Fund Director Compensation Reflects Industry in 2011

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 15th, 2012.

Management Practice Inc. (MPI) has just completed its 19th annual "Survey of Mutual Fund Director/Trustee Compensation and Governance Practices", with data covering 1,833 directors from 343 fund families. Full reports and specific board compensation comparisons are available from MPI.

While experiencing ever-growing challenges and responsibilities, fund directors overall appear to have held their pay to modest increases. Year-over-year (equivalent director) compensation increased an average of 3.2% in 2011 over 2010 levels. Boards at larger fund families saw slightly higher increases of approximately 3.7%.

Directors are adjusting to the "new normal" with regard to workload after the 2008-2009 financial crisis, however the industry continues to evolve and there are numerous ongoing factors that are influencing fund director compensation. While many boards made no changes to their compensation, others made more significant adjustments based on their particular circumstances.

At the "large board" end of the spectrum (the top 50 fund families in terms of AUM) many boards saw increases over the previous year due to mergers or other significant changes in their duties, or because they were long overdue after several years without an adjustment. Fund family merger activity can have the effect of dissolving one board and subsequently boosting the pay (perhaps significantly) of the surviving board.

At the smaller fund end of the spectrum, the industry may be starting to see the effect of the increasing use of administrator-sponsored funds or "funds in a box". These allow new players in the industry to start up a fund without creating their own unique boards, reducing the number of new (and typically very low paid) boards.

Below is a sample of the pay range for fund boards with between $1 billion and $7 billion in AUM:

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

The wide range of pay from the 10th to the 90th percentile in this illustrative grouping demonstrates that it can be difficult to properly set pay using just one or even two metrics. For this reason MPI continues to assess board compensation by looking beyond AUM and the number of funds overseen, taking into account factors such as breadth of distribution channels, use of sub-advisors, and complexity of products and investment types, among others.

The survey found that approximately 87% of all fund directors are classified as independent, with 70% of boards headed by an independent chairman. 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.

Committee chair fees continue to increase, impacting the aggregate compensation for many boards (though not always affecting the median). Chairs for committees such as investments or compliance have been receiving pay similar to or higher than the audit chair in some cases.

Roughly two-thirds 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 board compensation per $1 million in AUM amounted to just $18.01, nearly unnoticeable in comparison to the $10,000 in all 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 the US taxpayer, but rather by those who directly benefit from its protection.

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 $293 million, down 8.5% from last year and representing just a fraction of a basis point against the total industry assets. This decrease may be due to numerous factors, likely including a reversion to “normality” after the greatly increased costs resulting from the economic crisis at the end of the last decade.

The survey notes that the mutual fund industry is highly concentrated, with the top 25 complexes controlling about 74% of all fund assets. These 25 complexes have about 271 directors (including cluster boards). On average, each of these large complex directors oversees approximately $33 billion worth of assets, a much wider span of oversight than even directors of NYSE companies.

Our data finds that approximately 16% of all standing fund directors are female. Retirement policies continue to draw attention, with “director emeritus” programs gaining interest. Retirement ages have been trending upward, but the most frequently reported retirement age remains at 72.

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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.