# Personnel Issues

(Rev. March 2014)

- Introduction
    - Welcome to the "Personnel Issues" module of the Board Education eLearning series. Most people will tell you that a nonprofit's staff is its most valuable resource: after all, these are the people who work day in and day out to accomplish the organization's mission. And much of the nonprofit's budget is spent on personnel costs.
    - As a nonprofit board member, you should have at least a basic familiarity with the federal and state-specific laws and regulations that govern nonprofits. This includes regulations concerning how nonprofits interact with staff, contractors, volunteers, and their own board members (in this case, you).
    - As with the other courses in this series, the "Personnel Issues" module will provide you an overview of some important themes and challenges that nonprofits face in managing their human resources. Just as important as the information presented here are the additional resources you can access to gather more detailed guidance on each theme. You will find links to these resources throughout the module and by clicking the "Additional Resources" link below.
    - The topics we will cover are:
        - General human resources considerations
        - Executive and board compensation
        - Director orientation and onboarding
        - Succession planning
- General Human Resources Considerations
    - If your organization has an executive director and staff, you aren't likely to get involved in the day-to-day operations of the organization, including its human resources decisions. In fact, the Executive Director should generally have primary control of decisions related to personnel, hiring, and management functions. However, there are a few topics you should be familiar with when discussing staffing with the executive team:
        - Employee withholding taxes
        - Unemployment insurance and workers' compensation
        - Employee vs. independent contractor status
        - Whistleblower policy  and other employee related policies
    - Board member knowledge of these topics is especially important in smaller organizations where directors are expected to play a more active role in operational decision-making.
    - Employee withholding taxes
        - As an employer, the organization is responsible for withholding certain taxes from employees' pay checks, and paying certain amounts themselves. Federal employment taxes include the following: Federal income tax withholding (FITW),

Social Security and Medicare taxes (FICA, half of which is withheld from the employee's paycheck, and half of which is paid by the employer), and Federal unemployment taxes (FUTA, which is paid by the employer, not withheld from the employee's paycheck). Importantly, 501(c)(3) organizations are exempt from paying FUTA.

  - More information on this topic is available on the IRS website at http://www.irs.gov/Charities-&-Non-Profits/Employment-Taxes-for-Exempt-Organizations. See in particular IRS Publication 15 (2013), Circular E, "Employer's Tax Guide," and IRS Publication 15A, "Employer's Supplemental Tax Guide."
  - In addition, nonprofits with employees in Colorado must collect and remit state wage withholding taxes. You can find more information about withholding taxes on the Colorado Department of Revenue's website: http://www.colorado.gov/cs/Satellite/Revenue/REVX/1177017542100.
  - Finally, you should check with local municipalities to determine if they assess any additional taxes or fees on employees or employee wages.
- State unemployment insurance and workers' compensation
  - State unemployment Insurance
    - The IRS determines withholding taxes for federal unemployment insurance. Nonprofits must also keep in mind state regulations regarding unemployment insurance.
    - Nonprofit and charitable organizations are covered by the Colorado Employment Security Act (ESA) if they have four or more employees for some portion of a day in each of 20 different weeks within the current or preceding calendar year. This program is administered by the Division of Employment and Training of the Colorado Department of Labor and Employment.
    - Nonprofit organizations are not required to purchase unemployment compensation insurance through the State of Colorado, but they are required to register with the Unemployment Division if they have four or more employees. If a nonprofit organization does not purchase unemployment insurance from the State of Colorado, it becomes a direct reimburser, meaning that claims filed will be paid by the State and the nonprofit must reimburse the State.
    - Alternatively, your organization may wish to apply for an unemployment insurance account with the Colorado Department of Labor and Employment by filing Form UITL-100. The Unemployment Compensation Program is also administered by the Division of Employment and Training.
    - You can find this form, a copy of the ESA, and other information related to unemployment insurance at the Colorado Department of Labor and Employment's website: http://www.colorado.gov/cs/Satellite/CDLE-UnempBenefits/CDLE/1248095315884.
  - Workers' Compensation Insurance
    - Workers' compensation regulations vary by state. In Colorado, with limited exceptions, all employers must provide workers' compensation coverage for their employees if one or more full or part-time persons are employed. This includes nonprofit organizations.
    - The state workers' compensation system is administered by the Colorado Department of Labor and Employment - Division of Workers' Compensation. The division publishes several guides to the workers' compensation system; visit its website for more information at

http://www.colorado.gov/cs/Satellite/CDLE-WorkComp/CDLE/1240336932511 .

- For historians, the Colorado DLE also has an interesting, brief history of workers' compensation insurance on its website.

- Employee vs. Independent Contractor
  - One question that many nonprofits (and other private businesses) face is how to classify those people who provide services to the organization. Generally, these individuals can be classified as either independent contractors or as employees.
  - Classifying an individual as an independent contractor comes with many financial advantages, most notably that the organization is not required to withhold or pay any taxes on payments to that person. On the other hand, businesses must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to an employee. According to the U.S. Department of Labor, an independent contractor may cost a business 20 to 40 percent less than an employee. [1]
  - But wait! Before your nonprofit reclassifies all of its employees as independent contractors, you should know that both the IRS and the Colorado Department of Labor and Employment take very seriously the misclassification of individuals providing services. Both have stepped up audits in this area, and are fairly aggressive about seeking to reclassify workers.
  - Both the IRS and state agencies can levy stiff fines for misclassifying employees as independent contractors. To help your organization avoid trouble, the IRS has promulgated a test with 11 factors[2] that can help you distinguish between an independent contractor and an employee. The following presents a brief overview of this test. You can find more detail on the IRS website, and in IRS Publication 15-A.[3]
  - The 11-factor test
    - The test is designed to determine the degree of control and independence enjoyed by the individual and the organization.
    - The IRS divides the 11 factors into three types of control that an employer may exercise:
      - Behavioral Control: Does the company control or have the right to control what the worker does and how the worker does his or her job?
      - Financial Control: Are the business aspects of the worker's job controlled by the payer?
      - Type of Relationship: Are there written contracts or employee type benefits? Will the relationship continue and is the work performed a key aspect of the business?
    - Behavioral control includes the type and degree of:
      - Instructions that the business gives to the worker about when, where, and how to work. This includes instruction on location and time of work, use of tools or equipment, where to purchase supplies

[1] Statement of Seth D. Harris, Deputy Secretary, U.S. DOL, before U.S. Senate Committee on Health, Education, Labor, and Pensions (June 17, 2010), http://www.dol.gov/_sec/newsletter/2010/20100617-2.htm

[2] The current test is a refinement of an earlier 20-factor test used by the IRS. Some states continue to use the 20-factor test as a guide.

[3] IRS Website: http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Independent-Contractor-Self-Employed-or-Employee. Publication 15-A: http://www.irs.gov/pub/irs-pdf/p15a.pdf.

and services, etc. According to the IRS, the key consideration here is whether the business has retained the right to control the details of a worker's performance or instead has given up that right.
    - Training that the business gives to the worker. In general a company will train employees to perform work in a certain manner. Independent contractors, on the other hand, are more likely to work according to their own methods.
  - Financial control factors in whether the business has a right to control business aspects of the worker's job, including:
    - The extent to which the worker has unreimbursed business expenses. Independent contractors are more likely to have unreimbursed expenses, especially fixed costs incurred regardless of work being performed.
    - The extent of the worker's investment. Independent contractors often have significant investment in the tools and facilities used to perform services, though this is not necessary for a worker to qualify as an independent contractor.
    - The extent to which the worker makes services available to the market. Independent contractors are typically free to seek out other business opportunities.
    - How the business pays the worker. With some exceptions, employees are typically paid a regular wage amount over a period of time, while independent contractors are often paid a flat fee or on a time and materials basis for the job.
    - The extent to which a worker can realize a profit or loss. Independent contractors can make a profit or loss.
  - Other factors for determining the type of relationship between the two parties include:
    - Written contracts describing the relationship the parties intended to create.
    - Whether or not the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay.
    - The permanency of the relationship. Employees generally have the expectation that the relationship will continue indefinitely, while contractors are typically brought on for a specific project or period.
    - The extent to which services performed by the worker are a key aspect of the regular business of the company. If a worker provides services that are a key aspect of your regular business activity, it is more likely that you will have the right to direct and control his or her activities.
- In addition, the Mountain States Employers Council publishes an excellent guide on employees and independent contractors for its members; this eLearning course relies heavily on much of the information presented in the guide. In any case, your organization should consult legal counsel with any doubts concerning personnel classification
- Again, you should consult legal counsel if you have any doubts about how to classify your workers.

- Whistleblower policy and other employee policies

        - The board should approve a whistleblower policy that includes procedures for reporting violations of applicable laws or policies. The board will generally be part of the reporting process, as well.
        - A nonprofit also should have policies and guidelines for managing employees and volunteers. These can cover a variety of issues, including employee benefits, nondiscrimination, holidays and personal leave, and employee conduct. The board's involvement in creating or overseeing these policies will generally be more limited, assuming it has delegated this to staff members who work collaboratively and with legal counsel as needed.
- Executive and board compensation
    - As a nonprofit board member, one of your most important responsibilities is to help recruit and select the organization's executive leadership—those individuals who manage the nonprofit's day-to-day operations. Most often, the board will be responsible for selecting and evaluating the performance of the chief executive, but you may also be involved in selecting and evaluating the performance of other executive staff. It is prudent to have a structure in place which allows for a direct reporting relationship between the board and the senior financial officer of the organization.
    - When hiring executive staff, you and your colleagues will need to settle on a compensation package. While Colorado and federal law prohibit nonprofits from providing excessive compensation,[4] neither offers absolute black-and-white rules on what constitutes "reasonable compensation."
    - However, the IRS does provide a process that boards should follow for crafting a compensation package,[5] which allows a 501(c)(3) public charity or 501(c)(4) social welfare organization to establish a rebuttable presumption that compensation is reasonable. Though it technically does not apply to other types of tax-exempt organizations, it's a good process for them to follow regardless. This process requires the following steps:
        - The compensation package should be approved in advance by an independent governing body, which is usually the board or the board's compensation committee. Importantly, members of this body should recuse themselves if they have a material or perceived conflict of interest.
        - The independent body should obtain data on compensation for comparable duties or positions, and should rely on this information in making its determination.
            - CAUTION: some boards fall into the trap of using "questionable comparables" to determine executive compensation. This can occur if the board looks for comparable positions at larger entities, organizations in vastly different geographic areas or organizations working in different fields or market segments.[6] To avoid this pitfall, use care in selecting your comparable data.
        - The independent body should adequately document the basis for determination, including the comparables data and analysis, concurrently with making the determination.
    - Additional resources

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[4] CRS § 7-133-102; IRC §§ 501(c)(3)

[5] CFR § 53.4958. http://www.gpo.gov/fdsys/pkg/CFR-2012-title26-vol17/pdf/CFR-2012-title26-vol17-sec53-4958-6.pdf

[6] Cotter, Timothy J. "Advising the Executive Compensation Committee: Practical Suggestions for the General Counsel." 2011.

        - The Colorado Nonprofit Association publishes an annual "Salary and Benefits Survey." The study relies on detailed data from a range of Colorado nonprofits to help organizations like yours establish reasonable and competitive compensation packages. The guide is available at: http://www.coloradononprofits.org/help-desk-resources/research-publications/salarysurvey/.
        - Mountain States Employers Council also provides its members with annual compensation surveys for a broad range of industries, including nonprofits and foundations. You can view an index of the surveys at https://www.msec.org/services/surveys/Pages/Compensation-and-Benefit-Surveys.aspx, though the survey data and analysis are only available to MSEC members.
- Board compensation
    - In general, nonprofit board members do not receive compensation for their service, although Colorado law does allow for "reasonable" compensation for directors.[7] The federal tax laws also allow for it, though the IRS often frowns on this practice. "Principles for Good Governance and Ethical Practice," issued by the Panel on the Nonprofit Sector and the "Principles and Practices for Nonprofit Excellence in Colorado" issued by the Colorado Nonprofit Association both discourage compensation for board members. The Better Business Bureau's Standards for Charity Accountability recommend that not more than one or 10% (whichever is greater) directly or indirectly compensated person(s) serve as voting member(s) of the board, and that no compensated member serves as the board's chair or treasurer.
    - There are some cases where it may make sense to provide compensation for board members. Some organizations pay directors a fairly modest stipend, for example, in recognition of the time that directors put in to the organization and to emphasize that they provide much value. However, organizations should be mindful when they embark upon this practice that there can be some backlash by funders or watchdog groups.
    - Reimbursing directors for board-related expenses is more common, such as expenses related to board meetings and retreats. Ideally, these types of reimbursements are made in accordance with established corporate policy to ensure they are appropriate and reasonable.
    - In any case, it is important to remember that compensating board members can mean that the protection of volunteer immunity laws is lost (though this won't always be the case with respect to expense reimbursement). For more information about the volunteer immunity laws, see the eLearning module on the Fiduciary Duties of Nonprofit Directors.
- Director orientation and onboarding
    - Many of us have benefited from effective orientation and onboarding activities as new employees of an organization (more on how both terms are defined below). However, while it is common to have procedures in place to welcome new workers, nonprofit boards often do not place the same emphasis on bringing new board members up to speed quickly and effectively. This section provides a few tips for getting new directors engaged and up-to-speed quickly. While we focus on the board and its members, you (or, more likely, your organization's staff) could also apply many of these lessons to improve onboarding procedures for employees.
    - First, it's useful to differentiate between two related but separate concepts: orientation and onboarding. Colorado-based Mountain States Employers Council provides a useful distinction in one of its educational resources:

[7] CRS § 7-133-102(b)

        - "Orientation in its traditional sense is a one-time meeting with an HR professional where the employee completes paperwork and receives information about the organization. Onboarding, on the other hand, is an ongoing developmental process designed to include interaction, information, and instruction to the new employee." [8]
    - In the context of a nonprofit board, then, "orientation" is likely to happen prior to and during the new director's first few board meetings. Metro Volunteers lays out the purpose of such an orientation in its "Board Leadership Agency" training course. According to Metro Volunteers, the purpose of new director orientation is to:
        - Allow the new board member to get acquainted with other board members
        - Become familiar with board responsibilities
        - Get up to speed on current issues to effectively participate in their first board meeting
        - Provide an overview of programs, finances, etc.
    - Metro Volunteers goes even further to recommend some activities that the board can engage new members in during the orientation process:
        - Tell a success story or ask a program beneficiary to attend a meeting and highlight the difference that the organization has made in his or her life.
        - Go on a tour of the organization's facilities.
        - Outline how the board promotes effective working relationships between board members and the executive team.
        - Provide an overview of board responsibilities, including committees and resource development.
        - Do a quick review of your board handbook (this is a good refresher, too, even for long-standing members). The board handbook should contain at least the following information and resources:
            - A copy of the articles of incorporation with all amendments
            - A copy of the bylaws with all amendments
            - The organization's most recent IRS Form 990
            - A short summary of the organization's mission and objectives
            - A list of all board policies
            - A board meeting schedule (if applicable)
            - Director names and addresses
            - References to any other relevant information
        - Take some time to discuss current issues and happenings.
        - Allow plenty of time for questions and answers (remember how many questions you had when you first came on board?).
    - In short, an effective orientation should allow your new directors to hit the ground running.
    - "Onboarding," though, is a much more involved process. It may begin even before the new director attends her first meeting and last well into her first year. The American Association for Adult and Continuing Education (AAACE) identifies a few primary objectives for the onboarding process:
        - Provide resources to assist understanding of the organization.
            - In addition to the documents listed previously, it may be useful to provide annual reports, overviews of programs and services, fundraising summaries,

[8] "FYI: Independent Contractors." Mountain States Employers Council. September 2010.

                - and other documents that give new directors context for their work on the board.
        - Generate opportunities to meet and interact with others to build a sense of inclusion.
            - Remember, the best resources are often human resources. Make sure you and your fellow directors set aside time to spend with new board members outside of formal meetings to answer their questions and provide insight into the organization's work.
        - Identify high quality mentors or coaches to provide guidance regarding culture and expectations.
            - While general information about your organization is useful, new board members will often benefit from a close, structured relationship with a director or directors. Mentors can bring their experience to bear in helping new arrivals become active and productive board members.
            - It's very important to train your chosen mentors so that they know how best to help new board members. Think about holding brief group trainings so that all mentors are on the same page prior to taking on their mentees.
    - As with most policies and procedures, your board's orientation and onboarding processes will differ depending on the organization's specific characteristics like size, level of involvement, relationship to the executive team, etc. Regardless of what shape these processes take, though, your board will benefit from an organized and deliberate welcome for new directors.
- Succession planning
    - Here's a fact that may alarm you as a nonprofit board member: a 2006 study of 1,900 nonprofit leaders found that 75 percent of them planned on leaving their positions within the next five years.[9]
    - As a nonprofit board member, one of your most important responsibilities is to ensure the long-term viability of your organization. The board of directors can help bolster sustainability by establishing policies to identify and prepare individuals for leadership positions, a process typically known as succession planning or leadership development.
    - For-profit corporations engage in succession planning in order to maintain and grow their competitive advantage in the marketplace. For nonprofit organizations, succession planning is a means of ensuring good stewardship of charitable assets. For this reason, the Colorado Nonprofit Association recommends that nonprofit boards engage in succession planning for the chief executive, board members, and key staff.[10] As another guide puts it, "As the ultimate guardian of the community's investment in the agency, it is the board's duty to attend to succession planning—and long before leadership issues create a crisis for the agency."[11]
    - So, how do you get started? A number of useful guides provide outlines for succession planning, some of which we reference in the "Additional Resources" section of this course. One especially useful guide comes from a series called "Building Leaderful Organizations," published by the Annie E. Casey Foundation. The guide focuses on three approaches to succession planning, the particulars of which we'll explore briefly here.
        - Strategic Leader Development

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[9] Bell, J, et al. *Daring to Lead 2006*. CompassPoint Nonprofit Services, 2006.
[10] Colorado Nonprofit Association. "Principles and Practices for Nonprofit Excellence in Colorado." Page 15.
[11] Wolfred, Tim. *Building Leaderful Organizations: Succession Planning for Nonprofits*. The Annie E. Casey Foundation, 2008.

- The aim of this approach is to broaden the leadership pool within an organization over time.
- It's a good idea to associate this process with another important planning tool: your organization's strategic plan. A key component of the strategic plan is identifying long-term goals and direction. In turn, these objectives will allow you to isolate those leadership competencies that are critical to the organization's mission.
- Mountain States Employers Council suggests starting with a series of interviews with key leadership and staff to determine what competencies are truly needed to ensure success.[12]
- Based on these critical competencies, the board and the executive team can develop a plan to promote leadership skills and knowledge within the organization's staff.
- Of course, strategic leader development can be time-consuming and may be nearly impossible to execute in smaller nonprofits. In cases where long-term, strategic succession planning is infeasible or very difficult, the Annie E. Casey study presents two other viable options to help minimize risk to your organization.

▪ Emergency Succession Planning
  - This strategy is exactly what it sounds like: preparing your organization for sudden, unexpected departures of executive management and other key staff. The Annie E. Casey Foundation lays out several helpful steps for creating such a plan for the organization's executive director. You can adapt this process for other positions, including important board members.
    - Identify the position's critical leadership and management functions.
    - Discuss which functions should be covered by an acting director and which should be delegated to a secondary manager if the executive director departs.
    - Determine who has the authority to appoint an acting director (this could be a committee or specific members of the board).
    - If possible, select "standing appointee(s)" for the acting director position. It's also a good idea to appoint back-ups in case more than one member of the management team exits at the same time.
    - Develop a training plan for the back-ups that prepares them for the acting director role.
    - Determine how the board will support and supervise the acting director.
    - Create a communications plan to be used in the event of an emergency succession. This plan should include the "who" and "how" of communications.
  - You are probably asking yourself: "Well, how do I fit into this process?" The truth is, many nonprofits (especially larger organizations) will employ the services of a consultant to draw up an emergency succession plan. In any case, the board should ratify the final emergency plan for at least the top executive position. Your board may want to take a more pro-active approach. In this case, the Annie E. Casey Foundation recommends forming

[12] "FYI: Succession Planning." Mountain States Employers Council. September 2012.

a two-person Emergency Succession Planning Committee. This special committee can work with the executive director and/or consultant to create, vet, and approve emergency succession plans for key positions.

- Departure-Defined Succession Planning
    - The third type of succession planning identified by the Annie E. Casey Foundation is "Departure-Defined Succession Planning." As with Strategic Leader Development, this type of planning assumes that your organization is fortunate enough to have a strong executive director with the foresight to make clear medium- and long-term planning decisions.
    - Perhaps the most important component of the departure-defined succession plan is the departure date itself. Ideally, a nonprofit should start formulating a succession strategy two to three years out from a leader's planned exit. Sound like a long timeframe? For many nonprofits and their leaders, it is. But if you go down this route, make sure you allow at least 18 months to create and execute your plan.
    - Once the executive has decided on a departure date, the board can begin to work with him/her on a few key areas to pave the way for a successful separation:
        - Conduct a "sustainability audit": this involves identifying internal operations and external relationships that may be jeopardized with the executive's departure. The board can help to address these potential issues by directing organizational changes and developing or deepening relationships with donors and other external stakeholders.
        - Shoring up financials: many nonprofit executives (especially long-standing ones) retain important financial information informally—in other words, "it's all in my head." The board can avoid post-departure issues by ensuring that financial systems and procedures are standardized and that remaining staff understand the functions and their own place in the processes.
        - Sharing leadership responsibilities: the departure of a strong executive can leave large gaps in a nonprofit's leadership structure. If approached creatively, though, these gaps can provide opportunities to strengthen the organization over the long run. As a board member, you can help your organization take advantage of a leadership transition by promoting staff development opportunities that simultaneously address the weaknesses left by the departing executive and rejuvenate key staff members by providing them with new responsibilities.
    - Finally, an executive's departure may be a chance for you and your fellow board members to think about your own succession plan. Many boards have directors whose tenure, knowledge, and influence are sorely missed when they leave. Think about your own board and how you might apply the principles and steps above to ensure that the strength you've built continues as the board evolves.

- One final note. Succession planning is no different from other aspects of running a nonprofit: the way your board tackles the issue will differ from other organizations' strategies. That being said, we'll leave you with a thought from Anne Mulcahy, former Xerox CEO and Chairwoman, that we think applies to any nonprofit:
    - "One of the things we often miss in succession planning is that it should be gradual and thoughtful, with lots of sharing of information and knowledge and perspective, so that it's almost a non-event when it happens."

## Additional Resources

Bell, J, et al. *Daring to Lead 2006*. CompassPoint Nonprofit Services, 2006. http://www.compasspoint.org/research/daring-lead-2011-national-study-nonprofit-executive-leadership

Colorado Department of Revenue Website. http://www.colorado.gov/revenue

Colorado Department of Labor and Employment Website. http://www.colorado.gov/cs/Satellite/CDLE-Main/CDLE/1240336821467

Colorado Nonprofit Association. “Principles and Practices for Nonprofit Excellence in Colorado.” http://www.coloradononprofits.org/help-desk-resources/principles-practices/

Cotter, Timothy J. “Advising the Executive Compensation Committee: Practical Suggestions for the General Counsel.” 2011. http://www.healthlawyers.org/Events/Programs/Materials/Documents/IHC11/cotter_peregrine_resource.pdf

Wolfred, Tim. *Building Leaderful Organizations: Succession Planning for Nonprofits*. The Annie E. Casey Foundation, 2008. http://www.aecf.org/~/media/Pubs/Other/B/BuildingLeaderfulOrganizationsSuccessionPlann/Building%20Leaderful%20Organizations.pdf