HaRe Group newsletter: **4 May 2004**

Subject: **Executive pay update**

From time to time, there are media reports that provide worthwhile information on executive pay. This newsletter summarises and comments on selected reports in recent weeks.

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Regulation pressure lifts pay rates (The Age, 3 May)
Increased risk and corporate governance are adding to remuneration costs, according to a report by RPC. The highest increases between 2003 and 2004 were for non-executive directors, who received an average 22% rise in reported fees. This average is influenced by some extremely high increases in some industries (viz. alcohol & tobacco and paper & packaging, both average 63% - miscellaneous industrials and transport rose 83%). Median data was not quoted.

Managing directors and chief executives received average total pay increases of 11% between 2003 and 2004. In the RPC sample, average base salary stayed flat at $507,000. However average bonuses and short-term incentives increased from $361,000 to $456,000. Median data was not quoted.

Share options won't be tax deductible (AFR, 3 May)
The Federal Treasurer, Peter Costello, announced last Friday, 30 April, that the cost of share options will not be tax deductible. Mr Costello said a tax deduction was only provided for an economic loss, while issuing share options only diluted the capital of other shareholders. Not providing the tax deduction will increase the remuneration cost of options by about 40%. Macquarie Bank will be hit with a $40 million P&L charge, based on current practices. Macquarie's CFO, Greg Ward, said the P&L reporting change is not material and he was not surprised by the government's decision.

Remuneration strategies that pay off (AFR, 23 Mar.)
Research among the top 50 Australian companies has revealed that few have useful remuneration strategies. While there is lots of data on what & how executives get paid, the study by Wendy Attwater revealed that not much is said about WHY remuneration is paid. Objective job and executive evaluation is a rare discipline.

In many cases, the research found that board directors lack a sound understanding of remuneration issues. Commonly, the fixed remuneration package is based on highly subjective judgements, while the incentive component (often a variable percentage of fixed pay) is based on meeting quantitative targets.

There is also a strong trend to measuring how work is done - the job inputs, not the outputs. Business leaders are being assessed on communication, team building and other softer skills. Salary surveys don't give all the answers - boards are looking for tailored information to explain to shareholders WHY certain remuneration is being paid.

In my experience, the employers that understand and can communicate the "WHY" are usually the better performing organisations.

Performance hurdles at work (The Age, 15 Mar.)
On 11 March, a bunch of NAB executives' share options lapsed when the share price failed to clear the $37.20 hurdle. The market price was only $31.60 on 12 March.

More than 12 million options were issued five years ago at a strike price of $28.23. The options were in the money by $41 million ($[31.60-28.23] x 12.2M), but none could be exercised unless the NAB share price cleared the $37.20 hurdle. A NAB spokesman said the bank sets genuine stretch targets for the exercise of options.

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Comment

Media reports continue to reflect a trend to more performance-based pay. Shareholders are demanding more accountability from company directors, and boards are expecting better performance from their executive teams. These higher expectations will be realised more often when there is a sound application of the performance measures that monitor the execution of business strategies, and when executives are fairly recognised for their achievements based on these strategic measures.

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