

Set Your New Nonprofit CEO Up for Success: Start with an Employment Agreement

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You have found your new CEO after a long, arduous process. Your board is looking forward to years of stability and is eager to get the new leader started. But before you begin the onboarding process, do not overlook the value of an employment agreement. It could be the most essential tool for building a successful relationship.

A well-drafted agreement will set expectations for both parties, ensuring that your board and its new CEO are on the same page with respect to the role as well as the terms and conditions of employment. Hammering out the details of the relationship at the outset can help set the new CEO up for success, and it can help build a shared vision of the future of the organization. If things don't work out, an employment agreement can also help make the CEO's departure more orderly.

The employment agreement can help the board flesh out three key areas that will help get the CEO started on the right foot and smooth potential bumps down the road. These areas include:

- Setting expectations for the role
- Spelling out compensation and benefits
- Providing clear steps if the relationship doesn't work out

Setting Expectations

What does the board want the CEO to focus on in the first year? Does the board want to limit the term of the CEO's employment for any reason? What metrics will the board use to measure success? Setting—and documenting—these expectations can be a collaborative act, helping the CEO and board start with a mutual understanding about their respective roles.

For example, a CEO will likely want to know if the contract is for a specified term with an option to renew or an open-ended agreement that provides ongoing employment. Many organizations opt for a specified term with automatic renewal, but agreements also can be for an indefinite period. The board should ensure that, if the agreement is for a specified term, it can be terminated before the end of the term for various reasons, both with and without cause.

The agreement should also include a section that summarizes the CEO's job duties. This doesn't take the place of a more detailed job description but rather conveys in broad strokes the most important aspects of the role. Success in the CEO role often requires an understanding of—and commitment to—what matters to the board. An employment agreement offers an important opportunity to confirm that the board and the CEO are on the same page with respect to how the CEO will spend his or her time. For example, the agreement should spell out whether the board expects the CEO to dig in and work on implementing the new strategic plan, or delegate those duties and focus instead on fundraising, or juggle both of these important responsibilities. By including a summary of the CEO's job duties, both parties reduce the likelihood of misunderstanding the position's priorities. Many agreements also detail how, and how frequently, the CEO's performance will be evaluated. Performance feedback is an important facet to gauging a CEO's success, and the board should be willing to commit to a reasonable process and then follow through with it.

Employment Agreement Must-Haves

A well-drafted employment agreement includes, among other things, the following key provisions:

- Term of the agreement
- CEO duties
- Compensation and benefits
- CEO duties
- Performance evaluation process
- Reasons for termination (death, disability, for cause, without cause, for good reason, by mutual agreement)
- Severance
- Post-employment obligations
- Breach of contract

Benefits and Compensation

The financial aspects of the relationship are obviously a major issue for both the board and the CEO. The agreement should state how much and when the CEO will be paid. In addition, it is important to address the timing of salary increases and whether any increase is tied to a particular performance metric. Also important are details about bonuses the CEO may be eligible for as well as the other components of the total compensation package (i.e., retirement plan, health insurance, short and/or long-term disability benefits, life insurance, housing, education assistance plans, vacation, and other paid time off).

A cautionary note: many nonprofit organizations are subject to significant tax penalties if certain key executives, including the CEO, receive “excess benefits” from the organization. Excess benefits include compensation that exceeds the fair value of the services rendered. There are important exceptions to these rules as well as a “rebuttable presumption” of reasonableness if the organization, among other things, obtains and relies on comparability data when approving the compensation. These rules are complicated and the consequences for getting this wrong are serious. Therefore, before finalizing the agreement, the board should discuss the compensation package with experienced employment counsel.

Parting Ways

Although it may seem like bad karma to discuss the end of the employment relationship when it is just beginning, there is no better time to sort out the details of an amicable parting than when the CEO and the board are feeling good about the relationship and optimistic about the future.

The agreement should detail the various circumstances that would result in termination (by death or disability, termination by the organization with or without cause, or by the CEO for good reason) as well as what severance benefits the CEO is entitled to upon termination.

Defining the various termination options is a critical component of an employment agreement. Most agreements specify that employment terminates upon death or disability. In addition, agreements typically permit the board to terminate the CEO’s employment for cause. Nonprofit boards can expect to spend some time negotiating the definition of cause—the board will want a fairly broad definition and the CEO will want to ensure that the definition is narrow. For example, employment agreements often include in the definition of cause most criminal convictions, even if the criminal offense relates to off-duty conduct. The agreement also should include a provision for the board to terminate the CEO’s employment without cause, just in case the board decides to move in a different direction even if the CEO has not engaged in any misconduct. Many agreements have a fairly narrow definition of cause and a broad “without cause” provision. Finally, CEOs generally want to include a termination provision triggered by the CEO for “good reason,” such as if the CEO’s job duties change significantly or compensation decreases.

In addition to defining the various termination options, the agreement should also detail whether termination requires notice and, if required, how much. Notice is an important safeguard for both the CEO and the organization, increasing the possibility of a smooth transition. Most employment agreements require 30 or 60 days' notice. Typically, the CEO will continue to be paid during the notice period, whether or not the board expects the CEO to continue to work through the notice period. It is important for the agreement to spell out that the CEO can be relieved of duty during the notice period at the discretion of the board.

Most agreements provide for severance in the event the CEO is involuntarily terminated without cause or elects to resign with good reason. This soft landing in the event the relationship is not successful is important protection for the CEO. It is much less common to see severance offered in the event of a termination for cause or a voluntary resignation without a good reason. If severance is offered in any circumstance, the agreement should explicitly state that the CEO must sign a standard release agreement (under which legal claims are waived) in exchange for the severance payment.

In addition to addressing how the employment relationship will end, the agreement should also address post-employment restrictions, if any, such as non-compete or customer non-solicit obligations. While not all CEO agreements include such restrictions, all agreements should include a confidentiality provision that protects the organization's confidential information during and after employment.

Admittedly, it takes time to work through these provisions, but it will be time well spent. Negotiating these details provides an important opportunity for the board and the CEO to start the relationship on the same page. By stating the parameters of success at the beginning of the relationship, an employment agreement can set a critical foundation for arguably the most important relationship in your organization: the one between the board and the CEO.



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