



# Remuneration Review

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## KMP Remuneration Advisor Engagements

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### INTRODUCTION

External remuneration recommendations for key management personnel (KMP) are now a major issue to be addressed by all companies that are listed on the Australian Securities Exchange (ASX). It can also affect other companies but only in limited circumstances. If unsure then a company's legal position should be clarified.

The vast majority of ASX listed companies have financial years which commence in July and finish in the subsequent June. These companies are already operating under the new provisions of the Corporations Act and need to ensure that they do not inadvertently breach them. Significant penalties apply for breaches of the new provisions. For example, if a remuneration consultant is engaged to provide KMP remuneration recommendations without board approval then the penalty would currently be \$6,600 per offence.

Many companies have had an initial exposure to the new laws when they prepared their 2010-11 Remuneration Reports as they adopted the new reporting requirements as a good corporate governance process. Other companies will not face the new provisions until later this year or early next year, as they apply to financial years commencing from July 2011 onwards.

### REPORTING REQUIREMENTS

The amendments to section 300A of the Corporations Act require the following disclosures in Remuneration Reports if a "remuneration consultant" made a KMP "remuneration recommendation" (see Meaning of Terms section of this paper):

- a) information about the arrangements the company made to ensure that the making of the KMP "remuneration recommendations" would be free from undue influence by the KMP to whom the recommendations relate,
- b) a statement about whether the board is satisfied that the KMP "remuneration recommendations" were made free from undue influence from the KMP to whom the recommendation relate, and
- c) if the board is satisfied that the KMP "remuneration recommendations" were made free from undue influence from the KMP to whom they relate – the board's reasons for being so satisfied.

Other Remuneration Report disclosure requirements that will impinge on the perception of whether "remuneration recommendations" were free from undue influence include:

- d) if the consultant provided any other kind of advice to the company for the financial year – a statement that the consultant provided those other kind(s) of advice,
- e) the amount and nature of the consideration payable for the KMP "remuneration recommendations", and
- f) the amount and nature of the consideration payable for other kinds of advice.

The foregoing needs to be considered in the light of the need for the board or the Remuneration Committee to approve the appointment of the KMP remuneration consultant. These factors lead to the conclusion that boards needs to adopt policies and processes to ensure that they will be well placed to meet their obligations including the reporting obligations. Clearly, if these disclosures are not acceptable to shareholders then they will probably vote against the Remuneration Report which can (if more than 25% of votes are negative) lead to a spill of non-executive director positions.

### POLICIES AND PROCESSES

The following provides a list of policies and processes that should be considered in relation to KMP remuneration recommendations.

1. The Board or Remuneration Committee should formally appoint its remuneration consultant.
2. Before appointing a remuneration consultant a letter should be obtained from the potential remuneration consultant which indicates:
  - a. whether and why the remuneration consultant considers himself to be independent of the company's KMP, and
  - b. what other work has been undertaken with the company over say the last three years and the names and roles of the company personnel with whom the work was undertaken.
3. The company should have a Policy for Engaging External KMP Remuneration Consultants. This policy should cover a range of aspects including those that relate to the reporting requirements outlined in the previous section. Aspects that may be covered include:
  - a. A prohibition on engaging remuneration consultants to provide KMP "remuneration recommendation" unless the consultant has received the prior approval of the board as evidenced by an appointment letter.
  - b. A guideline as to which company roles may engage remuneration consultants to obtain KMP "remuneration recommendations".
  - c. A guideline indicating whether executives may obtain KMP market practice remuneration information, as opposed to recommendations, and whether or not that information may be obtained from KMP remuneration consultants who have been approved by the board.

- d. A requirement for KMP remuneration consultants to include with their KMP remuneration recommendations a declaration confirming that the recommendations have been made free from undue influence from the members of the KMP to whom they relate.
  - e. A guideline for employees to seek clarification from for example the Company Secretary or Legal Counsel should there be doubt as to whether an engagement of an external advisor needs to be approved by the board or could involve the provision of KMP remuneration recommendations.
  - f. A guideline on the provision of information etc. to remuneration consultants who are undertaking work that may lead to KMP remuneration recommendations. Such interactions and the information provision need to be undertaken in such a way as to avoid exerting or appearing to exert undue influence on the remuneration consultant. In companies that have comprehensive human resources functions it may be desirable to delegate the supply of information on current KMP remuneration practices to say the Remuneration & Benefits Manager and for the company policy to make it clear that: KMP must not seek to influence the information or advice to be provided by the Remuneration & Benefits Manager, and the Remuneration & Benefits Manager must limit their interaction with the KMP remuneration consultants to the provisions of facts and professional views that they are qualified to express provided that such views are unbiased.
  - g. A process needs to be installed for recording fees payable to KMP remuneration consultants for any work undertaken including non-KMP remuneration work. Such fees need to be disclosed in the company's annual report.
4. The company should communicate the broad terms of the new laws to all KMP and others who may be involved in either the engagement of or provision of information to remuneration consultants so as to avoid inadvertent breaches or actions that may cause the Board concern when making the required disclosures. Distribution of the relevant policy would a step in this communication process.

Companies that wish to appoint GRG as their KMP remuneration consultant will be provided with a letter confirming GRG's independence, a draft Policy for Engaging External KMP Remuneration Consultants and a draft letter of appointment. The draft Policy will enable companies to realise significant savings in time and legal fees as they modify the draft to reflect their particular circumstances.

## MEANING OF TERMS

**KMP** means those persons having authority and responsibility for planning, directing and controlling the activities of the company, directly or indirectly, including a director (whether executive or non-executive) of the company.

**Remuneration consultant** means a person:

- a) who is not an officer or employee of the company, and
- b) who makes a remuneration recommendation under a contract for services with the company to whose KMP the recommendation relates.

This definition is wide and brings within its scope a number of advisors who would not generally be regarded as "remuneration consultants" but nevertheless are contracted by the company to provide services which include KMP "remuneration recommendations" e.g. recruitment and search consultants.

**Remuneration recommendation** is a recommendation about either or both of:

- a) how much the remuneration should be, and
- b) what elements the remuneration should have.

The "remuneration recommendations" that are of concern are those that relate to one or more members of the KMP of a company.

It should be noted that the following are not "remuneration recommendations":

- a) advice about the operation of:
  - a. law,
  - b. accounting principles, and
  - c. actuarial principles and practice,
- b) the provision of:
  - a. facts, and
  - b. information of a general nature relevant to all employees of a company.

### Key Management Personnel Remuneration Advice

GRG is a specialist advisor on remuneration for key management personnel (KMP) i.e. non-executive directors, executive directors and other top executives. To facilitate its independent advisory function GRG maintains two remuneration databases with one concentrating on non-executive directors and the other on top executives. This data analysis allows GRG to remain up to date with current trends and developments and to be able to benchmark company practices against market practice. The increased focus being placed on KMP remuneration makes it more important than ever for Boards to be satisfied that they are adopting practices that are consistent with market practice and appropriate to their company's circumstances.

If you would like an independent review of the market competitiveness of your company's remuneration practices for KMP then GRG will be pleased to assist.

Please call Denis Godfrey or James Bouchier on (02) 8923 5700 or Mike Carroll on 0416 226 131.