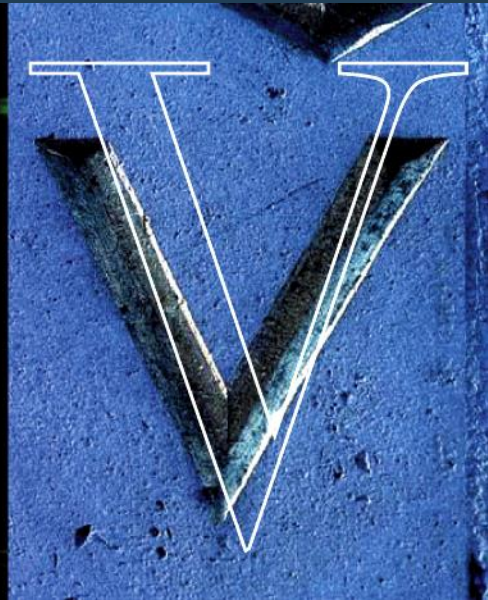
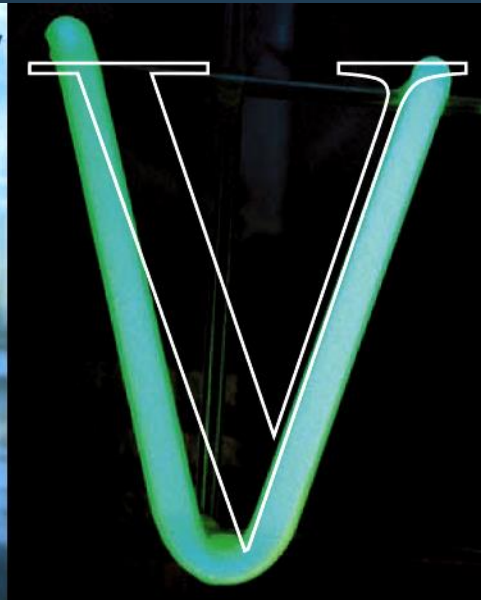
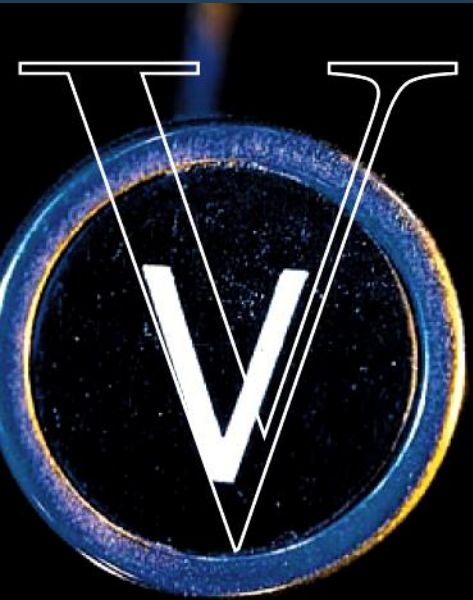


VENABLE<sup>®</sup><sub>LLP</sub>

## Designing Heads' Contracts: Maximizing Compensation and Benefits

Caryn Pass & Harry Atlas  
NAIS 2017 Annual Conference  
March 3, 2017



# Overview

- Heads Retiring in Increasing Numbers
- Baby boomers held on to jobs
- Fewer applicants; more competition
- Contracts different then before
  - New heads are more sophisticated
  - Looking for more benefits
  - Looking for protections should they get terminated



# Term

- Sends message to head
- Give security without extending beyond reasonable period
- Newer heads -- 3 years
- Renewed contracts – 3/5/7
- Evergreen Clauses
  - Benefit vs. Detriment
  - Allows contract to roll over for additional time following end of “term”
  - Time options: Additional year, term of agreement
  - Notice of decision not to “rollover”
    - Timing
    - Prior to end of last year of contract
    - After 2<sup>nd</sup> or 3<sup>rd</sup> year for period to allow for continued same term



# Compensation

- Salary
  - Amount to be paid in 1<sup>st</sup> year of contract
  - Each contract year in term
  
- Increase in salary
  - Determined by Board
  - Not less than “X” %
  - Same as faculty
  - Not less than prior year
  
- Bonus
  - Yearly or discretionary
  - Based on performance or result of “special performance”



## ***403(b) Retirement Plan***

- Most independent schools are subject to nondiscrimination requirements which preclude special treatment of the Head under the 403(b) plan
- Certain types of schools closely related to a church (but not all church-affiliated schools) are exempt from the nondiscrimination requirements and can provide special 403(b) contributions for the Head

*Wise In The  
School World*



## ***Deferred Compensation – IRC Section 457***

- 457(b) Plan
  - Fully vested at all times – a retirement benefit, not a golden handcuff
  - Annual contribution limit (\$18,000 for 2017)
  - Credited interest or participant-directed investment
  - Distribution elections made upon termination of employment with limited ability to change
  - Not eligible for IRA rollover
  - Section 457 is not applicable to certain types of schools closely related to a church



## ***Deferred Compensation – IRC Section 457***

- 457(f) Plan
  - Subject to taxation upon vesting – effective as a golden handcuff, less so as a retirement benefit
  - Can be subject to, or exempt from, IRC Section 409A, depending on whether payment of earnings is deferred beyond vesting date
  - No contribution limits
  - Credited interest or participant-directed investment
  - Distribution provisions must be set when each contribution credit is provided with limited ability to change
  - Not eligible for IRA rollover
  - Section 457 is not applicable to certain types of schools closely related to a church



## Tuition

- Tuition remission for a Head's children is non-taxable only if it meets IRS nondiscrimination requirements
  - Concept similar, but not identical, to the minimum coverage test for retirement plans
- Tuition remission must be *in addition to* salary; cannot be provided on a salary reduction basis
- Remission
  - If same as other employees, non-taxable
  - Greater than other employees: full amount taxable
- Payment of other institution tuition; taxable
  - Independent school or College
  - Amount of tuition of school
- Head executes enrollment document





## ***School Provided Housing***

- To be non-taxable under IRC Section 119(a):
  - School Housing
    - Property on or adjacent to campus
    - Condition of Employment
    - Used for benefit of employer
- “Qualified campus lodging” exemption under IRC Section 119(d) usually not helpful for off-campus housing because it only exempts rental value above 5% of the property’s FMV
- If not exempt, fair market rental value is subject to taxation.
- cleaning service, decorating budget, maintenance and repairs, etc.)
- value is taken into account when determining reasonableness of compensation



## Other Housing Options

- Housing Allowance
  - Taxable income
  - Considered in the intermediate sanctions
  - Preferable to increasing the base salary for optics on 990 and isn't impacted by % increase on base salary
- Loan
  - Careful with regard to amount of loan
    - Reportable on 990, Considered possibly in intermediate sanctions
  - Arms length agreement
    - Written document
    - Market Interest rate, term of payment, collateral
  - Forgiveness of loan issues (question of whether it is truly a loan)
    - Give bonus in year of forgiveness as “payoff of loan”



# Termination

- By Head
  - Notice period by Head
- Mutual
  - Parties agree as to time and transition
- Death or Disability
  - Payment of Salary, COBRA, House
- Expiration of Agreement
- Term for Cause
  - Define cause, Appearance before Board, Ability to cure, Notice in writing
- Without Cause
  - Notice period (6/12/18 months)
  - Execution of release
  - COBRA or other benefit continuation defined



# Severance

- Bona fide severance is exempt from the “tax when vested” rule of IRC Section 457(f)
- Severance can be exempt, in whole or in part, from IRC Section 409A
  - Short-term deferral (payment within 2-1/2 months after year-end)
  - Separation pay (limited amount within limited period)
- Be specific about timing of execution of release of claims relative to beginning of severance payments



## *Extras*

- Car
- Phone, Tablet and Laptop
- Child Care
- Country Club
- Relocation Assistance
  - Moving, house sale, purchase expenses
- Attorney Fees
- Financial Advisor
- Executive Coach
- Accounts
  - Heads discretionary Account, Professional Development, Entertainment and travel
- College Accounts
- Copyright
- Use of Pictures, Videos and images
- Non compete/Non solicitation
- Sabbatical

*Wise In The  
School World*



# *Intermediate Sanctions*

- Obligations
  - Intermediate sanctions impose a 25% excise tax on any “disqualified person” who receives an “excess benefit” from a tax-exempt organization
  - If excess benefit is not repaid or otherwise restored to the school within a certain amount of time, the disqualified person is subject to an additional 200% tax.
  - Any officers, directors, trustees or school managers who knowingly and willingly approve (or fail to vote against) the excess benefit arrangement will also be taxed up to 10% or \$10,000, whichever is less.



# Safe Harbor

- Components
  - No Conflict of interest
    - Decision makers are in compliance with Board Conflict of Interest Policy
  - Comparable Data
    - Information and figures of similarly situated qualified persons taken into consideration
  - Documentation of Basis of Decision
    - Review of documents and maintenance



## ***Comparable Data***

- Factors to consider when selecting schools:
  - Years as Head of the School
  - Total experience as a Head
  - Total Budget of School
  - Grades at School
  - Total Enrollment at School
  - Tuition
  - Faculty numbers
  - Other programs
  - Property
  - New projects or programs; construction, addition of grades





# Venable Independent School Law Practice

*wise in the school world*

[www.Venable.com/education](http://www.Venable.com/education)

@schoollawyer

Caryn Pass

[cpass@venable.com](mailto:cpass@venable.com)

(DC) 202.344.8039

(NY) 212.370.6260

(Cell) 202.222.8026

Harry Atlas

[hatlas@venable.com](mailto:hatlas@venable.com)

(BA) 410.528.2848

(DC) 202.344.8296

Washington, D.C.:

600 Massachusetts Avenue,  
N.W.

Washington, D.C. 20004

Baltimore, MD:

750 East Pratt Street  
Baltimore, MD 21202

New York:

1270 Avenue of the Americas  
New York, NY 10020

*Wise In The  
School World*



the road ahead  
is bright

*Wise In The  
School World*

