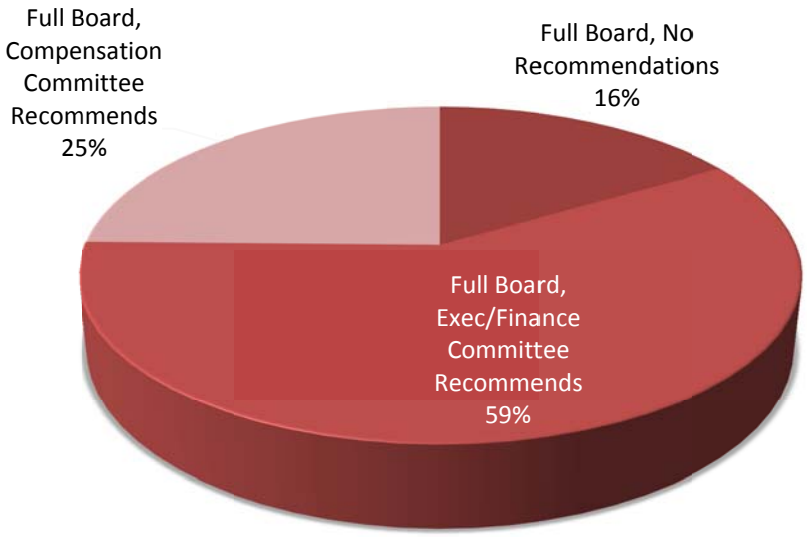
Contrasted with the larger group of executives who are "incentive eligible," only about one-quarter (26%) of the participants have formal bonus programs. While about a third of the smallest health centers reported formal programs, once past this group, the incidence of formal bonus programs increases directly with size. Roughly a third of the participants report formal targets for bonus awards; the methods for determining awards are displayed below. This should be a significant concern for governing Boards as well as executives, as discretionary awards are frowned-upon and may trigger further investigation into compensation practices. Setting incentive objectives and payouts in advance is more than just a "best practice" approach, and should be considered in all organizations using incentive compensation.



COMPENSATION GOVERNANCE

An important aspect of compensation programs in FQHCs is the manner in which they are governed. The Board has but one employee – the CEO, and the manner in which compensation for that employee is managed is crucial not just for compliance and disclosure, but for good management.

The manner by which the Board determines CEO compensation is shown below:



Responsibility for Executive Compensation Research

A key element of a best practice executive compensation program, and one which provides the most support when challenged, is the use of competitive data. Because of the number of data sources available, and the choices that can be made in selecting data, it is crucial that this process is transparent. Of course, the most transparent process is one that relies on a stated compensation philosophy. Of as much importance as the data that is used is the credibility of the individual or group analyzing it:

	All Health Centers	Under $5 mm	$5 – 9.9 mm	$10 – 14.9 mm	$15 – 24.9 mm	$25 mm and Over
Primary Source of Compensation Research						
Member of Board	38.5%	60.6%	39.1%	40.4%	26.3%	21.4%
Inside HR/Finance Staff	40.6%	35.0%	34.8%	45.0%	31.6%	64.3%
Outside Attorney	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Outside Accountant	3.1%	0.0%	0.0%	10.0%	5.3%	0.0%
Outside Consultant	17.7%	5.0%	26.1%	5.0%	30.8%	14.3%

Only about 20% of the participants use the services of an outside advisor in establishing the compensation of the CEO. Of those, only about 25% are known to be considered qualified under the Internal Revenue Service's Guidelines as an ***Independent Compensation Consultant***. Of perhaps greater concern is the fact that 40% of the health centers using outside advisors do not know if their advisor is an Independent Compensation Consultant.

What is an Independent Compensation Consultant?

An ***Independent Compensation Consultant*** is an individual who meets the standards set forth by the Internal Revenue Service as qualified to provide advice and counsel to a non-profit organization concerning its executive compensation program. An independent compensation consultant does not need to have a particular educational background or certification/license, but must be experienced and qualified to provide the services which he or she offers. The definition which follows is from the IRS instructions for Form 990, Schedule J:

> ***Independent compensation consultant*** refers to a person outside the organization who advises the organization regarding the top management official's compensation package, holds himself or herself out to the public as a compensation consultant, performs valuations of nonprofit executive compensation on a regular basis, and is qualified to make valuations of the type of services provided. The consultant is independent if he or she does not have a family relationship or business relationship with the top management official, and if a majority of his or her appraisals made during his or her tax year are performed for persons other than the organization, even if the consultant's firm also provides tax, audit, and other professional services to the organization.

Because the "not for profit" world is broad, and includes organizations of all types with completely different characteristics and needs, it is important for the *Independent Compensation Consultant* you engage to have expertise with Federally Qualified Health Centers.

About Merces…

Merces Consulting Group, Inc., located in the Detroit Metropolitan Area, has served the needs of Federally Qualified Health Centers for nearly 20 years, providing support and guidance in the development and implementation of "best practice" compensation programs, and supporting services such as organization design and documentation, executive compensation governance and planning, and performance management. With FQHC clients across the United States, of varying sizes and found in numerous settings, Merces can help your organization design an approach to better manage the most significant item in your budget.

Edmund B. Ura, MAIR, JD, President and Senior Consultant at Merces, has more than 25 years of compensation consulting experience, and nearly 20 working specifically with Federally Qualified Health Centers, and meets the IRS definition as an Independent Compensation Consultant. To learn more about the firm, its services and technical information concerning compensation program design and best practices, visit our website at www.mercesconsulting.com. For more information, or to schedule a consultation, contact Ed by phone at 248-507-4670, or by email, at ebura@mercesconsulting.com.

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