

# Do ‘Good Governance’ Codes Enhance Financial Accountability? Evidence from Managerial Pay in Dutch Charities

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**Abstract:** This paper examines the initial impact of a ‘good governance’ code for charitable organisations that was promulgated in the Netherlands in 2005. Data are gathered from publicly available annual reports of 138 charities in the post-implementation phase of the code (2005–2008). We first examine whether the code altered charities’ governance structures. Next, we investigate managerial pay as a key aspect of discharging financial accountability because prior literature focused on ‘excessive’ compensation. The findings indicate that a strengthened governance structure positively affects the likelihood of disclosing information concerning managerial pay, as well as mitigating managerial pay level.

**Keywords:** nonprofit sector, charities, governance, codes, managerial pay

## INTRODUCTION

Charitable organisations are facing increased public scrutiny to ensure that they meet the legitimate expectations of their stakeholders. In recent years, numerous cases of charities mismanaging entrusted resources have been documented in the press (e.g., Gettler, 2007; Guardian, 2009; and Independent, 2009). As a result, donors are more sceptical of the charitable sector and closely scrutinise where they put their money in these difficult economic

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times. A key area of debate that remains controversial concerns the way in which charities determine compensation levels for their officers and directors (Aggarwal et al., 2012; Hallock, 2002; Jobome, 2006; and Steinberg, 2010). Charitable organisations are struggling to find the right balance in compensation arrangements. Pay schemes should motivate and fairly reward executives in alignment with the best practices of the labour market while simultaneously complying with stakeholders' expectations. When charities decide to pay excessive compensation, they are diverting money away from the intended organisational purposes and beneficiaries. Unscrupulous pay practices or excessive pay within a charity can taint the public's perception of donating, especially when compensation abuses receive widespread media and public attention (Prakash and Gugerty, 2010).

In response to stakeholders' concerns regarding questionable compensation systems and to encourage self-regulation, charity governance assumes greater prominence. Best practice guidelines have been developed with the explicit aim of enhancing 'good governance' and, among other objectives, curbing excessive executive compensation (e.g., Breen, 2012; ECNL, 2009; Ostrower, 2007; Phillips, 2012; and Szper and Prakash, 2011). Despite these developments, empirical evidence regarding the adoption and effects of 'good governance' guides to increase financial transparency and reduce disputable managerial pay practices has been subject to limited attention in prior research (Helmig et al., 2009; Hyndman and Jones, 2011; Hyndman and McDonnell, 2009; Ostrower and Stone, 2010; and Stone and Ostrower, 2007). This study addresses this gap by investigating the initial impact of a 'good governance' code that was promulgated in the Netherlands in 2005 ('Code Wijffels') by the national accreditation program. We first examine whether the establishment of the code altered the governance structure of Dutch charities. We then assess the impact of a strengthened governance structure for affected organisations on their likelihood of disclosing information about managerial pay and, eventually, mitigating compensation levels. Investigating the executive compensation effects of the code is not only relevant in evaluating whether best practice guidelines or legislative acts achieve their intended objectives but also in informing the broader policy debate on regulatory efforts to improve governance in a nonprofit setting.

The remainder of the paper is structured as follows. We first present a review of prior research and justify the research questions addressed by this study. Next, we briefly illustrate the institutional background of the charity sector in the Netherlands and the 'good governance code' ('Code Wijffels') promulgated in 2005. Next, we describe the sample and the research methodology applied. A section addressing the descriptive statistics, univariate and multivariate analyses is subsequently presented. The concluding section summarises the main findings and implications, discusses the limitations of this study and advances ideas for future research.

## LITERATURE REVIEW AND RESEARCH OBJECTIVES

The effective management of charities is important, not only because of the prominent place of these organisations in national economies but also because of the public nature of the charitable sector (Phillips, 2012; and Prakash and Gugerty, 2010). Charities depend for their survival on public support, which can be in the form of donations, volunteer service, or preferential tax and other legal treatment (Jegers and Lapsley, 2003; and Van Puyvelde et al., 2012). When those entrusted with fiduciary responsibility use charities to advance their own private purposes, the reputation of the charitable sector is broken, which may result in lower individual giving and reduced public support (Steinberg, 2006).

In the last few years, the charity sector has attracted a number of reports and inquiries across the world that ultimately call for enhanced external oversight and intervention. For example, cases of fiduciary wrongdoing in high profile organisations such as the United Way, the Nature Conservancy, and the Red Cross were exposed by media coverage (Christensen, 2004). Consequently, the charitable sector has been increasingly characterised as suffering ‘little accountability’ (Gettler, 2007, p. 5), as an ‘excessive City pay culture’ (Guardian, 2009; and Independent, 2009) and as being in need of improved scrutiny and reporting (Baker Tilly, 2012). It is not an exaggeration that a relatively rare incidence of fiduciary wrongdoing or abuses of a few ‘bad apples’ are beginning to undermine the reputation of the sector as a whole (Prakash and Gugerty, 2010).

These growing concerns have placed a greater focus in contemporary scholarly discussions on the importance of ‘good governance’ practices in the charitable sector (Breen, 2012; Hyndman and Jones, 2011; Hyndman and McDonnell, 2009; Phillips, 2012; Stone and Ostrower, 2007; and Szper and Prakash, 2011). Typical features of ‘good governance’ include the disclosure of measures that provide insight into the effectiveness and efficiency of a charity’s performance and publicly reporting such results for the benefit of key stakeholders (Dellaportas et al., 2012; and Hyndman and McDonnell, 2009). With the proliferation of ‘good governance’ initiatives across different countries (e.g., Breen, 2012; ECNL, 2009; and Ostrower, 2007), Hyndman and McDonnell (2009, p. 27) emphasise that scant empirical evidence is currently available about the impact of such best practice guides or legislative acts. While these initiatives may represent a useful tool for charitable organisations, the extent of adherence to these types of policy recommendations or interventions must still be determined. Moreover, there is a clear paucity of academic research on the consequences of such adherence (Cornforth, 2011; Hyndman and McDonnell, 2009; Hyndman and Jones, 2011; and see Neely, 2011, for a notable exception), therefore raising doubts about the relative merits – or lack thereof – in regulating the charitable sector through the enactment of ‘good governance’ guides.

In this paper, we address the research gap identified by Hyndman and McDonnell (2009, p. 27) and focus on two interrelated issues regarding the

best practices of 'good governance'. First, we investigate whether charitable organisations adhere to recommendations and guidelines promulgated to improve their governance systems. Second, we examine whether the adherence to a 'good governance' code actually impacts a charity's financial accountability. We focus on the disclosure and level of managerial pay, as these have been addressed as key issues in both the academic (Hyndman and McDonnell, 2009) and practitioner (e.g., Baker Tilly, 2012) literature. Next, we provide a review of prior research in these areas and justify the research questions addressed in the empirical analysis.

### *Adoption of 'Good Governance'*

According to extensive literature reviews (Cornforth, 2011; and Stone and Ostrower, 2007), research on nonprofit governance has predominantly focused on board characteristics. These include issues such as the role of the board, the relationship between the board and the management of the organisation, and the composition of the board (Cornforth, 2003 and 2011; and Lambert and Lapsley, 2011). While it must be acknowledged, as Carver (1997, p. 2) contends, that nonprofit boards hold the 'ultimate accountability' for organisational action, recent calls for governance research argue that such research should extend beyond board-focused constructs. There is a need for longitudinal and comparative research designs that not only focus on board characteristics and behaviour but also explicitly examine how 'good governance' structures and practices change over time and are influenced by external and internal contingencies (Brown et al., 2012; and Cornforth, 2011, pp. 13–14).

While the concept of 'good governance' is more an umbrella term with several meanings tailored to the contingencies in which charities operate, financial accountability is frequently considered to be the 'crux of good governance' (Dellaportas et al., 2012; Reheul et al., 2014; and Ritchie and Richardson, 2000, p. 451). Much of the extant charity literature has therefore focused on exploring the discharge of financial accountability by means of the reporting practices and disclosures made by charitable organisations via their annual reports (Crawford et al., 2009; Hyndman and McDonnell, 2009; Lambert and Lapsley, 2011; and Reheul et al., 2014). Several studies examine the developments in reporting practices of charities in the UK (see Connolly and Hyndman, 2004; Connolly et al., 2013; and Hyndman and McDonnell, 2009, for reviews). The findings provide evidence that large charitable organisations have improved their discharge of the most basic levels of accountability following the gradual imposition of the more regulated financial reporting environment of the Statements of Recommended Practices series (Connolly et al., 2013; Crawford et al., 2009; and Hyndman and McMahon, 2010). The diversity of accounting practices and a lack of standardisation still have an impact on compliance levels and accountability to stakeholders and donors.

In their field study conducted among Scottish charities, Crawford et al. (2009) document that the main drivers of change in the governance/accountability processes in the charity sector appear to be regulation and legislation, where charitable organisations adopt evolutionary changes in response to their dynamic environment and to new (legal) requirements. This finding is similar to the for-profit sector. For example, Aguilera and Cuervo-Cazurra (2004) also find that both legislation and changes in the environment are important drivers of the adoption of 'good governance' codes. Furthermore, Crawford et al. (2009) argue that new regulations and legal requirements spread over time, with larger organisations adopting good governance and accountability arrangements more quickly than smaller charities. Although change processes may not be directly transferable across countries, this evidence suggests that changes in governance systems may be adopted more easily by relatively large organisations that already have a rather well-developed governance system relative to smaller organisations that hardly separate decision-making from monitoring activities. Such structural changes are likely to be considered 'evolutionary' relative to smaller organisations that need to make more 'revolutionary' changes to their governance and accountability systems.

Attempts to regulate contentious governance issues in the nonprofit sector provide a rich setting that allows a comparison regarding the impact of governance regulation in the for-profit sector. Empirical evidence from the for-profit sector indicates that a noteworthy number of firms may choose not to comply<sup>1</sup> with governance regulations, even after a significant period of time (Aguilera et al., 2008). For example, Laksmana (2008) documents that voluntary disclosures about managerial compensation increased over time after the SEC made boards more accountable for their decisions regarding compensation practices. Despite this increase in voluntary disclosures on managerial compensation, not all firms fully comply with such regulation; in addition, there is a significant amount of variance in the disclosure of specific compensation-related items. Von Werder et al. (2005) suggest that German companies generally tend to comply with voluntary governance codes requiring, amongst others, the disclosure of executives' compensation schemes. Von Werder et al. (2005) also find that approximately 20% of German companies do not disclose managerial compensation, as it would allow conclusions about the compensation of specific board members, which is viewed as undesirable and unjust. In the nonprofit sector, Reheul et al. (2013) document that 17% of the Belgian organisations in their sample did not file their annual statements within the legal time span.

In summary, past studies suggest that governance initiatives are widespread, yet some organisations decide not to comply with such initiatives for several reasons. As the literature on charities does not provide conclusive evidence on the (voluntary) adoption rate of governance initiatives amongst charities, our first objective is to examine the level of adherence to a 'good governance code'. We therefore empirically investigate the level of adoption following the

enactment of a self-regulatory policy in the Dutch charitable sector by addressing the following research question:

RQ1: What is the adoption rate over time of a (voluntary) 'good governance' code in charitable organisations?

While addressing RQ1 provides insights into the *adoption* of governance practices, investigating the *efficacy* of those practices remains crucial to evaluating whether regulatory reform efforts to improve governance mechanisms have achieved their intended objectives. Two key governance effects with regard to accountability and executive compensation are examined: a) disclosing executive compensation arrangements to stakeholders and b) determining the level of managerial pay by the board. Next, we provide a review of the literature and justify the other two research questions addressed in this paper, namely addressing the effects of 'good governance' adoption on managerial pay disclosure (RQ2) and managerial pay levels (RQ3).

#### *Effects of 'Good Governance' Adoption on Managerial Pay Disclosure*

In assessing the impact of governance regulation in the nonprofit sector, a major issue examined in the extant literature pertains to executive compensation (Caers et al., 2006; Jegers, 2009; and Steinberg, 2010). Two reasons justify this focus. From a practical point of view, 'excessive' executive compensation in nonprofits has long been a source of concern (Baker Tilly, 2012). As briefly illustrated above, compensation abuse in charities is not a small problem and should not be overlooked. While guidelines to determine reasonable compensation in the sector are being developed and implemented, there is a clear paucity of research examining whether recent policy initiatives in this area have resulted in desirable effects (see Neely, 2011, for a notable exception). Hence, an investigation of executive compensation effects is of particular relevance in any evaluation of governance intervention.

From a theoretical point of view, the charitable sector provides a powerful setting to examine governance theories that are predominantly applied in the for-profit sector. Accountability to donors can be described as a common principal-agent problem, where a set of donors employs an organisation to aggregate their donations and produce something to beneficiaries they all care about (Steinberg, 2010; and Szper and Prakash, 2011). In this setting, agency problems arise if the quality or quantity of that product diverges from donor expectations. In particular, the absence of intense monitoring by a residual claimant and the presence of multiple principals with different objectives provide managers in nonprofit organisations a greater opportunity to expropriate the firm's assets and engage in opportunistic behaviour (Calabrese, 2011; Jegers, 2009 and 2013; and Szper and Prakash, 2011). This, in turn, tests the ability of the principal-agent framework to resolve questions of accountability, although

the assumptions behind agency theory may not apply in a nonprofit context (Caers et al., 2006; and Van Puyvelde et al., 2012).

Agency theory posits that the amount of time allocated to and the resource commitment of directors to perform their tasks is positively associated with the extent of compensation practice disclosure. Empirical analyses from the for-profit sector are largely consistent with this disclosure argument. For example, Laksmana (2008) provides evidence that more independent boards disclose more information about executive compensation practices. Nevertheless, prior research indicates that the principal-agent paradigm may not provide a sufficient explanation of disclosure and compensation practices in the nonprofit sector (Callen et al., 2010; Dhanani and Connolly, 2012; Hyndman and McDonnell, 2009; Jobome, 2006; and Van Puyvelde et al., 2012). Empirical evidence from charitable organisations is inconclusive and is based solely on data from US charities. Ostrower and Stone (2010) suggest that charities in which the decision making and monitoring board functions are not separated (i.e., charities with one-tier boards) face lower accountability. However, Ostrower and Stone (2010) do not include the disclosure of managerial pay (one aspect of accountability) in their empirical analyses. Neely (2011) examines the regulatory effects of the Nonprofit Integrity Act (NIA) enacted in 2004 in a sample of charitable organisations in California. Comparing the data in the year immediately before and after the passage of the Act, Neely (2011) documents a limited improvement in charities' accountability (proxied by financial reporting quality) in the period following the NIA implementation.

To the authors' knowledge, no studies have empirically investigated whether 'good governance practices' are associated with enhanced managerial pay disclosure (a measure of accountability) in European-based charities. To shed light on this issue, we explore the link between expected increase in charities' accountability (specifically: managerial pay disclosure) *vis-à-vis* governance regulation by addressing the following research question:

RQ2: Is the (voluntary) adoption of a 'good governance' code associated with increased managerial pay disclosure?

Next, we provide insights into the relation between governance characteristics and managerial pay level, drawing upon a consolidated stream of studies on 'excessive' executive compensation in the accounting literature.

### *Effects of 'Good Governance' Adoption on Managerial Pay Level*

Agency theory predicts that 'good governance' increases the pay-for-performance sensitivity of CEO compensation, thereby reinforcing the use of managerial pay as a powerful incentive device (Core et al., 1999). In line with this argument, empirical evidence from US charities (e.g., Aggarwal et al., 2012; and Baber et al., 2002) suggests that managerial compensation is significantly

tied to nonprofit performance measured by program spending ratios and fundraising activities. Hallock (2002) finds that the greater the number of paid board members, the lower the CEO's compensation, therefore supporting the intuition from agency theory that paid board members are effective monitors. Alternatively, it could also be posited that paid board members take on some tasks normally assigned to management, with the result that organisations with paid boards can employ a less skilful manager and pay him less.

Relying upon another argument, Jobome (2006) posits that managerial incentives may be less relevant to CEO's of charities because intrinsic motivation may be more important, hence pointing to stewardship theory as a suitable alternative theoretical framework in the nonprofit sector (see also Van Puyvelde et al., 2012). In this case, structural governance arrangements may not affect managerial compensation. Stewardship theory assumes that relations amongst organisational members (including the relation between the supervisory board and the CEO) are based on mutual trust (Jobome, 2006). In addition, stewardship theory suggests that CEO's may be intrinsically motivated, may focus on self-actualisation rather than bonus optimisation, and may have high value commitment and a long-term orientation. The net result is that stewardship theory posits that supervision structures may be less formal and less focused on monitoring relative to agency theory predictions and that pay-for-performance sensitivity will be relatively low. Consistent with this reasoning, Jobome (2006) finds no empirical relation between three governance measures (whether the board has audit, nomination, and remuneration subcommittees; board size; and whether the organisation's members participate in the board) and managerial compensation levels in large UK charities.

In summary, no single theory seems to explain the contradictory findings from the extant literature on managerial pay. What is currently missing (with the notable exception of Neely, 2011) is research that documents the ability of governance regulation and policy interventions to curb excessive compensation through imposing or suggesting certain restrictions on pay levels. While there is evidence that the promulgation of the Sarbanes-Oxley Act has led to changes in the executive compensation mix in the for-profit sector (namely, from incentive compensation towards fixed salaries; see Cohen et al., 2007), the efficacy of governance interventions in this area has yet to be documented in the nonprofit sector. We expect that in the presence of excessive compensation and an effective implementation of compensation review requirements the adoption of a strengthened governance structure would show a decrease in executive compensation (Calabrese, 2011). The third research question explored in our study is thus stated as follows:

**RQ3:** Is the (voluntary) adoption of a 'good governance' code associated with lower managerial pay levels?



## INSTITUTIONAL CONTEXT

*The Charity Sector in the Netherlands*

Our empirical study is conducted in the Netherlands. According to the Dutch Central Fundraising Agency (CBF), the charitable sector in the Netherlands has an established philanthropic tradition in which approximately 95% of the public donate for charitable purposes. In 2009, the 806 registered charities achieved a historical high of €3.6 billion in revenues. Approximately €1.3 billion was received by means of the organisations' own fundraising activities, whereas the other €2.3 billion was collected by means of subsidies, third-party campaigns and revenue from their own investments (e.g., interest received). Ultimately, approximately €3.0 billion of these funds were used for charitable purposes. Most funds were allocated international aid (38%) and the social sector (34%), whereas 15% were directed to nature and the environment and only 13% to health care purposes (CBF, 2010). To qualify as a charity, the CBF uses the following definition: 'A foundation or association operating with full legal rights under the Dutch law that acquires funds from the public to achieve charitable, cultural, scientific or other goals that relate to public welfare. The acquired funds are provided on a voluntary basis, do not provide a (proportional) exchange for goods or services, and do not provide any rights relating to health care or other help' (CBF, 2012). In addition to the CBF definition, a charity has to meet a number of requirements from the Dutch tax authority to qualify for tax benefits.

Charities in the Netherlands have certain characteristics that differ from those of for-profit and other public sector organisations (such as hospitals, municipalities, or housing corporations). These characteristics have an impact on the governance characteristics of these organisations (Code Wijffels, 2005). First, charities have external goals and objectives; they intend to help societal issues or fulfil societal needs. Second, a large percentage of the funds is obtained through donors, government and lotteries. These stakeholders expect that the available funds are spent to achieve a charity's purposes. Contrary to government and lottery organisations, individual donors do not have the instruments to monitor how funds are being spent. The decision-making rights of the individual donor are usually limited to the choice whether to donate to individual charities and how much money should be donated. Some charities have a general meeting of charity members where individual members can exert influence.

Volunteers play an important role within the organisation, either in operations (i.e., acquiring funds) or in a supervisory role (as members of the supervisory board). Finally, neither the individual donors nor the beneficiaries of the organisations have substantial influence on the decisions made within the charity; rather, they depend upon the decision-makers within the organisation (i.e., the board of directors and the supervisory board). Similar to other for-profit and nonprofit organisations in the Netherlands, Dutch charities operate under a 'two tier' board structure in which the board of directors and the

supervisory board<sup>2</sup> are legally separated. The board of directors is charged with daily management. The supervisory board supervises the board of directors from a distance and controls the followed strategy. Relative to the Anglo-Saxon structure ('one-tier' board), the supervisory board of Dutch charities is less involved in developing and implementing the charity's policy but instead focuses on monitoring and fundraising (Code Wijffels, 2005).

### *Development of the 'Good Governance' Code in the Netherlands*

In the last decade, several cases of Dutch charities with questionable compensation policies and alleged fraud have attracted media attention. For instance, Plan Nederland experienced a substantial comedown when the salary of the interim manager and the non-existent charity's beneficiaries were the object of a media campaign (Algemeen Dagblad, 2002). The charity Nederlandse Hartstichting received harsh criticism from the general public, donors and volunteers regarding the high salary of their medical director (Volkskrant, 2004). Among the initiatives taken to restore trust, a commission was initiated by the Foundation for Fundraising Institutions (VFI) in 2004 to develop a code (Code Wijffels, 2005) that advises charitable organisations on their governance arrangements. The VFI represents more than 120 (mostly large) charities in the Netherlands. Its main tasks are lobbying for charities, self-regulation of the sector, and provision of services to charities.

Code Wijffels was promulgated in 2005 and has the objective of establishing and implementing forms of 'good governance' so that stakeholders have the opportunity to form an opinion about the management quality in charitable organisations. Among the key requirements of the Code are that charities provide information on the organisational structure (separation of duties), the composition of board and supervisory bodies, the level and composition of executive compensation, the allocation and effectiveness of funds, and strategies for fund raising. Members of the VFI are expected to either adhere to this code or explain why it was not adhered to ('comply or explain'). Monitoring whether charities adhere to the code is delegated to the CBF. Non-adherence to the code may result in cancelling the charity's membership in the VFI, thus losing the CBF quality mark. The CBF quality mark signals to the public (donors, government, other stakeholders) that the strategy, quality of management, acquisition and allocation of funds, and accountability of the charity (including the annual report) are considered reliable. However, neither the VFI membership nor the CBF quality mark are legally required to operate as a charity in the Netherlands.

Code Wijffels recommends that charities separate decision making tasks from supervising and monitoring tasks. Four types of board structures have been envisaged. Three structures (labelled 'Board models', or Types I-III) do not use independent oversight. One structure (labelled 'Oversight Model', or Type IV)

uses independent supervision by a separate supervisory board. Thus, Type IV represents a 'full' two-tier governance structure. Code Wijffels states that larger organisations *must* and smaller organisations *can* have different bodies for the supervising and managing function. In this code, a large organisation is defined as an organisation with either 15 FTEs or €2.5 million in revenues per year. Type IV of Code Wijffels thus seems most desirable, as the decision making and monitoring functions are assigned to different bodies.

With regard to managerial pay practices, societal turmoil about (perceived) abuses and excessive compensation led to a separate guideline in Code Wijffels on how to determine an appropriate pay level (based on the method developed by the consultancy firm Hay, adapted to the charity sector). An annex to the guideline document proposed a maximum salary for executives in 2009 of €154,172 (VFI, 2011), which is equal to the maximum salary of a central government official. Executive compensation in charities that use the 'Oversight Model' (Type IV) is mainly the responsibility of the supervisory board. Based on four criteria (organisational size, complexity of the organisation, organisational context, and type of governance structure), each charity can determine what level of managerial compensation is acceptable (Code Wijffels, 2005).

## RESEARCH METHODOLOGY

### *Data and Sample Selection*

Following previous studies in the area (e.g., Aggarwal et al., 2012; and Jobome, 2006), we empirically investigate the three research questions stated above by applying a quantitative approach. The analysis is performed using data from publicly available sources (i.e., hand-collected data from annual reports) regarding Dutch charities. Publishing a financial statement is not mandatory for all charities in the Netherlands; as a result, not all charities provide annual reports. Starting with all the organisations listed by the Dutch Central Fundraising Agency (CBF), we filtered the CBF database to include charities that publish financial data in an annual report. If an annual report was not directly downloadable from the CBF website (which acts as a national repository of reports), a search on the charity website was performed or a direct request was forwarded to obtain a copy of the charity's financial statement. The sample selection process is shown in Table 1.

Our final sample holds a total of 516 organisation-year observations from 138 unique organisations.<sup>3</sup> The data on these charities were gathered for 2005 (the year in which Code Wijffels was promulgated) to 2008. Compared with the total number of charities in the Netherlands, our sample is biased towards charities of a larger size and covers approximately half the CBF population in each of the four years examined. The sample, therefore, is largely representative of the population of charitable organisations in the Netherlands.

**Table 1**  
Sample Selection

	2005	2006	2007	2008
Initial sample (CBF accredited charities)	237	245	260	282
Charities with split financial years	9	9	9	10
Charities' branches	10	10	10	11
Annual reports not available	92	92	101	123
Final sample (total N = 516)	116 (49%)	124 (51%)	138 (53%)	138 (49%)

### *Variables and Regression Model Specifications*

To address RQ1, we present descriptive statistics depicting the trend of diffusion of governance structures and compensation levels across the initial years following the 'good governance' code establishment. Based on information from the annual reports, we classify an organisation in one of four different types of governance structures over the years in our analysis (Type I to Type IV). We use this information to examine the adoption of governance structures over time following the adoption of Code Wijffels.

Consistent with previous literature in this area (e.g., Aggarwal et al., 2012; Callen et al., 2010; Jobome, 2006; and Szper and Prakash, 2011), we use regression analyses to test RQ2 and RQ3. Our dependent variable for RQ2 is the disclosure of managerial compensation by charities in the annual report (DCOMP), where DCOMP is equal to one if managerial compensation is disclosed in the annual report, and zero otherwise. Our key independent variable is governance structure, labelled DGSTRUCT, which ranges from 1 to 4 for Type I to Type IV governance structures, respectively. In additional regressions, we include dummy variables for governance structures (DGSTR3 = 1 when a governance structure is of Type III, and 0 otherwise; and DGSTR4 = 1 for a governance structure of Type IV, and 0 otherwise) to test for the individual effects of specific governance structures. The interpretation of the regression coefficients for DGSTRUCT, namely, DGSTR3 and DGSTR4, is as follows. A significant positive (negative) coefficient for DGSTRUCT suggests that higher governance structures result in more (less) disclosure of managerial pay with respectively higher (lower) managerial compensation. A significant positive (negative) coefficient for DGSTR3 or DGSTR4 suggests that, relative to other governance structures, a specific structure results in more (less) disclosure of managerial pay with higher (lower) managerial compensation.

In running the regressions, we control for several factors that can plausibly influence managerial pay disclosure and managerial compensation. We control for board characteristics (board size, number of board meetings) and audit firm characteristics because they may affect the accountability of charities (Aggarwal et al., 2012; Callen et al., 2010; Hyndman and McDonnell, 2009;

and Ostrower and Stone, 2010 and 2007). We include operational performance measures (administrative efficiency, fundraising efficiency ratio and program expenditure ratio) because they affect accountability decisions (Reheul et al., 2013) and managerial compensation (Baber et al., 2002; Callen et al., 2010; Jacobs and Marudas, 2009; and Jobome, 2006). We include size as a control variable as a proxy for the external visibility of the charity (which, in turn, should increase disclosures) as well as for organisational complexity (which can be expected to increase managerial pay).

Furthermore, we control for institutional donor dependency as a control variable, as dependence on institutional donors is likely to be associated with more intense monitoring; whether this results in increased disclosure and reduced managerial compensation, is an empirical question. On the one hand, institutional donor dependency may result in pressure to comply with regulations, resulting in more disclosure and lower pay. On the other hand, institutional donors may already have information about managerial compensation through other sources than the annual report, resulting in lower disclosure. Age (number of years that have passed since the establishment of the charity) is included because older organisations have a track record and may have superior (financial or non-financial) performance (Szper and Prakash, 2011). We use dummy variables for different sectors in which the charity operates because both disclosure and managerial pay practices may be affected by the activities of the charity.

Finally, governance and accountability practices may vary because international organisations may have to comply with 'parent organisation governance practices' (Szper and Prakash, 2011). We use a dummy variable to indicate whether the charity has an international parent. We additionally include dummy variables for the years 2005, 2006 and 2007 to control for time effects. A list of definitions for both the dependent and independent variables, as well as the hypothesised effect of the independent variables on the dependent variables, is presented in Table 2.

In summary, we test RQ2 by estimating the following logistic regression,<sup>4</sup> which predicts the disclosure of managerial compensation (DCOMP) in our sample:

$$\begin{aligned} \text{DCOMP}_{i,t} = & b_0 + b_1 \text{DGSTRUCT}_{i,t} + b_2 \text{DGSTR3}_{i,t} + b_3 \text{DGSTR4}_{i,t} \\ & + b_4 \text{LGBDSIZE}_{i,t} + b_5 \text{LGBDFREQ}_{i,t} + b_6 \text{AUDITOR}_{i,t} \\ & + b_7 \text{ADMEFF}_{i,t} + b_8 \text{FUNDRAIS}_{i,t} + b_9 \text{PROGSPEND}_{i,t} \\ & + \sum b_n \text{CONTROLS}_{i,t} + u_{i,t}. \end{aligned} \quad (1)$$

Finally, by restricting our analysis to the sub-sample of charities that disclose managerial pay, our aim is to examine whether the same set of predictors explains the level of compensation.<sup>5</sup> The equation to test RQ3 is thus similar to the logistic regression previously illustrated, with the only difference that

**Table 2**  
Variables

<i>Variable</i>	<i>Definition</i>	<i>Expected Effect (RQ2, RQ3)</i>
<b>Dependent:</b>		
DCOMP <sub><i>i,t</i></sub>	Disclosure of managerial compensation (1 = disclosure; 0 = lack of disclosure)	
COMP_FT <sub><i>i,t</i></sub>	Actual level of manager compensation standardised by the number of hours that the manager works (FTE in €)	
<b>Independent:</b>		
DGSTRUCT <sub><i>i,t</i></sub>	Governance structure (ranging from one to four for Type I to Type IV governance structures, respectively)	+,-
DGSTR3 <sub><i>i,t</i></sub>	Governance structure (1 = governance structure Type III; 0 = other governance structures)	?,?
DGSTR4 <sub><i>i,t</i></sub>	Governance structure (1 = governance structure Type IV; 0 = other governance structures)	+,-
LGBDSIZE <sub><i>i,t</i></sub>	Natural logarithm of board size (number of officers in the board)	-,-,+
LGBDFREQ <sub><i>i,t</i></sub>	Natural logarithm of number of board meetings during one year	+,-
<b>Control:</b>		
AUDITOR <sub><i>i,t</i></sub>	Auditing firm (1 = non-Big-4 firm, 0 = Big-4 firm)	-,-,+
ADMEFF <sub><i>i,t</i></sub>	Administrative efficiency ratio: administrative expenses / total expenses	-,-
FUNDRAIS <sub><i>i,t</i></sub>	Fundraising efficiency ratio: fundraising expenses / fundraising revenues	-,-
PROGSPEND <sub><i>i,t</i></sub>	Program expenditure ratio: program expenses / total revenues	+,+
SIZE (mln €)	Organisational size: natural logarithm of fundraising revenues	+,+
INSTT	Institutional donor dependency: institutional donations/fundraising revenues	?,?
AGE (years)	Age of the organisation: natural logarithm of the number of years that passed since a charity was established	+,+
HEALTH	Health care sector dummy (1 = health care; 0 = other)	?,?
INT_AID	International aid sector dummy (1 = international aid; 0 = other)	?,?
SOCIAL	Social welfare sector dummy (1 = social welfare; 0 = other)	?,?
NATURE	Nature and environment sector dummy (1 = nature and environment; 0 = other)	?,?
INTER	Charity has an international parent (1 = international parent; 0 = other)	?,?

the dependent variable in RQ3 measures the level of managerial compensation among the organisations that disclose this type of information in their annual report:

$$\begin{aligned} \text{COMP\_FT}_{i,t} = & b_0 + b_1 \text{DGSTRUCT}_{i,t} + b_2 \text{DGSTR3}_{i,t} + b_3 \text{DGSTR4}_{i,t} \\ & + b_4 \text{LGBD SIZE}_{i,t} + b_5 \text{LGBDFREQ}_{i,t} + b_6 \text{AUDITOR}_{i,t} \\ & + b_7 \text{ADMEFF}_{i,t} + b_8 \text{FUNDRAIS}_{i,t} + b_9 \text{PROGSPEND}_{i,t} \\ & + \sum b_n \text{CONTROLS}_{i,t} + u_{i,t}. \end{aligned} \quad (2)$$

Descriptive statistics and regression results are presented next. We additionally develop and test a series of alternative regression models in which the specification of the two equations stated above slightly changes to evaluate the robustness of our findings.

### EMPIRICAL RESULTS

#### *Descriptive Statistics*

The descriptive statistics of our sample are shown in Table 3. Our data indicate that, on average, about 80% of the charities in our sample disclose information

**Table 3**  
Descriptive Statistics

	<i>N</i>	<i>Min.</i>	<i>Max.</i>	<i>Mean</i>	<i>Std. Dev.</i>
DCOMP	516	0.00	1.00	0.81	0.39
COMP_FT (thousand €)	382	23.51	199.00	95.36	29.99
DGSTRUCT	516	0.00	1.00	3.19	0.59
DGSTR3	516	0.00	1.00	0.66	0.48
DGSTR4	516	0.00	1.00	0.27	0.45
BDSIZE	516	3.00	35.00	7.48	3.14
BDFREQ	427	1.00	13.00	5.16	2.01
AUDITOR	516	0.00	1.00	0.65	0.48
ADMEFF	516	0.00	0.89	0.10	0.10
FUNDRAIS	496	0.00	0.86	0.16	0.10
PROGSPEND	516	-1.02	2.65	0.90	0.26
SIZE (mln €)	516	0.21	239.00	15.75	33.67
INSTIT	516	0.00	0.94	0.18	0.25
AGE (years)	516	1.00	194.00	44.10	35.71
HEALTH	516	0.00	1.00	0.23	0.42
INT_AID	516	0.00	1.00	0.37	0.48
SOCIAL	516	0.00	1.00	0.23	0.42
NATURE	516	0.00	1.00	0.17	0.37
INTER	516	0.00	1.00	0.23	0.42

*Note:*

Refer to Table 2 for a definition of the variables.

on managerial pay in the period examined. On average, managerial pay is approximately €95,000 (based on a full-time position). About 4% of the charities in our sample compensate their officers more than the norms set by the VFI. Approximately 27% of the organisations have an independent supervisory board, as recommended by the VFI (which reflects Type IV of Code Wijffels). Charities have, on average, roughly €16 million in annual revenues, with a base exceeding 100,000 donors. Approximately 18% of the revenues originate from institutional donors. All sectors (HEALTH, health care sector; INT\_AID, international aid sector; SOCIAL, social welfare sector; and NATURE, nature and environment sector) are represented in our sample. Most of the charities in our sample (37%) belong to the international aid sector (INT\_AID). Finally, 23% of the organisations belong to an international parent.

The correlation matrix of the variables in our sample is presented in Table 4. Our data indicate that disclosure of managerial pay (DCOMP) is positively and significantly correlated with governance structure (DGSTRUCT) and Type IV structure (DGSTR4), suggesting – as expected – that charities adopting a better governance structure are also relatively more likely to be financially accountable. In contrast, the Type III structure (DGSTR3) is negatively and significantly correlated with DCOMP, therefore implying a relatively lower propensity to disclose for this type of governance framework. No significant correlation is found among DCOMP and board characteristics. It also appears that ADMEFF is negatively associated with DCOMP, indicating that charities reluctant to disclose information about managerial pay show relatively lower levels of performance. Furthermore, DCOMP is positively and significantly correlated with the charity's size and the international aid sector.

The managerial pay level (COMP\_FT) is positively and significantly associated with governance structure (DGSTRUCT) and Type IV structure (DGSTR4), but not with DGSTR3, for which the correlation is negative and significant. Furthermore, there is a positive and significant correlation with board size and non-Big-4 auditing firms, while no significant relationship is found with organisational performance (except for ADMINEFF). COMP\_FT is positively and significantly associated with a charity's size and age and charities operating in the health care sector.

#### *Adoption Rate of the 'Good Governance' Code*

From the rate of adoption of the governance structure types following the implementation of Code Wijffels in 2005 (see Figure 1), there is an evident increase in the number of charities with the Type IV structure (from 17 organisations in 2005 to 51 in 2008). We also observe a decreasing trend of charities opting for a Type III governance structure (from 92 organisations in 2005 to 78 organisations in 2008). Additional analysis (non-tabulated) indicates that the increase in Type IV structure charities is due to organisations 'moving up' from Type III. Few organisations 'migrate' from a Type I or Type II structure



**Table 4**  
Correlation Matrix

<i>I.</i>	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.	16.	17.	18.
1.	1.000																
2.	0.928**	1.000															
3.	0.219**	0.263**	1.000														
4.	-0.169**	-0.241**	0.842**	1.000													
5.	0.215**	0.256**	0.842**	-0.846**	1.000												
6.	0.004	0.200**	-0.049	0.029	-0.053	1.000											
7.	0.062	0.029	0.013	0.144**	-0.080	0.013	1.000										
8.	0.070	0.312**	0.229**	-0.027	0.164**	-0.061	0.169**	1.000									
9.	0.005	0.068	0.150**	0.001	0.087	-0.141**	0.015	0.013	1.000								
10.	-0.065	0.003	0.028	0.034	-0.003	-0.025	-0.010	0.013	-0.212**	1.000							
11.	-0.100*	-0.187**	-0.051	0.113*	-0.099*	-0.053	0.031	0.011	0.059	-0.078	1.000						
12.	-0.020	0.055	0.198**	-0.086	0.174**	0.211**	-0.001	-0.046	-0.004	-0.068	-0.126**	1.000					
13.	0.168**	0.634**	0.374**	-0.138	0.302**	0.251**	0.290**	0.295**	0.028	-0.023	-0.305**	0.356*	1.000				
14.	-0.019	0.200**	0.063	0.013	0.024	0.215**	0.184**	0.053	-0.014	0.031	-0.041	-0.031	0.229**	1.000			
15.	0.109*	-0.208*	-0.003	-0.036	-0.070	-0.002	-0.032	-0.002	-0.134**	0.064	-0.120**	0.245**	-0.106*	0.106*	1.000		
16.	0.021	0.263**	0.110*	-0.014	0.082	-0.144**	-0.090	-0.055	0.145**	-0.030	0.050	-0.291**	0.109*	-0.420**	-0.420**	1.000	
17.	-0.067	-0.054	-0.00	-0.070	0.053	0.023	0.084	-0.137**	0.029	0.021	0.048	0.104*	0.003	-0.340**	-0.245**	1.000	
18.	-0.086	0.020	-0.099**	0.095*	-0.125**	0.126**	0.052	0.067	-0.018	-0.062	0.045	-0.080	-0.009	-0.422**	-0.218**	-0.246**	1.000
19.	0.079	0.035	0.031	0.066	-0.023	0.053	-0.049	-0.009	-0.040	0.033	-0.044	-0.001	-0.054	0.160**	0.152**	0.080	-0.051

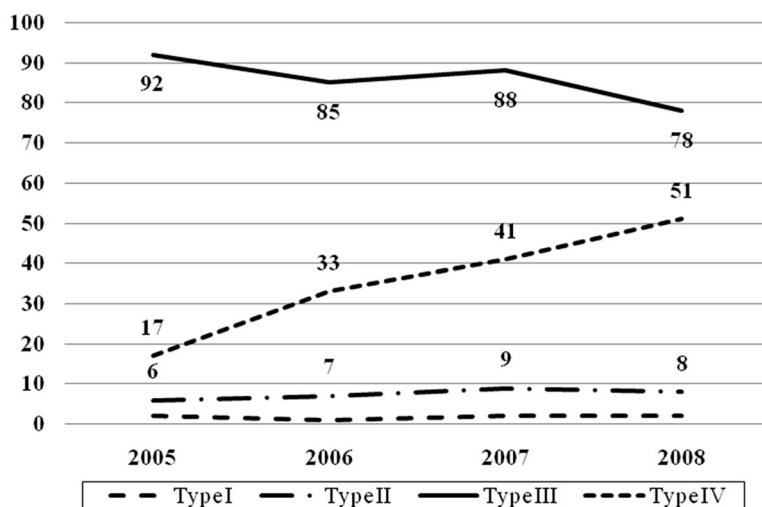
**Table 4** (Continued)

<i>Notes:</i>	
**, *, significant at the 1% and 5% levels (two-tailed), respectively.	
1. DCOMP	Disclosure of managerial compensation (1 = disclosure; 0 = lack of disclosure)
2. COMP_FT	Actual level of manager compensation standardised by the number of hours the manager works (FTE in €)
3. DGSTRUCT	Governance structure (ranging from one to four for Type I to Type IV governance structures, respectively)
4. DGSTR3	Governance structure (1 = governance structure Type III; 0 = other governance structures)
5. DGSTR4	Governance structure (1 = governance structure Type IV; 0 = other governance structures)
6. LGBDSIZE	Natural logarithm of board size (number of officers in the board)
7. LGBDFREQ	Natural logarithm of number of board meetings per year
8. AUDITOR	Auditing firm (1 = non-Big-4 firm; 0 = Big-4 firm)
9. FUNDRAIS	Fundraising efficiency ratio: fundraising expenses/fundraising revenues
10. PROGSPEND	Program expenditure ratio: program expenses/total revenues
11. ADMEFF	Administrative efficiency ratio: administrative expenses /total expenses
12. INSTIT	Institutional donor dependency (in €); institutional donations/ fundraising revenues
13. LNSIZE	Natural logarithm of organisation size (fundraising revenues in €)
14. LNAGE	Natural logarithm of organisational age (in years)
15. INT_AID	International aid charity (dummy)
16. HEALTH	Health care charity (dummy)
17. NATURE	Nature/environmental charity (dummy)
18. SOCIAL	Social welfare charity (dummy)
19. INTER	International parent: 0 (no international parent), 1 (international parent)

to Type IV, suggesting that the adoption of governance structures is evolutionary rather than revolutionary. Our sample shows no change for charities with Type I and Type II structures.

From the mean value of the main variables capturing financial accountability exhibited in Table 5, it appears that disclosure of managerial pay increased significantly from 67% in 2005 to 97% in 2008, suggesting an increased

**Figure 1**  
Adoption of Governance Structures (2005–2008)



*Note:*

The graph shows the trend of adoption of the four governance structure types following the implementation of the 'good governance' code (Code Wijffels) among our sample of charitable organisations.

**Table 5**  
Mean Values of Managerial Pay and Organisational Performance  
(2005–2008)

	2005	2006	2007	2008
DCOMP	0.67	0.77	0.81	0.97
COMP_FT	95,894 (28,880)	90,934 (26,501)	96,358 (32,447)	97,314 (30,774)
ADMEFF	0.117 (0.109)	0.119 (0.113)	0.077 (0.090)	0.074 (0.062)
FUNDRAIS	0.167 (0.106)	0.164 (0.095)	0.159 (0.113)	0.159 (0.099)
PROGSPEND	0.942 (0.245)	0.976 (0.253)	0.818 (0.189)	0.865 (0.294)

*Notes:*

Standard deviations are reported in brackets. Refer to Table 2 for a definition of the variables.

pressure towards financial accountability. The level of compensation in the years examined is rather stable. These results are consistent with the findings from Crawford et al. (2009), who find that external requirements are key drivers for change in governance processes. It is also consistent with prior evidence from the private sector (e.g., Von Werder et al., 2005), which suggests that a (small) group of organisations may resist additional disclosures. If this group is too large, voluntary adoption of good governance codes may not result in the desired effects, and enforcement through regulation may become an alternative route of action for the stakeholders involved. Next, we present the results of the regression analysis.

#### *Effects of the 'Good Governance' Code on Managerial Pay Disclosure*

The results of the logistic regressions predicting the disclosure of managerial pay (DCOMP) are reported in Table 6. Column 1 provides the coefficients for DGSTRUCT without the board characteristics (LGBDSIZE and LGBDFREQ). Regression (1) reveals a positive and significant coefficient ( $b_1 = 0.489$ ,  $z = 3.18$ ,  $p < 0.001$ ), indicating that a strengthened governance structure is associated with higher levels of financial accountability. Among the control variables, organisations that are larger, relatively younger and less dependent on institutional funding tend to disclose more. We then evaluate a variation of regression (1) to investigate whether the inclusion of board characteristics would alter the results. Regression (2) (using a smaller sample due to missing data of board characteristics) reports that the coefficients of LGBDSIZE and LGBDFREQ are not significant, therefore confirming the previous significant effect of governance structure as a predictor of managerial compensation disclosure. We also note that charities with relatively large boards are not associated with a lower chance of disclosure of managerial pay.

Regressions (3) and (4) include two dummies measuring the impact of a Type III (DGSTR3) and Type IV (DGSTR4) structure, respectively, to isolate the effects associated with each governance framework. The results are consistent with the previous regressions, with DGSTR4 positively and significantly associated with DCOMP ( $b_3 = 0.634$ ,  $z = 2.32$ ,  $p < 0.001$  in regression (3)). Consistent with previous research in the profit (Laksmana, 2008) and nonprofit (Ostrower and Stone, 2010) sectors, this result suggests that the separation of duties is key for enhancing accountability.

The results for the control variables indicate that larger organisations are more likely to disclose managerial pay. This finding is consistent with the political cost hypothesis, which suggests that more visible organisations tend to disclose more information to reduce the likelihood of adverse political or societal actions and the associated costs. Charities that rely more on institutional donors are less likely to disclose managerial pay levels; one potential reason is that these institutional donors have access to managerial pay levels through other information sources. Finally, charities are relatively more likely to disclose

**Table 6**

Regressions with Managerial Pay Disclosure as Dependent Variable

$$\text{DCOMP}_{i,t} = b_0 + b_1 \text{DGSTRUCT}_{i,t} + b_2 \text{DGSTR3}_{i,t} + b_3 \text{DGSTR4}_{i,t} + b_4 \text{LGBDSIZE}_{i,t} \\ + b_5 \text{LNBDFREQ}_{i,t} + b_6 \text{AUDITOR}_{i,t} + b_7 \text{ADMEFF}_{i,t} + b_8 \text{FUNDRAIS}_{i,t} \\ + b_9 \text{PROGSPEND}_{i,t} + \sum b_n \text{CONTROLS}_{i,t} + u_{i,t}$$

	(1)	(2)	(3)	(4)
Intercept	-1.940**	-2.917**	-2.194	-1.217
DGSTRUCT	0.489***	0.580***		
DGSTR3				-0.069
DGSTR4			0.634**	0.731*
LGBDSIZE		-0.478	-0.617	
LGBDFREQ		0.716	0.687	
AUDITOR	-0.123	0.013	0.002	-0.121
ADMEFF	-0.486	-0.413	-0.104	-0.250
FUNDRAIS	-0.248	-0.713	-0.441	-0.005
PROGSPEND	-0.222	-0.206	-0.120	-0.175
LGSIZE	0.521***	0.614***	0.748***	0.599***
INSTIT	-0.957**	-1.428***	-1.405***	-0.925**
LGAGE	-0.423*	-0.439	-0.396	-0.379*
HEALTH	0.104	0.179	0.139	0.084
INT_AID	0.378*	0.496	0.424	0.343
NATURE	0.049	0.074	-0.037	-0.059
INTER	0.144	0.032	0.055	0.197
Year05	-1.551***	-1.551***	-1.472***	-1.496***
Year06	-1.277***	-1.280***	-1.240***	-1.235***
Year07	-1.122***	-1.062***	-1.028***	-1.097***
N	491	404	404	491
McFadden R-squared	19.3%	23.6%	22.4%	19.9%
LR statistic	86.67***	85.80***	81.39***	89.20***

Notes:

\*\*\*, \*\*, \*, significant at the 1%, 5% and 10% levels (two-tailed), respectively. Refer to Table 2 for a definition of the variables.

managerial pay over the years, potentially as a result of increasing political and societal pressure and increasing adoption of the Code.

### *Effects of the 'Good Governance' Code on Managerial Pay Level*

The results of the regressions regarding the level of managerial pay are shown in Table 7. In regressions (1) and (2), we enter the governance structure variables to test whether they explain compensation levels without including other governance characteristics. The results show no significant coefficients. In turn, regression (3) exhibits a negative and significant coefficient of LGBDFREQ ( $b = -31,122$ ,  $z = -3.81$ ,  $p < 0.001$ ) on COMP\_FT. One potential reason for this result is that charities with a higher number of board meetings tend to

**Table 7**  
Regressions with Managerial Pay Level as Dependent Variable

	(1)	(2)	(3)	(4)	(5)	(6)
$\text{COMP\_FT}_{i,t} = b_0 + b_1 \text{DGSTRUC}_{i,t} + b_2 \text{DGSTR3}_{i,t} + b_3 \text{DGSTR4}_{i,t} + b_4 \text{LGBDSIZE}_{i,t} + b_5 \text{LGBDFREQ}_{i,t} + b_6 \text{AUDITOR}_{i,t} + b_7 \text{ADMEFF}_{i,t} + b_8 \text{FUNDRAIS}_{i,t} + b_9 \text{PROGSPEND}_{i,t} + \sum b_n \text{CONTROLS}_{i,t} + u_{i,t}$						
Intercept	-176,317***	-172,757***	-193,855***	-184,288***	-178,201***	-189,142***
DGSTRUC	1,465		-1,459			
DGSTR3		852		-13,388**	-24,745	-13,599**
DGSTR4		2,345		-14,497**	-17,692**	-6,114
LGBDSIZE			-123	-980	-25,056	7,391
LGBDFREQ			-31,122***	-31,537	-13,137	-41,229
DGSTR3 x LGBDSIZE					32,758	
DGSTR3 x LGBDFREQ					-28,228	
DGSTR4 x LGBDSIZE						-33,374
DGSTR4 x LGBDFREQ						-28,362**
AUDITOR	9,503**	9,517**	8,140**	8,333	8,323	8,316
ADMEFF	5,596	5,594	23,312**	23,444**	23,506**	23,569**
FUNDRAIS	25,666**	25,697**	27,168**	27,674**	30,074**	30,097***
PROGSPEND	11,665***	11,671***	16,198***	16,308***	18,020***	18,119***
LGSIZE	35,746***	35,740***	42,842***	42,851***	43,383***	43,368***
INSTIT	-16,963**	-16,942**	-17,391**	-17,033	-16,940	-16,868**
LGAGE	3,765	3,757	2,613	2,524	2,317	2,261
HEALTH	13,133***	13,132***	9,667**	9,587**	8,517*	8,500*
INTAID	-7,913	-7,931	-13,302**	-13,646***	-14,154**	-14,178**
NATURE	-2,805	-2,805	-5,402	-5,035	-5,476	-5,774
INTER	-2,796	-2,782	-1,868	-1,698	-1,347	-1,342
Year05	-5,826*	-5,812*	-6,110*	-5,921	-5,728	-5,664
Year06	-7,141***	-7,130***	-7,392***	-7,267***	-7,156***	-7,100***
Year07	-1,864	-1,858	-1,194	-1,188	-1,339	-1,187
N	373	373	319	319	319	319
Adj. R-squared	59.58%	59.58%	64.49	64.6%	65.29%	65.30%
F-value	35.07***	32.79***	32.16***	30.39***	28.04***	28.03***

Notes:  
\*\*\*, \*\*, \* significant at the 1%, 5% and 10% levels (two-tailed), respectively. Refer to Table 2 for a definition of the variables.

discuss managerial pay levels to a larger extent than charities with a few board meetings, eventually having a mitigating effect.

More importantly, the regression coefficients of both DGSTR3 and DGSTR4 taken together in (4) are negative and significant, suggesting an association between governance structure and pay level, even in the presence of a mitigating effect by board frequency meetings. To provide robustness to this result, we introduced an interaction term between board characteristics and governance structures in regression models (5) and (6), respectively. Our results suggest a negative main effect of DGSTR4 in combination with a negative interaction term for DGSTR4xLGBDFREQ. This indicates that the adoption of a Type IV governance structure reduces managerial pay level, with frequency of board meetings strengthening the effect. Jointly, these results suggest that 'good governance' reduces the likelihood of paying 'excessive compensation'.

The results for the control variables indicate that managerial pay is tied to organisational performance characteristics (fundraising, program spending and administrative efficiency ratios). It also appears that having a Big-4 firm as an auditor mitigates managerial pay level and that organisations with more institutional donors appear to have lower managerial pay levels. Moreover, older organisations tend to have higher managerial pay levels, perhaps because these organisations have developed towards greater professionalism relative to their younger counterparts. Charities in health care are also associated with higher pay levels; this may be explained by the fact that charities in health care tend to be headed by a former medical practitioner. These managers may want to hold on to the salary levels they previously earned in medical practice.

### CONCLUDING DISCUSSION

This study examines the initial impact of a 'good governance' code that was promulgated in the Netherlands in 2005 ('Code Wijffels'). Our results from a representative sample of organisations indicate that in the period subsequent to the implementation of the code, charitable organisations significantly modified their governance structure. We summarise our empirical findings in Table 8.

First, we observe an increased adoption of independent supervision by installing a separate oversight board following the implementation of the code (Type IV governance structure). Our results extend previous literature by assessing the adoption of governance codes in the charity sector. Prior research on 'good governance' codes (e.g., Aguilera and Cuervo-Cazurra, 2004) suggests that legislation is a key driver for the adoption of good governance practices. Our findings confirm that the promulgation of a regulatory reform indeed modified the governance structure of a large portion of Dutch charities.

Our analysis also indicates an improvement in financial accountability in the form of enhanced disclosure of managerial pay following the adoption of good governance practices. Previous research from both the profit (e.g., Laksmana, 2008) and nonprofit (e.g., Ostrower and Stone, 2010) sectors suggests that 'good

**Table 8**  
Summary of Main Findings

	<i>Research Question</i>	<i>Empirical Findings</i>
RQ1	What is the adoption rate over time of a (voluntary) 'good governance' code in charitable organisations?	Adoption rate increases over time. Similar pattern of diffusion as legislative 'good governance' codes in the private for-profit sector.
RQ2	Is the (voluntary) adoption of a 'good governance' code associated with increased managerial pay disclosure?	Confirmed. Separation of decision making and monitoring tasks is associated with an increase in the disclosure of managerial pay.
RQ3	Is the (voluntary) adoption of a 'good governance' code associated with lower managerial pay levels?	Confirmed. Separation of decision making and monitoring tasks is associated with lower managerial pay. A higher number of managerial board meetings strengthens this effect.

governance' enhances accountability. Specifically, Laksmana (2008) shows that independent boards increased their disclosure of managerial pay practices, with board size and more board meetings having variable (positive) effects in curbing agency problems. We provide evidence that charities separating decision making from monitoring tasks are more likely to disclose managerial pay in their annual report, controlling for several organisational characteristics. Board size and board meeting frequency do not appear to have a significant effect, thereby suggesting that the separation of decision making and monitoring tasks may help maintain effective monitoring, even in the presence of large boards. This finding is important for policy-makers and regulators, as it indicates the importance of independent boards for improving charity disclosures and accountability.

Furthermore, we investigate the determinants of managerial pay level among the charities that disclose this type of information. Consistent with our previous analysis, we document that (controlling for organisational characteristics and performance levels) enhanced governance structures have a mitigating effect on the level of managerial pay. Specifically, we find that charities that separate decision making from monitoring tasks have lower managerial compensation. It also appears that a higher number of board meetings strengthens this relation. These results extend previous (mostly for-profit sector) empirical evidence documenting that good governance reduces executive pay levels (Core et al., 1999; and Hallock, 2002). A managerial implication of our findings is that regulators and donors should strive for independent boards and a minimum number of annual board meetings to control for agency problems. This is especially important for larger, highly visible charities, considering the societal impact of governance failures in these types of organisations. In addition, regulators could consider (higher) fines and/or alternative sanctions for



charities that do not adhere to governance guidelines (e.g., those withdrawing fiscal benefits or funding in the form of government grants or those denied accreditation by the CBF). Overall, our findings indicate that the Code Wijffels seems to have delivered the expected effects in terms of increased accountability and transparency to address the declining trust in the Dutch charitable sector at the beginning of this century.

The contribution of our paper to the governance literature in the nonprofit sector is threefold (Helmig et al., 2009; Hyndman and Jones, 2011; Hyndman and McDonnell, 2009; Jegers and Lapsley, 2003; and Lambert and Lapsley, 2011). First, the paper contributes to the limited evidence of the impact of regulation on financial accountability and transparency in charities (see Neely, 2011). Few studies have investigated the effects of adherence to 'good governance' codes on managerial compensation disclosures and pay levels; this is rather surprising, as a number of these codes have been initiated as a response to a lack of accountability or the (suggestion of) 'excessive' managerial pay levels. The results of this study provide insights to policy-makers, stakeholders and managers of charitable organisations attempting to evaluate the efficacy of (voluntary) 'good governance' initiatives in the nonprofit sector. Second, our empirical analysis explores data collected across four consecutive years with the objective of tackling the issue of causality. In this way, we are able to investigate the adoption rate of 'good governance' practices and to go beyond critiques formulated against reliance on cross-sectional settings in prior empirical analyses (Jegers, 2009, p. 151). Third, our study attempts to enhance comparative research on this theme by enlarging the scope of research and allowing insights into institutional contingencies outside the United States and the United Kingdom, where most of the prior data have been collected. Our analysis of the Dutch context could be especially useful for policy-makers of other European countries with similar institutional environments that are contemplating similar policy interventions as the Code Wijffels.

The exploratory evidence documented in this study has several limitations and leads to further research directions. First, the analysis is limited to the first years following the implementation of the Code Wijffels, leaving open plausible questions about the actual change exclusively caused by the code's adoption. A comparison with data in the pre-implementation phase would have added robustness to our findings, similar to the natural experiment research design adopted in Neely (2011) in the US context. The absence of available data in our setting constrains this option because most of the required information cannot be retrieved from available reports in the Dutch charitable sector before 2005. Future research examining the effects of the Code Wijffels on charity performance (e.g., donor support, managerial compensation) over a longer post-period time frame would also be fruitful to provide additional insights to regulators. Second, while attempting to include in the analysis theoretical variables as plausible explanatory factors of managerial pay disclosure and levels, the regression models tested in this

study remain incomplete. Future studies could build on this paper to further examine determinants of compensation disclosure and levels and to investigate which additional governance characteristics are significant factors in explaining financial accountability (De Andres-Alonso et al., 2006; and Ostrower and Stone, 2010). Third, this study did not focus on an 'excessive' compensation level as a dependent variable. Another extension of our study would be to identify factors other than the adoption of a code of 'good governance' that are most effective in curbing 'excessive' pay.

We further acknowledge that the involvement of the sampled charities through committees in developing the governance code may be unique to the Dutch setting. A potential reason for the high adoption rate is that the charities themselves have been involved in developing the code; this involvement may increase the likelihood that charities consider the code important, efficient and/or effective (e.g., Breen, 2012; and Phillips, 2012). In addition to the involvement of charities when developing the code, the Dutch institutional environment is characterised by clear and strict standards that facilitate compliance and enforcement (e.g., through the CBF) and the effective publicity of the self-regulatory scheme through mass media (Breen, 2012). As such, our results may not be transferable to other countries with less enforceable standards and lower public exposure regarding charity government regulation. Another reason may be provided by the political cost hypothesis: charities in the Netherlands may have felt that adoption of the code would reduce the likelihood of (potentially more strict or costly) legislation. Additional research among these lines in other countries with different institutional environments can provide interesting insights.

Finally, determining whether managerial pay disclosure also affects donor support (e.g., Calabrese, 2011; and Szper and Prakash, 2011) or overall managerial compensation levels remains a crucial issue that could be explored in future studies. That is, the provision of information on managerial compensation is only effective when external principals (donors, other supervisory boards) find this information relevant and act upon it. Donors may not be affected by managerial compensation unless it is considered 'extremely excessive'. In addition, an unintended consequence of increased managerial compensation disclosure may be that managers in other charities believe that they are underpaid relative to their counterparts and may use managerial compensation disclosures from other charities to bolster their arguments for increased pay. Further research combining quantitative and qualitative data should thus consider the complex interrelations among governance characteristics, organisational performance and donations levels to establish a more comprehensive understanding of such relationships, particularly from a theoretical point of view (Brown et al., 2012; Calabrese, 2011; Callen et al., 2010; and Jacobs and Marudas, 2009).

## NOTES

- 1 Consistent with past studies on corporate governance (e.g., Aguilera et al., 2008), we use the terms 'comply' and 'compliance' with regard to the adherence of firms to governance regulations, codes or provisions. While compliance with legislation may be compulsory (e.g., mandated), compliance with governance codes is largely voluntary. The need to comply with voluntary governance codes may stem from purposes ranging from efficiency to legitimisation (Aguilera et al., 2008).
- 2 The supervisory board is similar to the Board of Trustees in a UK setting. The supervisory board usually consists of volunteers from the private sector, the central government or other public sector organisations. Supervisory board members are usually appointed by the Supervisory board themselves based upon a profile that is developed jointly by the Board of directors and the Supervisory board.
- 3 Our database includes VFI as well as non-VFI members.
- 4 We use Eviews to estimate the regressions. We apply a binary logistic regression to estimate the regression models for RQ2. We use ordinary least squares with Newey-West corrected standard errors and covariance to estimate the regression models for RQ3.
- 5 In the Netherlands, managers can opt to work part-time (for example, one day a week). This is a pervasive characteristic in nonprofit settings; therefore, we standardise the level of compensation by calculating a full-time equivalent (FTE) pay.

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