HaRe Group newsletter: **24 April 2007**

Subject: **Market remuneration update**

Recent media articles have been reporting the continuation of relatively high executive pay rises. While EBAs usually deliver a 3-4% salary increase to employees, chief executives tend to receive double. When incentive and equity awards are included, the chiefs are likely to receive increases of up to 30%. All this when the latest CPI (for the year to 31 March '07) was just 2.4%.

However, chief executive remuneration in Australia is not extravagant by global standards. The increases in executive incentives (both cash and equity) are considered necessary by many Australian boards – critical for companies operating globally and needing to attract and retain talented executives. Nevertheless, there is an ongoing concern that the "fair value at grant" of share options is not being justly reported – too many executives exercise their options at actual values that far exceed the fair values disclosed in annual reports. An ISS Proxy report has stated that, among the ASX100 chief executives, the actual value was an average three times greater than fair value.

Senior managers are tending to receive average base pay increases within 5-7% – but wide variations occur in different market sectors. The highest average increases are enjoyed by executives in the finance and resources industries. Managers and professional staff tend to receive average increases within 4-5%.

While you will note that these trends are "same incumbent averages", a significant challenge for most employers is ensuring that there is a transparent, fair and motivating (or not demotivating) distribution of base pay increases to all employees. The most important factors to address include:

- Market sector pay rates for different positions at each business location
- Selecting a market rate that should be the target for "fully competent" individual performance
- Tracking the target pay rate and projecting its future movement (roughly about half the same incumbent averages quoted above)
- Establishing a fair and acceptable method of assessing employee performance
- Defining a pay range for every position that will reflect (1) the required elasticity around the target pay rate, and (2) the need to recognise the experience & contribution of each employee
- Managing the whole employee pay review process within a budget

As many of you will know, the HaRe Group Remuneration Planning System can manage all these issues.

Another concern of many company boards is how to offer and deliver variable rewards that will be a performance incentive…and not cost the company a fortune. The key issues for consideration include:

- Identifying the people who should participate, and how their efforts & behaviour should be channelled or focussed
- Benchmarking industry practices – both local and global
- Selecting the right mix of performance measures – both short term and long term
- Determining performance targets for each measure that will reflect business expectations
- Establishing the target reward (either cash or equity, or both) that should be paid for target performance
- Defining minimum and maximum payments that will reflect performance thresholds and stretch targets, respectively
- Good corporate governance and reporting performance hurdles & realistic fair values for share options

Simon Hare

HaRe Group