TREE FUND MEMORANDUM

Date: April 23, 2019

To: TREE Fund Board of Trustees

Fm: J. Eric Smith, President and Chief Executive Officer

Re: Report for May 6, 2019 Trustee Meeting at Bartlett Labs

INTRODUCTION:

I am preparing this month's report from my new apartment in Des Moines, Iowa, where Marcia and I moved effective February 1, consolidating our two prior apartments and storage units after three years apart. It makes a big difference in the quality of our lives as a family (our daughter now lives across the street), and so I very much appreciate your willingness to allow me to establish and work from this remote office location.

Thus far, the new paradigm seems to be going well. Having Maggie Harthoorn and Barb Duke together full-time in the office, with Monika Otting there three days a week, relieves my primary concern about leaving anyone in the office alone most of the time. We all hold a regular "check-in" video meeting each Monday so that the remote employees (me and Communications Manager Teresa Recchia) can kick off the week with updates and exchanges of information with office staff in a conversational setting, and we're all able to collaborate with document exchanges and other business matters via our secure VPN and a new high-speed, dedicated internet access line. TREE Fund's office lease expires in August 2021, and we have an agenda item for this meeting to establish a working committee to evaluate options should we wish to move or reconfigure around or before that time. Our next check point on the current arrangement is in October 2019, when the Board and I need to assess whether we consider having the CEO working remotely is good for both parties. I will prepare an assessment from my end before that deliverable date.

Many of the activities that I am engaged in are covered in Committee Chair reports, so per my normal convention, rather than re-stating them here, the balance of my report summarizes other actions required or recommended, or emergent matters, arranged by the Committee under which they primarily fall for oversight purposes.

GOVERNANCE/EXECUTIVE:

Salary Benchmarking: As a Strategic Plan deliverable, I provided the Governance/Executive Committee with an assessment of my salary and staff salaries, using the *2018 Guidestar Nonprofit Compensation Report* and its related raw data set, provided to us at no cost by CCS (the consultant who helped us with feasibility planning a few years back).

In assessing how our salaries align with industry norms, I looked at nonprofits both in the $500,000 to $1.0 million range, and then the $1.0 million to $5.0 million range, and also looked nationally, regionally, and by National Taxonomy of Exempt Entities (NTEE) codes. While our annual operating budget is usually a bit over $1.0 million each year, I looked at data above and below that level because the higher range has us comparing ourselves to nonprofits with budgets as high as $5.0 million, which is a bit of a stretch for us from a comparative standpoint. Also, when you consider that a sizable chunk of what we spend money on is essentially pass through (e.g. we are "buying" research from contract providers, we pay Paul Wood a flat fee to manage the Tour as a contractor instead of having that function in house, we out-source accounting to a contractor, we manage sponsored grant for a fee, etc.), the reality of what our office and staffing environment looks like when you consider what we spend in Naperville is much more like a smaller nonprofit in that $500K range.

As a general summary, the results of the analysis did not surprise me: you pay me at the high end of the spectrum for comparable organizations (at or over 75^{th} percentile in all comparative cases, and over 90^{th} percentile in many cases), and the remainder of the staff are paid in the low ranges: 25^{th} percentile range most of the time. As I have told you before, I was aghast when I was hired and learned how little our other employees were being paid in relative comparison to what you pay me. I have diligently worked to increase compensation for the staff since I have been here, both through bonuses and annual increases, and through enhanced benefits (expanded paid time off, increased employer contributions to 403b plans, improved office working environment, etc.), and I am committed to continuing to do so. But there are boundary issues there in terms of what I can do here, since so much of the funding we raise is for endowment, which cannot pay employee salaries, or comes via Tour riders, and we commit to spending that on research.

When the time comes that I leave the organization, I most emphatically recommend that the Board needs to "reset" the CEO's compensation to something more closely approximating the median compensation for organizations of our size – around $90,000 in 2018 – and then encourage that new CEO to use those "freed up" funds to bring other staff salaries up closer to their median levels too. When you hired me, I believe that you benchmarked my salary around what you were paying Janet Bornancin at the time of her retirement. Janet and I were/are both "end career" employees, and I believe that you would be better served in your next hire for leadership with a "middle career" CEO, who will more likely be with the organization for the long haul, and who will be pleased to join it at a nonprofit industry-appropriate salary level.

I welcome your thoughts and perspectives on this topic, and have no specific recommendations, other than noting that as part of the Strategic Plan update I have asked the Board to only evaluate and adjust compensation for me every other year, while I will continue to pursue regular annual increases for the team, as I did already for Maggie Harthoorn.

Business Continuity and Risk Management Plan: At the Executive/Governance Committee's request, I developed a new Business Continuity and Risk Management Plan as part of our Trustee Policy Handbook to ensure efficient and effective responses in the event of unforeseen circumstances that could have material impact on our operations or reputation. The Committee accepted the policy, and it will be presented to you for a ratification vote at our meeting.

Strategic Plan Update: In hewing to a commitment that "planning is more important than plans," we are updating our three-year Strategic Plan annually, evaluating and rolling off the completed year, and adding the out year. I assisted the Strategic Planning Task Force (an ad hoc subcommittee of the Executive/Governance Committee) with this update, and it will be presented to you for a ratification vote at our meeting.

Hyland Johns Endowment Fund: Hyland Johns contacted us recently and let us know that it was his wish and desire that his planned estate gift be earmarked for an endowment to support the annual grant issued in his name. While we have been awarding these grants since our inception (actually before, as they were awarded under ISA Research Trust purview too), we have never endowed this program. I would like to honor Hyland's wishes, which require your vote to establish a new Fund. To preclude adding additional competitive forces as we actively fundraising for Tree and Soil Research Fund and Larry Hall Fund, I would recommend that the endowment have an open ended cap: we are already awarding these grants, so do not need an "activation" goal, and could just begin drawing from this endowment pool annually once it is established. We can certainly announce its establishment while Hyland is still with us, as I know that will generate interest and support, but I do not want to lock Hyland's estate gift or other gifts that could defray existing John's grants expenses up for years while we work toward a high endowment goal. Whatever goes in there would help, now. We do have other planned gift agreements made in past years that also involve new small endowment funds, and we could dedicate their proceeds to the annual Hyland Johns grants as well.

DEVELOPMENT/LIAISON:

Tour des Trees: Early registration and fundraising for this year's Tour are robust, so I feel good that the changes we made to structure and timing of the Tour, as well as seeking out new routes in Chapters where we have not been before, are proving successful. As noted in early correspondence, I suspect we will have to cap registration and create a waiting list, but that is not a bad problem to have, unless we get strong blowback from people who are shut out. We do have fairly severe lodging constraints in some of our overnight locations this year, and I do not want to exceed the allowable rider-to-vehicle limits per our contract, upon which our insurance policies are built, so it is an emphatic cap without wiggle room.

Partnerships: We are in good shape at the end of first quarter for partnerships and other operating support, though as always, I welcome any leads any of you may have, and also welcome your assistance in leveraging your professional networks with asks. As one recent example, Will Nutter and I are at the final "dotting the I's and crossing the T's" stage of a new partnership with Lewis Tree for $75,000 over five years. I know there are others out there who would be able and willing to engage in multi-year deals like that, and I would like to move us more in that direction, as it assists with financial planning and stability.

AUDIT/FINANCE:

Annual Financial Audit: We have completed the 2018 Annual Financial Audit with Sassetti LLC, and the Audit/Finance Committee has voted on behalf of the entire Board to accept its findings, from which there were no material issues to report. We are currently working on the related tax documents to support timely filing of State Charitable Registrations before May 15, 2019. It was a solid year, marred only by that fact that the brief stock market adjustment in fourth quarter of 2018 bottomed out right around December 31, when our fiscal year ends, making it the point at which all of our financial data are developed. We show a net loss in assets accordingly, though it is entirely attributable to reduction in the value of the Chicago Community Trust (CCT) investments, which have mostly rebounded already by the end of first quarter of 2019.

Chicago Community Trust: While CCT cannot control the market, and we can expect our assets there to fall when the market falls, I was surprised at the severity of the fall in their Growth Pool (where our funds are invested) in late 2018, given that the express purpose of their investment strategy is to preserve the corpus over the long term. For the third year running, after agreeing with my proposed budget numbers for the coming year, CCT informed me that our actual payout would be lower than what we budgeted. In digging into this annual disparity, I realized that their calculation methodology for the purported annual "4.5%, less fees" drawdown is disadvantageous to us, while keeping more of our needed funds in CCT's hands.

My discomfort with them over this, routine late reports, a general lack of "value added" beyond keeping our endowment funds safe from future predation, and them "holding all the cards" per a punitive instrument of gift (e.g. they could reduce the annual payout anytime they wanted, as they already did once – it was 5.0% when we first contracted with them) finally leads me to the point where I believe we must have a parallel investment option that provides us with more latitude in how to manage our long-term endowments. With Finance/Audit and Executive/Governance Committees' concurrence, I am currently holding all permanently restricted funds in our operating account, while we evaluate options. I am running into problems finding a viable alternative, though, because our approved investment policy is fairly prescriptive about the size and type of investment manager we can employ, and we will not have enough to invest up front to get into some of the more premium investment instruments offered by major brokerages.

To help on this front, I would request the Board's approval to making a request (and it is only a request, they have the right to refuse it) of CCT to return funds from the endowment pools that have yet to reach their goals (Davey Fund, Tree and Soil Research Fund, Larry Hall Fund, Bartlett Fund; note that the latter was an unrestricted fund inappropriately placed with CCT, so technically it could be dissolved, though I am mindful of the optics of doing that), so that we may use those funds as seeds for the new investment account, along with whatever we raise this year. I would welcome insight and perspective from you on advisors you would like me to consider, or your direction if you wish us to move in a different direction (e.g. a simple account with no advisor, and decisions made by Audit/Finance Committee). Once we have this established, we need to make decisions on whether funds already endowed at CCT will have all future funds to those pools sent there, or be split between the two investment pools.

COMMUNICATIONS:

Website: Our website update went smoothly, and I'm pleased with the more modern look (now phone and tablet compatible) and significantly improved functionality and back-end maintenance. With this new platform, we will be able to better integrate our social media and email-based communications activities, and we will conduct audits of these functions annually going forward.

Customer Satisfaction Survey: We completed the survey in January per the Strategic Plan and will repeat it annually. A summary of the results is provided with your meeting materials; the key takeout, for me, was that we need to continue to better communicate outputs and outcomes so that key constituents feel connected and advised on how their support made a difference.

RESEARCH AND EDUCATION:

SGL 33 Contract: I appreciate your email vote on the second year of this contract. I have the contract and funding from Asplundh and their cooperators (Corteva, PECO, First Energy) in hand, so am just working with Penn State on finalizing their contract, at which point we will send their first installment payment for the year. Duquesne Light and Power had expressed an interest with Penn State in conducting a similar sizable project on one of their rights of way, and we have been working to bring that to pass, though the utility seems at the last minute to be waffling, so I'm not terribly optimistic at this point. That said, these types of large, sponsored grants are good for us from a financial standpoint, so I will continue to cultivate them.

Other Grants: Dr. Hudler and his team are hard at work on the Hyland Johns and UARF research grants, along with all education and scholarship awards, and will carry recommendations for your action at our meeting. We will be awarding the first Bob Skiera Memorial Building Bridges Fund grant in the fall ($30,000, of which $25,000 is from the Skiera Fund, and $5,000 is from the John White Fund, which we recently completed), as well as the first Barborinas Family Fund grant, and our normal Duling and Kimmel awards.

We also shifted Safe Arborist Techniques Fund (SATF) grant cycle from spring to fall this year to balance review load. For SATF, we have had only two applicants each year that we have awarded it, and we are hearing from the researcher on the second award (Alexander Laver) that he is struggling and may not produce any meaningful outcomes for us.

We have as a New Business item on our meeting agenda to discuss Biomechanics Week, since we have again been asked to provide funding for it, though they were declined for a Duling grant last year. We have provided funding for this initiative in the past, but not via grants. This concerns me and sets a bad precedent, because we are not in the "sponsorship" business, which is essentially what they are seeking from us and others. That said, it is a high visibility research gathering that ties to our mission, and there is strong energy around it that we need to be represented and supportive.

An argument could be made that it is a viable option for SATF funding, though with the move of that grant program to fall cycle, the timing does not work this year. That said, the Trustees could elect to direct this year's SATF funding to Biomechanics Week in lieu of conducting a competitive grant review process. Or we could just say that Biomechanics Week is simply not something that fits in our portfolio. This topic keeps coming to me from a variety of people around the industry, so I would like the discuss with you all and have clear direction on how we are going to handle this, once and for all.

I look forward to our Research Workshop after the Board meeting to help frame and focus all of our grant programs for the next few years.

CONCLUSION:

As always, please let me know if you have any questions, concerns or comments on anything in this report. I remain grateful for your wise counsel and support.

All best,

J. Eric Smith, President and Chief Executive Officer