



REMUNERATION UPDATE REMUNERATION UPDATE

AUGUST 2005

This Newsletter covers a range of remuneration and governance issues relevant to both the private and public sectors:

- **Changes to Victorian State Government policy on executive remuneration.**
- **CLERP 9 Remuneration Reporting - Round 1 begins.**
- **Balanced Scorecard thinking shifts boardroom focus.**
- *Variable Reward in Australia in 2005 - National Remuneration Centre, in association with Geoff Nunn & Associates to undertake a new survey of incentive practice.*

Changes To Victorian State Government Executive Remuneration Policy

When the Liberal Government came to power in Victoria in 1992 it introduced a comprehensive range of government reforms. Some of these impacted upon executive employment in Government Business Enterprises and Statutory Authorities. Changes included:

- The introduction of fixed term contracts for all executives.

- Eligibility to participate in a short term incentive plan which had the potential to deliver up to an additional 20% of package.

- Partial delegation of executive remuneration setting to Boards and Board Remuneration Committees. Many opted for a market aligned approach.

Stricter controls were re-introduced with the appointment of the Government Sector Executive Remuneration Panel in 1997 (which succeeded the earlier Joint Advisory Panel).

In July, 2005 the Victorian State Government announced that executives in Government Business Enterprises and Statutory Authorities would be given the option of 'converting' 3% of their (20%) incentive opportunity to fixed annual remuneration. This follows a similar decision with regard to Executive Officers in the Public Service in late 2004.

On the surface this seemed an attractive proposition. However there was a sting in the tail. Overall executive incentive payments (for those that elected to convert the 3%) were to be capped at 6% of the total package value of participating executives. In other words total earning capacity could reduce by up to 11%.

Many GBEs and Statutory Authorities in Victoria currently have market aligned short term incentive plans.

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Up to 50% of the maximum is paid if organisation, business unit and individual targets are achieved. This strategy delivers moderately competitive total reward packages.

The current change forms part of a broader agenda of winding back reforms and returning a traditional approach to government sector remuneration. In 2004 the State Government moved away from broadbanded remuneration structures and reverted to fixed incremental structures for non-executive employees.

Several commentators are watching this shift in policy with some concern. There is a general perception that Government Business Enterprises and Statutory Authorities in Victoria enjoy better corporate governance and management, and deliver higher levels of performance than they did in the 1980s and early 1990s.

CLERP 9 Round One Commences

In the February 2005 **Remuneration Update** we provided an outline of listed company's requirements under the Corporate Law Economic Reform Program (*Audit Reform and Disclosure*) Act 2004 (CLERP 9).

Essentially this Act requires companies to include a 'Remuneration Report' as part of the annual reporting process to shareholders. The report is subject to a non-binding vote by shareholders.

Over the past few months we have had the opportunity to work with a number of organisations in preparation for their first CLERP 9 Remuneration Report. We have observed a sharpening of focus and rigour in relation to board and executive remuneration decisions. Responsible executives have been very concerned to ensure the accuracy of job evaluations and validity of market data utilised. They have also gone to great lengths to clearly articulate the linkages between performance and incentive payments.

Over the next two months the first of these Remuneration Reports will be presented to shareholders. The results are certain to make interesting reading.

Balanced Scorecard Thinking Shifts Boardroom Focus

In the July edition of *Company Director*, John Arbouw discusses the fact that non-executive directors now need to look beyond the financials and ensure they have a comprehensive understanding of all key facets of the business. In an environment where directors are ultimately held accountable for the actions of the company it is no longer acceptable to assume all is well if the numbers look OK.

A parliamentary committee is set to examine the role of boards and non-executive directors of incorporated entities in terms of 'corporate social responsibility' and 'triple bottom line' reporting.

Kaplan and Norton developed the Balanced Scorecard in the early 1990s. Their methodology provided a holistic mechanism whereby managers and executives could set measures against a comprehensive range of 'performance drivers' covering all key aspects of the business. These measures could then be used to monitor and drive performance.

The Balanced Scorecard provides an excellent mechanism for Board reporting. Non-executive directors can be kept up to date and informed about all key drivers of the business.

Arbouw asks which factors, in addition to financial performance and compliance, boards should be monitoring. From a Balanced Scorecard perspective the answer to this question is clear. The Board should monitor all factors which impact upon business performance. Examples of these factors include:

- Marketing and sales performance including market share, product development, growth sectors and so on;



- Operational performance such as energy utilisation, wastage, client satisfaction indices;
- Environmental performance such as emissions and other environmental incidents;
- Occupational Health and Safety performance including safety policies, major incidents and so on;
- Human resource effectiveness as measured through various performance management mechanisms.
- The role of business as a 'member' of the community in which it operates.

This list is not intended to be comprehensive. Clearly measures need to be specific to each organisation's operating environment.

In our experience many Boards already insist on comprehensive reporting across a range of financial and non-financial measures.

For an interesting analysis of the importance of tracking financial and non-financial indicators see the Deloitte paper *'In the dark: What boards and executives don't know about the health of their businesses'* October 2004. It can be obtained by searching the Deloitte website:

<http://www.deloitte.com>

Let's hope we don't have to see another raft of legislation before all Australian company boards take a broader view of company performance.

Geoff Nunn & Associates Strengthens Trans Tasman Ties

For a number of years we have had the good fortune to enjoy an 'Associate' relationship with New Zealand's most highly regarded independent specialist remuneration firm 'McBride HR'. McBride HR manages the major remuneration database in New

Zealand. Director, Kevin McBride specialises in providing expert remuneration advice to clients across all industry sectors.

Our relationship has intensified over the past twelve months and we have worked with a number of New Zealand companies (upon referral from McBride HR) with operations in Australia or are seeking to set up in this country. Some New Zealand based companies are now checking Australian market rates for jobs seen as having trans-tasman comparability.

If you have New Zealand operations or are seeking to check market rates in that country please either contact us or Kevin directly :

kevin@mcbridehr.co.nz

See also: www.mcbridehr.co.nz

Variable Reward in Australia in 2005

The National Remuneration Centre, in association with Geoff Nunn & Associates, will launch a new survey this quarter on the incidence and structure of variable reward plans in Australia. In the last ten years the growth of incentive plans has been dramatic. Many have argued about their effectiveness, but the fact is that such plans are now a permanent feature of the remuneration strategy of many organisations.

It will build upon a solid foundation developed by Henry Warren, Managing Partner of the National Remuneration Centre in 1995 when he worked with KPMG to develop the most comprehensive 'Pay for Performance' survey undertaken in Australia.

Other surveys on the market tend to be too general for organisations to use as a reference when developing new plans or checking the currency of existing plans.

The focus of this survey will be to provide a comprehensive analysis and commentary on the effectiveness of different variable reward plans.



About Geoff Nunn and Associates

Geoff Nunn & Associates was established in Melbourne, Australia in 1993. Since then, the Company has established a reputation for professionalism and quality service. Projects have been completed in over 650 organisations across Australia.

Our Philosophy

- ❑ As professional providers, the highest standards of service delivery and quality apply.
- ❑ Depth of expertise is critical in any field of professional endeavour. Our consultants and associates are all professionally qualified and specialists in their fields.
- ❑ Independence increases the options available for addressing organisational problems.
- ❑ Each organisation's operating environment is unique. This uniqueness suggests the need to tailor specific solutions rather than rely on generic approaches.
- ❑ All stakeholders should share in the risks and rewards associated with organisational performance.

Our Services

- ❑ **Remuneration Strategy Development.**
- ❑ **Job Evaluation.**
- ❑ **Market Remuneration Advice.**
- ❑ **Remuneration Packaging.**
- ❑ **Board and Executive Remuneration.**
- ❑ **Performance-Based Incentives.**
- ❑ **Competency Modelling and Profiling.**
- ❑ **Balanced Scorecard Performance System.**
- ❑ **Organisation Structuring and Design.**
- ❑ **Contracts of Employment.**

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