Testimony of

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Testimony for the Committee for Purchase From People Who Are Blind or Severely Disabled

Public Hearings Relating to Governance and Executive Compensation

January 12, 2006

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We appreciate having this opportunity to comment on the issues regarding the Committees' plan to reissue a proposed rule on Non-Profit Agencies (NPA) Governance and Executive Compensation. NISH is one of two central nonprofits agencies (CNA's) charged with the responsibility to assist the Committee for Purchase From People Who Are Blind or Severely Disabled (the Committee) in implementing the Javits-Wagner-O'Day (JWOD) Program. As such, we assist 553 producing nonprofits (including private non-profit agencies, state agencies, county agencies, hospitals, schools and other entities) as they provide jobs for nearly 42,200 people with severe disabilities who deliver $1.8 billion annually in quality goods and services at a fair market price to the Federal government.

The JWOD Program is the largest single employer of people with severe disabilities in the United States with operations in every state. We understand and support the Committee's desire to address the executive compensation and governance issue. Like the Committee, our highest priority is to ensure the continued confidence of Congress, taxpayers, Federal agencies and the 20 million people with severe disabilities, of whom 70% are unemployed or under employed, that the JWOD Program operates with integrity and efficiency.

Qualified Agencies Have Good Governance Practices

The Committee has requested further information and perspective in several areas related to governance practices. My statement is structured to address each of these areas. In a few areas the questions have been combined where the basic theme is the same.

(1) Are these criteria comprehensive and inclusive enough to effectively evaluate that a nonprofit agency demonstrates good governance practices and should be deemed qualified to participate in the JWOD Program?

The criteria stated in the Federal Register of December 16, 2005 provide a comprehensive template for good governance as they closely follow recommendations in the report, <u>Strengthening Transparency, Governance, and Accountability of Charitable Organizations</u>, published by the Panel on the Nonprofit Sector convened by the Independent Sector in June of 2005. This report is the compilation of the wisdom of thousands of people involved with charities and foundations who conducted a thorough examination of the sector's best practices in governance, transparency, and ethical standards. This exercise, which responded to increased attention to these issues stimulated by Congressional concerns, involved the participation of people from organizations of widely varying sizes and programs and reflected the charitable community's long-standing commitment to accountability.

(2) Are there additional criteria that should be used, or substituted for the above, to evaluate evidence of good governance practices by nonprofit agencies in the Program?

No additional criteria need to be used with or substituted for the published criteria. The criteria stated in the Federal Register notice of December 16, 2005 sufficiently addresses the standards of best practices in good governance as described by the report, <u>Strengthening Transparency, Governance, and Accountability of Charitable Organizations</u>, published by the Panel on the Nonprofit Sector convened by the Independent Sector in June of 2005. NISH believes that the JWOD Program should remain in step with the larger non-profit community thinking as it is taking a proactive approach to following governance best practices.

(3) Should accreditation by state or national organizations be recognized as evidence of a nonprofit adhering to good governance practices without review by the Committee?

(6) What is the best way to ensure that only qualified central nonprofit agencies and nonprofit agencies, with an internal structure that minimizes opportunities for impropriety, participate in the Program?

In reply to questions three and six, the Committee should recognize accreditation as evidence of a nonprofit agency adhering to good governance practices if the accreditation criteria used by the reviewing national, state, or local entity includes governance provisions that are comparable to or exceed the criteria stated in the Federal Register of December 16, 2005. A list of acceptable third party organizations and their accrediting standards could be published in advance by the Committee.

In those few instances where accreditation has not been obtained, an alternative might be for the Committee and OMB to explore whether legal authority exists for requiring the two central nonprofits to take on that role using some recognized accreditation process, or as a variation of this approach, to develop certification procedures that include peer review standards that are collaboratively developed in the areas covered by the proposed rulemaking. This would create a new reporting burden on the nonprofits and the CNA's, but this burden might be offset by the benefit of encouraging participation by the JWOD nonprofits in the creation and implementation of appropriate and achievable standards. However, using existing accrediting organizations remains our preferred solution to address this issue.

(4) Should different benchmarks be used for nonprofit agencies that are state, county, or local government agencies, or should they be exempt from Committee regulations in this area?

Nonprofit agencies that are state, county or local government agencies should be exempt in the executive compensation and governance areas from any Committee regulations that might be implemented in this area because they are still subject to scrutiny by public entities using comparable public sector measures. These agencies should continue to be subject to all other JWOD Program regulations.

(5) Should the size and/or the annual revenue of the nonprofit agency be a factor or factors in assessing appropriate governance practices?

JWOD/NISH nonprofit agencies have the ongoing burden of meeting a plethora of local, state, and federal reporting mandates, including Department of Labor reporting regulations associated with complying with Section 14C of the Fair Labor Standards Act (the commensurate wage program). This frequently stretches the reporting ability of many small nonprofits to their limits. We are concerned that any added burden may make the JWOD Program less financially feasible to them and result in a loss of jobs for people with severe disabilities. NISH proposes that agencies with small amounts of JWOD sales and/or revenues be exempt from the rule. Specific thresholds could be determined; however, a proposed threshold might be $100,000 in total JWOD sales and total sales revenue from all sources of $500,000 or less (there are 75 of the 553 nonprofit agencies or 13.5% that meet this criteria). This would provide some relief but governance practices would still apply to the vast majority of JWOD producing nonprofits. It should be noted that many of these small nonprofits that would benefit from such an exemption exist in inner city and rural locations in underserved communities across the country. It is important to be sensitive to the burden placed on small and inner city locations with high concentrations of unemployed persons with disabilities and in rural locations where alternatives for employment are nonexistent or remote.

(7) What if any enforcement mechanisms should be adopted to ensure only the qualified central nonprofit agencies and nonprofit agencies participate in the JWOD Program?

The Committee should continue to conduct periodic compliance visits that are based upon generally accepted auditing standards utilizing both its own staff and staff of the two central nonprofit agencies. However, the frequency and extent of compliance monitoring to ensure the NPA's are employing people with severe disabilities should also be carefully reviewed. There are many ways to clarify and buttress program requirements for ensuring compliance including recommendations to shorten time between reviews, resource for more in-depth, random reviews, and increase mandatory training. Given the dynamic growth of the program in volume and complexity there should be an annual review of enforcement mechanisms processes. If the Committee seeks additional enforcement and/or movement from the traditional consultative approach provided for by current policies to more formal investigative audits by the CNAs, the Committee would need to provide for or delegate such added authority.

(8) What steps will the nonprofit agencies and central nonprofit agencies need to take to avoid conflicts of interest among its board members?

To avoid conflicts of interest among its board members nonprofit agencies and central nonprofit agencies should follow the guidelines published by the IRS and the Independent Sector addressing disclosure, board member selection, and compensation. These guidelines involve having specific policies and training that relate to disclosure, conflict of interest, compensation, and related matters and provide guidance that, if followed, outline actions to preclude conflict of interest. While existing guidelines provide guidance, the Committee could be assured that a systematic process is in place if a certification to this effect could be added to the Form 404 Report along with the information specified in the answer to number nine (9) below.

(9) What steps will the nonprofit agencies and central nonprofit agencies have to take to demonstrate financial responsibility?

CNAs and NPAs should submit an annual written statement or declaration, ideally as part of the currently submitted Form 404 Report, signed by the Chair of the NPA Board of Directors and the NPA Chief Executive Officer (CEO)/President, explicitly certifying that the NPA is maintaining a board of independent members, that the Board of Directors approves compensation arrangements for highly paid executives and individuals using independent comparative salary data gathered from similar organizations for similar executive positions. Additionally it should document data used in decision making for compensation packages. As noted above, a conflict of interest statement could also be included in this declaration.

Effect of Executive Compensation on Fair Market Price Determinations

(1) What is the threshold beyond which the compensation paid to the executives in a JWOD-participating nonprofit agency should be considered as influencing a proposed fair market price determination? For example, if the agency receives more than a certain percentage of its total revenue from sales through the JWOD Program, is there a compensation level (total dollars paid or total dollars paid as a percentage of total revenue) at and above which fair market price impact would be deemed to occur?

(2) Conversely, is there a point below which executive compensation, regardless of the dollar amount paid, would not be considered as influencing a recommended fair market price? Is such a *de minimis* test appropriate for large diversified nonprofits where total JWOD sales represent only a small percentage of total revenue?

(3) Without regard to any analysis of JWOD-related revenue, is there an established benchmark or absolute dollar threshold above which compensation would be deemed as influencing a proposed fair market price?

In reply to these three related questions NISH believes that there is no absolute dollar threshold that could equitably take into account the vast differences in scope, complexity, product and service mix, populations of people with blindness or severe disabilities, rehabilitation and government funding sources, community needs, and varying federal, state, and local regulatory requirements of all 640 NPAs in the JWOD Program.

However, while there may not be an absolute dollar value that can fairly be used to assess compensation reasonableness, an assessment can be made of the objectiveness of the process used to determine salary and total compensation using the certification on the Form 404 described elsewhere in this statement. Additionally, compensation could be compared on a percentage basis to overall revenue or budget similarly to how it is done by *The Chronicle for Philanthropy* and other publications and organizations that compare and analyze compensation data of NPA executives.

In regard to recent assertions and/or speculations that higher CEO compensation on the part of a producing JWOD Non-Profit Agency (NPA) has a direct effect on JWOD Fair Market Prices, this does not hold up upon an examination of the facts.

First, JWOD contract prices are tied to prices from the commercial market. The Committee's guidelines, Pricing Memorandum # 3 (PR3), require that prices proposed by NPAs be tied to actual prices paid in the commercial market for the same or similar services. In fact, two of the JWOD Program's largest federal customers, the Defense Commissary Agency (DeCA) and the General Services Administration Public Buildings Service (GSA/PBS) established Market Pricing agreements that explicitly tie agreed to prices to the commercial market. In the case of DeCA, NPA's must have prices in line with other small businesses for the same or similar services. GSA/PBS prices are benchmarked against a very in-depth commercial market pricing indicator that is calculated by an independent third party on a rolling quarterly basis.

Second, JWOD approved Fair Market Prices allow for a General and Administrative (G & A) plus overhead rate that is capped at a rate 9.5% calculated on the NPA's subtotal of all costs for a given contract. This overhead rate includes fee (profit in commercial terms). This rate is generally considered to be 6% to 10% below the commercial market industry. NPAs have the ability to have their G&A rate set higher if they can demonstrate that their rate is higher based on actual experience. However, the overwhelming majority of producing NPAs use the 9.5% rate.

Finally, JWOD contracts are fixed price contracts which differ significantly from other contract vehicles such as fixed price plus incentive fee, cost plus or time and material contracts. The contractor is not able to claim increases in any rates or costs associated with the contract unless expressly agreed to by the parties at the time the contract is initiated. The risk for increased costs not associated with increased labor or health and welfare rates is solely the responsibility of the NPA. In other words, even if an NPA wanted to pay excessive salaries or bonuses, these costs can not be added to the pricing calculation because of the fixed price nature of the contract.

(4) Should receipt of documentation to support a "rebuttable presumption of reasonableness" serve to demonstrate that executive compensation does not by itself influence a proposed fair market price or any adjustment thereto?

As noted earlier, an annual written statement or declaration, ideally as part of the currently submitted Form 404 Report, signed by the Chair of the NPA Board of Directors and the NPA Chief Executive Officer (CEO)/President certifying that the NPA is maintaining a board of independent members, that the Board of Directors approves compensation arrangements for highly paid executives and individuals using independent comparative salary data gathered from similar organizations for similar executive positions, and documents data used in decision making for compensation packages.

(5) To what extent should there be a relationship between the pay and compensation of line workers and highly compensated individuals?

To the maximum extent possible existing law and regulation including Internal Revenue Service law and regulation, the Service Contract Act, and the Fair Labor Standards Act should govern this process. Federal law and regulation govern the determination of compensation for both line workers and highly compensated individuals. NPAs should be expected to follow the spirit and letter of all applicable laws and regulations regarding the determination of compensation for both line workers and highly compensated individuals with equal vigor so that they can hire and retain the most talented individuals throughout all levels of the enterprise. The JWOD Strategic Plan is clear in its stated objective that improving the quality of jobs and compensation for line workers is a high priority. Any revised rules should increase emphasis on NPA accountability in this area with positive reinforcement including perhaps utilizing incentives.

(6) At what point would be appropriate to begin a review of an executive compensation package even if the proposed price for a product or service would fall within a range that it could be considered as a fair market price?

To the maximum extent possible existing Internal Revenue Service law and regulation should govern this process. A review of an executive compensation package should begin whenever there is an indication of a need. The IRS has procedures for determining compensation for a "highly compensated individual." If they deem that these procedures have not been followed, they can initiate a review and appropriate sanctions. From a Committee perspective, if an NPA either fails to submit a declaration (as noted below) or indicates an inadequate process, the Committee could conduct follow up queries. As explained in detail earlier, the assumption that price is influenced by excessive executive compensation is not the case when examining the facts in a market based system using fixed-priced contracts.

(7) What approaches are available to identity and monitor nonprofit agencies executive compensation that would provide such information to the Committee routinely but without placing an undue burden on agencies?

A written statement or declaration, ideally as part of the currently submitted Form 404 Report, signed by the Chair of the NPA Board of Directors and the NPA Chief Executive Officer (CEO)/President certifying that the NPA is maintaining a board of independent members, that the Board of Directors approves compensation arrangements for highly paid executives and individuals using independent comparative data gathered from similar organizations for similar executive positions, and documents all data used in decision making for compensation packages. As discussed in a previous question, an assessment can be made in percentage terms on the relationship of compensation to overall budget or revenues.

Once again, NISH appreciates having this opportunity to comment on the proposed rule and would like to reserve the right to add further input on these issues in the future. We look forward to working with the Committee and OMB to ensure the continued success of the program in its many roles but most importantly as the largest single employer of people with severe disabilities in the United States.

Supplemental Statement of

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NISH is writing this supplemental statement to the Committee for Purchase From People Who Are Blind or Severely Disabled (the Committee) to express its deep concern regarding the questions, answers, and discussion on the commensurate wage issue as it was discussed during three recently completed hearings on NPA Governance and Executive Compensation. Our concerns regarding this issue can be summarized in these areas:

- The Committee was supplied with inaccurate data by several speakers that were mischaracterized as fact.
- On the surface, paying all JWOD workers with blindness and severe disabilities the “minimum wage” rather than commensurate wage is a desirable outcome, and per the JWOD Strategic Plan, we should consistently be working to increase wages whenever possible; however,
    - Paying all JWOD workers with blindness and severe disabilities the “minimum wage” rather than commensurate wage is complex with far-reaching legal, operational, and personnel impacts.
    - Paying all JWOD workers with disabilities the minimum wage may have a plethora of unintended consequences for the entire JWOD Program, including the federal customer, NPAs, and people with severe disabilities.

Inaccurate Data

Several speakers provided data to the Committee through their oral testimony that contained serious factual errors. It is imperative that the Committee base its upcoming rulemaking on facts rather than anecdote and perception.

One speaker stated that the average wage paid to JWOD Program direct labor workers in 2004 was $4.00 per hour, which is not a fact. The published fact is that the average wage earned by direct labor workers in 2004 was $9.14 per hour.

Another speaker suggested that JWOD Program NPA CEO’s should be allowed by regulation to earn executive compensation at a ratio of no more than 15 to 1 of the lowest paid direct labor worker, similar to the 7 to 1 ratio once employed by the Ben & Jerry’s Ice Cream Company as referenced by the same speaker. However, according to multiple media reports, “the company has grown big enough to bring in professional managers. In order to attract those managers, the company said it had to sacrifice its self-imposed limit on the gap between its lowest and highest compensation rates.” In addition,

> The practices of Vermont ice-cream maker Ben & Jerry's, where the average senior manager earns less than five times as much as the average manufacturing worker, have become something of a quaint anomaly in business. The reason, according to investors and consultants, is that artificial pay caps are unrealistic. "We found the ratio to be rather arbitrary," says Nilloufer Daruwala, senior social research analyst at Calvert. "It just didn't get to the kind of results that we were trying to accomplish." What's more, those seeking top talent won't get it if they constrain earning power to make a point, according to Meyer, the executive consultant. "You're dealing with a market, and you have to pay market value," she says. "When you bring someone in and say, 'Save me,' you have to

> pay them.... While [pay levels] seem unethical or inappropriate, you have to get down to the reality of the situation." [1]

A third speaker stated that people with disabilities could earn $20,000 and retain their disability-related benefits. This statement this is true but only as it applies to some individuals. It is true that some people with disabilities who are SSDI and/or SSI beneficiaries can earn $20,000 or higher and retain their benefits (presumably Medicare and/or Medicaid, but could include many federal, state, and local benefits). This is especially true for blind individuals who are allowed to earn $1,450 a month before reaching the Substantial Gainful Activity (SGA) level, which is nearly twice the $860 a month that is allowed of people with other disabilities. Blind workers also enjoy a richer set of work incentives than people with other disabilities. This is certainly not true of many people with severe disabilities.

Further, the calculation of when people with disabilities reach the amount at which they begin losing benefits varies widely by state, locality, type of earnings, and other factors. This level is, in fact, an individual calculation that requires sophisticated software to determine. NISH strongly urges the Committee to research this issue exhaustedly using tools created by the Employment Support Institute at the Virginia Commonwealth University School of Business before taking any regulatory activities in this area.

Legality of Paying Minimum Wage

There are legislative requirements that make mandating through rulemaking paying all JWOD Program direct labor workers the “minimum wage” problematic. The Service Contract Act defines “minimum wage” to be the monetary wage rates found prevailing in the locality. These wage rates are often higher—sometime much higher—than the current federal minimum wage rate of $5.15 an hour as provided in Section 6(a)(1) of the Fair Labor Standards Act. In some large urban settings these rates are upwards of $30 an hour. A movement in this direction would likely reduce employment for people with severe disabilities. This is counter to the stated strategic plan priorities of the Committee and NISH.

Unintended Consequences of Paying Minimum Wage

The rationale behind paying commensurate wages to people with severe disabilities who have limited productivity is to create an economically feasible method of assisting them to enter the workforce. Artificially increasing their wages to the full minimum wage by rulemaking does nothing to solve the underlying problem. It is treating the symptom but not curing the condition. This will lead to any number of unintended consequences such as NPAs being forced to employ people with severe disabilities who can work at high productivity levels rather than those who have low productivity.

Rather than employ people with severe disabilities with higher productivity some NPAs will leave the JWOD Program. This could mean that some federal customers would not receive the

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[1] Scandal fallout: tougher evaluation of CEO pay, G. Jeffrey MacDonald, March 21, 2005, The Christian Science Monitor

services and products they need. Moreover this may result in many missed jobs for people with severe disabilities.

Paying all people with severe disabilities the minimum wage or higher will have major negative impacts on performance and morale. Workers will soon realize that they may be paid a minimum wage no matter how much they produce. Why should a worker at 80% productivity deliver any additional units than a 40% productivity worker if they will both receive the same pay?

In some societies the government provides *wage support* funds to business to use to supplement the wages of low earning workers. In the US, the government provides *income supports* to individuals with low earnings in the form of Supplemental Security Income (SSI) and Social Security Disability Insurance (SSDI) cash assistance. There is no mechanism that is known to NISH for government to provide wage supports to people with severe disabilities working for either for-profit or non-profit employers.

The best way to increase wages of people with severe disabilities to the full minimum wage is to invest in assistive and rehabilitation technologies that increase their productivity in their current jobs or that moves them into jobs where they can be fully productive.

NISH strongly urges the Committee to limit its anticipated rule making to the issues of NPA Governance and Executive Compensation. This was the purpose of the published intent of the hearings as stated in the Federal Register notice. Discussion of these other issues violates the process in place to properly and fairly evaluate issues. NISH urges the Committee to proceed with great caution. It is recommended that the Committee conduct a detailed study prior to any rulemaking as NISH believes that some actions could negatively impact the employment of people with severe disabilities who are not blind. If at a future time the Committee wishes to consider the issue of commensurate wages paid to JWOD Program direct labor workers NISH would be pleased to provide additional data for that purpose.