Mutual Fund Director Compensation in 2012

By Jay Keeshan and C. Meyrick Payne of Management Practice, Inc.
MPI will participate in a webinar covering this topic with the Mutual Fund Directors Forum on May 14th, 2013.

Management Practice Inc. (MPI) has just completed its 20th annual "Survey of Mutual Fund Director/Trustee Compensation and Governance Practices", with data covering 1,761 directors from 368 fund families. Full reports and specific board compensation comparisons are available from MPI.

Facing a continued increase in industry and regulatory complexity and a 12% increase in assets, mutual fund board pay on average was up only modestly again last year. After rising just 3.2% in 2011, year-over-year (equivalent director) compensation increased an average of 3.4% in 2012 over 2011 levels, from $82,000 to $84,798. Directors at 50 of the largest fund families saw slightly higher increases at 4.9%.

As is often the case, however, the industry-wide percentage changes do not tell the full story. While the majority of boards likely took little or no increase, a smaller group adjusted their pay significantly, sometimes as high as 15%-20% or more. This could be due to several factors, including their pay having fallen well behind their peer group, or having experienced significant changes or restructuring at their fund management company.

Setting director compensation has become more difficult in recent years as the use of AUM as a metric becomes less relevant in the face of a rapidly evolving industry. Factors such as breadth of distribution channels, use of sub-advisors, and complexity of products and investment types have a greater impact on directors' responsibilities and are being taken into consideration more often when selecting comparable peers.

Using AUM as the sole metric can be problematic, as is displayed in the table below. This is the pay range for fund boards with between $1 billion and $7 billion in AUM from 2010 - 2012:

Range of Trustee Compensation for Boards Overseeing $1 billion to $7 billion in AUM (in Percentile)

	10th	25th	50th (median)	75th	90th
2010	$20,000	$37,000	$48,875	$63,719	$81,250
2011	$19,032	$35,000	$50,735	$71,000	$92,400
2012	$12,804	$24,000	$46,000	$64,638	$91,800

For this grouping, the median compensation actually decreased when compared to the previous two years. This is possibly the result of more highly paid directors moving out of the grouping and lower paid directors joining this grouping as their assets increased during the year, which creates a net downward effect on the compensation numbers. Furthermore, the wide range of pay from the 10th to the 90th percentile in any given grouping demonstrates that it can be difficult to properly set pay using just one or even two metrics.

The survey found that approximately 87% of all fund directors are classified as independent, with 70% of boards headed by an independent chairman and an additional 15% headed by a lead independent director. The vast majority of these chairmen (along with many lead independent directors) receive additional fees of anywhere from $10,000 to $200,000 or higher.

Boards continue to adjust their committee structures as the industry and their fund complex evolves. Committee chairs, often hired specifically for a particular background, are receiving a fee more often and at increasing levels.

Roughly two-thirds (68%) of US fund boards continue to be paid with a combination of retainer and meeting fees. While a level of total annual compensation is typically set as a target, this structure allows some flexibility during extenuating circumstances.

The relative cost of fund governance remains a mere fraction of the total costs of running a fund. Total US fund board compensation per $1 million in AUM amounted to just $16.86, compared to the $10,000 in management fees and other expenses a typical mutual fund might incur (assuming a 1% expense ratio). Independent directors provide a highly efficient system of oversight that is paid not by US taxpayers, but rather by those who directly benefit from its protection.

After decreasing 9% last year, the "Total Cost of Governance", which includes the total amount paid to US fund directors, as well as other board expenses such as T&E and legal costs (as reported by NSAR filings), was $369 million, up 26% from last year. This still represents just a fraction of a basis point against the total industry assets.

The survey notes that the mutual fund industry is highly concentrated, with the top 25 complexes controlling about 66% of all fund assets. These 25 complexes have about 252 directors (including cluster boards). On average, each of these large complex directors oversees approximately $34 billion worth of assets, a much wider span of oversight than even directors of NYSE companies.

Our data finds that approximately 17% of all standing fund directors are female, and 36% are retired from their primary profession. The median director age was 66, with the average at 65.

Retirement ages continue to trend upward. 76% of participating boards have a mandatory retirement policy, with the most frequently reported age at 72. However nearly half of boards have retirement ages above 72. "Director Emeritus" plans also continue to draw interest but do not appear to be widely used.

******

Management Practice Inc. is a specialized consulting firm based in Stamford, Connecticut, and provides governance, economic, and business advice to mutual fund boards. More information regarding this report is available at www.MFGovern.com or from C. Meyrick Payne or Jay Keeshan at (203) 973-0535 or email JKeeshan@MFGovern.com.

Management Practice Inc.
216 West Hill Road, Suite 200
Stamford, CT 06902

Telephone (203) 973-0535
Fax: (866) 749-6826
JKeeshan@MFGovern.com