Lower Bonuses Reduce Pay for Higher-Paid CCOs in 2008

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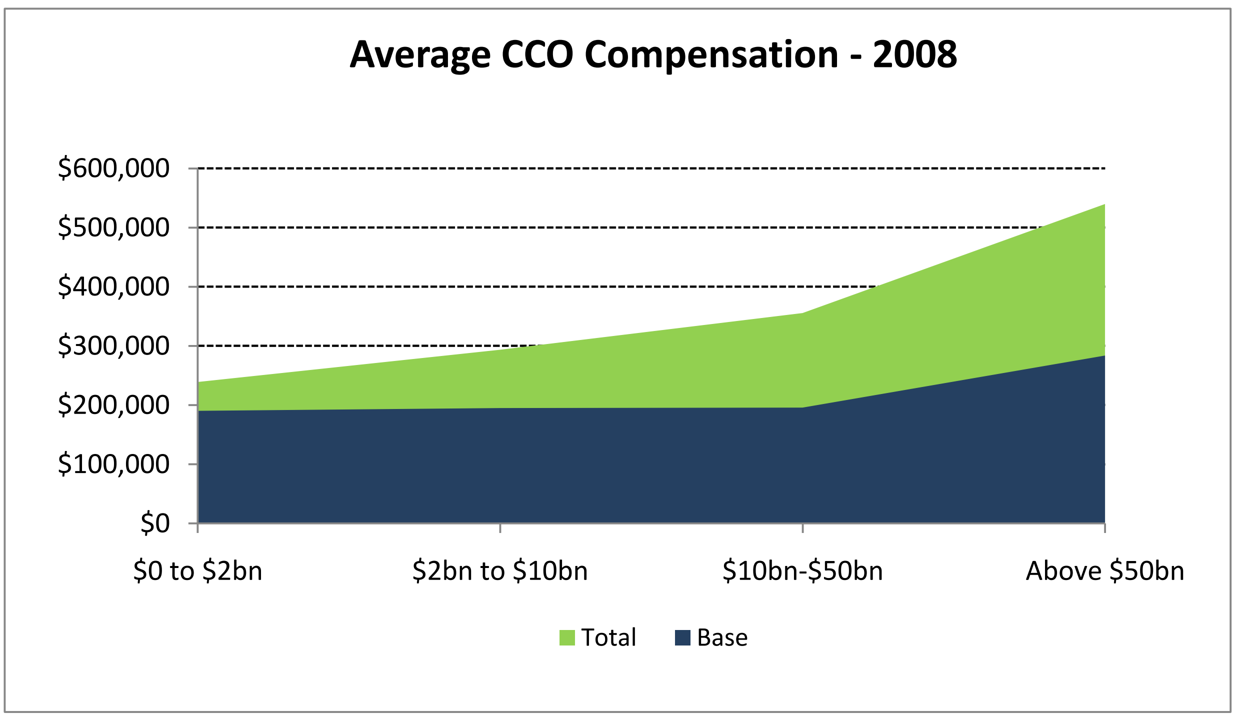
MPI recently completed its fourth annual Survey of Mutual Fund Chief Compliance Officer Compensation and Organizational Practices. This bulletin summarizes the findings and is based on the submissions of 56 fund CCOs, representing funds with $2.3 trillion in assets. 66% of the participants were full-time employees and serve as CCO to both the fund and the advisor.

The majority of mutual fund CCOs saw moderate or no increases in total compensation in 2008 when compared to 2007. The overall picture was on par with expectations that CCOs would not see the large gains seen over the past few years. Based on the 56 participants in the 2009 study (not exactly the same group as in 2008), total CCO compensation on average rose from $336,976 to $349,266, an increase of just 3.6%.

While some CCOs received increases in base salaries (up 7.2%), many others saw their bonuses fall due to the economic crisis in the last quarter of 2008. 92% of CCOs receive a bonus as part of their pay. The effect was greatest was for the highest paid CCOs, some of whom had in recent years seen bonuses as high as 200% of base pay. This year the majority saw a bonus closer to 100%. The higher the bonus as a percentage of total compensation, the more likely it was that they saw their total compensation decrease in 2008.

While not necessarily the most valid driver of total compensation, the below chart plots total compensation against assets under management. We found that CCO compensation increases as size increases, but that economies of scale exist (i.e. a CCO is paid more for the first $1 billion of assets than the second $ billion and so on). We found that the highest paid CCOs approach or exceed $1 million per year and very few are paid less than $150,000.



Bonuses typically range from 25% to 100% percent of base pay, with (as mentioned above) some of the highest-paid CCOs in the past receiving as much as 200% or more. The bonus, which is usually based on how well the CCO completes the pre-agreed compliance plan, often represents a larger portion of compensation at larger fund families. There was a firm expectation among CCOs that the bonus would be paid. But the bonus program has the practical effect of giving the board – and the management company where the CCO has advisor responsibilities – discretion to ensure that the annual compliance plan is achieved.

We emphasize that these projections are inexact. The range of CCO compensation for the reporting fund families was wide and depended on many variables, such as geographic location, number of funds and portfolios, retail or institutional distribution, number of sub-advisors, and mix of insurance related products. We also found that many CCOs had been long term employees of the management company, or had had many years of experience in another fund company. As a result CCO compensation was sometimes correlated with age and experience.

An important finding of our survey was that while CCOs often participate in the advisor's 401(k) plan, they do not typically qualify for the advisor's long term capital accumulation plan. These plans are usually based on restricted share grants or qualified stock options, and are worth, in a good year, 20% to 30% of total compensation for an executive of the typical CCO's salary grade. As a result the CCO's base compensation is typically set 20% to 30% above that of his or her grade's salary range to make up for the loss of a capital accumulation plan. This discrepancy sometimes can cause tension with executives of the management company, and sometimes leads to friction with the fund board, which is responsible for approving the CCO's pay.

As the true costs and benefits of compliance become clearer over time, there is a trend toward splitting the cost of CCO compensation between the funds and the manager. This year 56% of CCOs reported being paid at least in part by the fund, up from 52% last year. We also saw an the emerging pattern of CCOs performing certain compliance functions for other parts of the advisor's business. We found that 78% of the reporting CCOs perform analytical functions directly for the fund board, which might include involvement in the 15(c) contract renewal process or monitoring soft dollar expenditures. Other findings include a reported increase in "Risk Management Support" as an additional duty of the CCO, rising to 62% from 54% in 2007.

Finally, this year 43% of the respondents were lawyers (compared to 34% in 2007) and 25% were CPAs (34% in 2007).

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Any individual CCO's compensation must be evaluated in proportion to the effort, expertise and exposure of that particular complex. CCO compensation, as with any other position, is the result of determining how best to attract, motivate and retain the requisite talent for the specific assignment.

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