

**Phase I Report:
Remuneration Packages for Principal Officials of HKSARG
Appointed Under the New Accountability System**

**Findings of Survey of Remuneration of CEOs, Managing Directors and
Managing Partners and Review of Overseas Practices**

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Introduction

1. At present, all principal officials holding Secretaries of Department and Directors of Bureau positions in the HKSARG are civil servants. They are remunerated according to the relevant civil service pay scale and enjoy fringe benefits provided for in the civil service system. They are subject to the civil service management system and the civil service disciplinary mechanism.
2. There have been views expressed that as senior officials are involved in policy making and play a leading role in public affairs, they should be held accountable for the outcome of their policies. In his 2000 Policy Address, the Chief Executive of the HKSAR undertook to examine how, under the leadership of the Chief Executive, the accountability of principal officials for their respective policy portfolios could be enhanced. In his 2001 Policy Address, the Chief Executive outlined the initial thinking on enhancing accountability of principal officials. The idea is to introduce a new system of appointment applicable to the Chief Secretary, the Financial Secretary, the Secretary of Justice, and most Directors of Bureaux. They would be appointed on terms different to those in the civil service. Their term of office would not exceed that of the Chief Executive who nominated them for appointment.
3. This study includes a review of the approaches taken in a number of developed nations to determine reward levels for appointed, ministerial-level positions. This study also encompasses a survey of pay practices for top executives in a range of sectors in Hong Kong. Together, these reviews and surveys will support the recommendations as regards the approaches that could be adopted.
4. This Phase I Report describes in detail the methodology, selection criteria for organisations included in the remuneration survey, selection criteria for countries to be included in the review of overseas practices, and detailed presentation and analysis of the results of these surveys and reviews.

Part I. Survey of Remuneration of Chief Executives, Managing Directors and Managing Partners

Purpose of Remuneration Survey and General Criteria for Selection of Organisations

5. The purpose of the survey is to provide an indication of compensation levels for chief executives, managing directors, and managing partners of leading private sector, public sector and professional services firms. These compensation levels form the basis for determining the range of alternative earnings opportunities available to potential candidates for principal official positions.
6. The Secretary for Constitutional Affairs set the following standard: information on chief executive remuneration should be provided for no less than 25 private sector corporations, no less than 25 professional services firms, and no less than 6 public sector organisations.
7. To support this purpose, the organizations selected for this comparison must in their totality meet several general criteria:
 - Collectively, they represent sectors that are possible sources of candidates for the various portfolios of principal official positions;
 - Collectively, they provide a reasonable indication of the possible range of compensation levels and represent a cross-section of key industries and sectors found in Hong Kong;
 - They are leading companies in their sectors, in Hong Kong; and
 - The selected position should be a CEO, Managing Director, Managing Partner, or other position with substantial control of all company operations, with a multi-year strategic view subject only to review and approval of a board of directors. The jobholder may or may not be chairman of the organization.
8. Therefore, the selected organisations are drawn from sectors that reflect the strength and diversity of the Hong Kong economy. Principal official positions are highly complex and responsible positions, and only the highest level executive positions in the largest organisations in the private, public, and professional services sectors are comparable to these positions. In view of this, the selected organisations should be among the largest in their respective sectors, and the positions selected should represent possible sources of candidates for principal officials.
9. Detailed criteria for each major sector are provided below.

Selection Criteria for Private Sector Organisations

10. Detailed criteria for selection of private sector organisations are summarized and explained below:
 - Sufficient numbers of companies to provide representation from a range of industries such as financial services; property & construction; utilities; transportation; diversified trading, communications, hi-technology, and retail.
 - May be local or multinational firms with chief executive officers of any nationality or ethnicity.
 - Whether local or multinational, the company should be a recognized leader in its industry within HK, HK/China, or the Asia Region and the span of control of the executive being surveyed could extend from Hong Kong to Mainland China, the Asia region, or the world.

Selection Criteria for Public Sector Organisations

11. Hay Group recommends the selection of at least six to eight public sector corporations including non-governmental organisations involved in providing public services.
 - The selected organisations should not link their CEO's pay to government pay practices (e.g., by reference to directorate scale).
 - Non-governmental organizations are similar in many regards to government-owned corporations and also provide a relevant point of reference for principal officials.

Selection Criteria for Professional Services Firms

12. Professional services firms carry out their business by applying the expertise and knowledge of a profession on behalf of their clients. Professional services firms encompass professions such as accounting, law, real estate, communications, strategy consulting, and engineering.
13. Hay Group recommends representation in accounting, law, real estate, business and technology consulting, and engineering, architecture, and related areas. The firms should include internationally-recognized firms as well as leading local firms.
14. The medical profession is another important branch of professional services. One listed healthcare firm was invited to participate in the survey, as were two public sector organisations with significant healthcare services. However, there is only a very small number of

medical professional services practices that are of a size sufficient to be considered within this survey.

Other Criteria for Selection to Survey

15. Selected firms should have sufficient size and complexity to reflect the complexity and impact of positions of principal officials. Complexity in organisations can be measured by the size of the business (revenue), geographic scope, and the diversity of business areas. As revenues are the most objective available measure of complexity, Hay Group have defined minimum revenue levels for inclusion of organisations in the analyses that follow. The minimum revenue for inclusion of a private sector company is HK\$2 billion per annum, while the minimum for a public sector organisation is HK\$500 million. The minimum revenue for a professional services firm is set at HK\$100 million per annum.
16. The complexity of professional service firms reflects their impact on the strategy and operations of their clients' organisations. Engineering consultants manage highly complex multi-billion dollar projects for their clients. The revenues of their firms reflect only the fees for the services of their engineers and project managers, often less than 10% of the total project value. Strategy consultants advise on long-term strategic business issues that impact the direction of a client's business for years, but fees usually reflect time spent providing services. Therefore, the revenue standard for professional services firms is set lower than for corporations.
17. Likewise, some of the public sector organisations have regulatory or advisory impacts that have a larger economic and social impact than is indicated by revenues or fee income. Therefore, a lower minimum revenue has been set for these organisations.
18. Organisations selected for inclusion in the survey must also be able to provide accurate information on cash compensation and long-term incentives that reflects the earnings opportunities enjoyed by their chief executives or managing partners.

Organisations Invited to Participate

19. The selected list of organisations invited from each sector is given in Appendix 1. To ensure information can be collected from a sufficient number of organisations, additional organisations have been selected for invitation.

Organisations Included in the Remuneration Survey

20. Exhibit 1 lists, by sectors, the organisations that provided data for the survey. For reasons of confidentiality, Exhibit 1 includes all

organisations that have provided compensation information even if they do not meet criteria given in paragraphs 15-18 above. Analyses shown later in this report include only the organisations that meet the criteria.

21. In the event, of the 77 private sector corporations, 13 public sector organisations, and 50 professional services firms invited to participate in the survey, 34 private sector corporations, 11 public sector organisations, and 22 professional services firms provided compensation information within the required timeframe. Of these, 27 private sector corporations, 9 public sector organisations, and 20 professional services firms met the criteria set out above. Although the number of professional services firms included falls just short of 25, Hay Group considers that the data collected from 20 firms are sufficient for the purposes of the present study.

Exhibit 1: Organisations Included in Survey

Organisation	Industry Group
<i>Public Sector Organisations</i>	
Hong Kong Hospital Authority	Public Sector
Hong Kong Housing Society	Public Sector
Hong Kong Monetary Authority	Public Sector
Hong Kong Mortgage Corporation	Public Sector
Hong Kong Securities & Futures Commission	Public Sector
Hong Kong Trade Development Council	Public Sector
KCR Corporation	Public Sector
Mandatory Provident Fund Schemes Authority	Public Sector
MTR Corporation	Public Sector
Tung Wah Group of Hospitals	Public Sector
Urban Renewal Authority	Public Sector
<i>Private Sector Corporations</i>	
Chevalier Construction	Construction
Gammon Construction	Construction
Shui On Construction Ltd	Construction
Amway China	Consumer Product
Lam Soon (HK) Ltd	Consumer Product
Swire Coca-Cola Bottling Ltd	Consumer Product
CITIC Pacific Ltd	Diversified Companies
Hutchison Whampoa Ltd	Diversified Companies
New World Services	Diversified Companies
Dah Sing Financial Group	Financial Services
Hong Kong Exchanges and Clearing	Financial Services
HSBC Holding	Financial Services
Standard Chartered	Financial Services
AXA China Region	Insurance
CMG Asia	Insurance
Manulife (Int'l) Ltd	Insurance
Pacific Century Insurance	Insurance
DuPont China	Others
HAECO	Others
Shangri-la Asia Ltd	Others
South China Morning Post	Others
Television Broadcasts Ltd	Others
Hang Lung Development Co. Ltd	Property

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Organisation	Industry Group
Hysan Development	Property
Giordano	Retail and wholesale distribution and trading
Shun Hing Electronic Trading Co., Ltd	Retail and wholesale distribution and trading
Siemens	Telecom, IT/HT
Cathay Pacific Airways Ltd	Transport
Kowloon Motor Bus	Transport
Modern Terminals Ltd	Transport
OOCL (HK)	Transport
CLP Holdings Ltd	Utilities
Hong Kong & China Gas	Utilities
Hong Kong Electric Holdings	Utilities
<i>Professional Services</i>	
BDO McCabe & Lo	Accounting
Deloitte Touche Tohmatsu	Accounting
Ernst & Young	Accounting
Grant Thornton	Accounting
J Walter Thompson	Communications
Leo Burnett	Communications
Bain & Company (Hong Kong)	Consulting (IT/Strategy/HR)
PA Consulting	Consulting (IT/Strategy/HR)
Pricewaterhouse Coopers	Consulting (IT/Strategy/HR)
Atkins China Ltd	Engineering/Architecture/Surveying
Binnie Black & Veatch HK Ltd	Engineering/Architecture/Surveying
Maunsell Consultants	Engineering/Architecture/Surveying
Ove ARUP & Partners HK Ltd	Engineering/Architecture/Surveying
Scott Wilson	Engineering/Architecture/Surveying
Baker & McKenzie	Legal
Clifford Chance	Legal
Johnson Stokes & Master	Legal
Kwok & Yih	Legal
Woo, Kwan Lee & Lo	Legal
Centaline Properties	Real Estate
Chesterton Petty	Real Estate
Vigers Hong Kong Ltd	Real Estate

22. Most organizations that did not agree to participate did so on grounds of confidentiality of information, or unavailability of executives due to annual leave and business travel. Other organisations that provided information were screened out because they did not meet the criteria for size.
23. Exhibit 2 provides summary statistics for the organisations that are included in the remuneration analysis, including revenues or operating budget, number of employees, and geographical scope. These statistics represent the scope of business managed by the chief executive, managing director, or managing partner whose remuneration is included in the survey. A total of 56 organisations are included in the analysis, including 27 private sector corporations, 20 professional services firms, and 9 public sector organisations.

Exhibit 2: Summary Statistics of Organisations Managed by Participating Chief Executive, Managing Director, or Managing Partner

Sector		Distribution of Revenues (HK\$million)	Distribution of Number of Staff	Distribution of Geographical Scope	
Private (27 orgs.)	P90	26,350	22,155		
	P75	11,194	12,715	HK	5
	P50	6,500	3,900	HK/China	12
	P25	3,504	1,690	Regional	4
	P10	2,725	1,233	Global	6
	Ave	10,561	10,431		
Professional Services (20 orgs.)	P90	1,156	2,430		
	P75	813	1,275	HK	1
	P50	538	665	HK/China	12
	P25	223	298	Regional	7
	P10	120	185	Global	0
	Ave	618	985		
Public (9 orgs.)	P90	–	–		
	P75	7,573	5,600	HK	6
	P50	6,400	890	HK/China	1
	P25	1,500	600	Regional	0
	P10	–	–	Global	2
	Ave	10,605	7,870		
All (56 orgs.)	P90	19,625	15,370		
	P75	7,680	5,450	HK	12
	P50	3,008	1,690	HK/China	25
	P25	795	650	Regional	11
	P10	270	295	Global	8
	Ave	7,017	6,646		

Notes:

- (1) Statistics reflect operations under the control of the participating chief executive, managing director, or managing partner.
- (2) – indicates insufficient information to calculate this statistic.

Categorization of Organizations into Tiers

24. Organisations have been grouped into three tiers based primarily on revenues. Exhibit 3 shows the revenue ranges for each tier, which are determined separately for Private and Public organisations and for Professional Services firms. The Exhibit also indicates the distribution of organizational scope and numbers of employees for each of the tiers.

Exhibit 3: Analysis of Tiers

Sector	# of Orgs.	Revenues (HK\$million)	Staff Distribution	Geographical Scope
Private	27			
Tier 1	12	\$8,000 above	P75 21,444 P50 11,350 P25 4,636 Ave 18,551	HK 0 HK/China 5 Region 3 Global 4
Tier 2	7	\$4,000 - \$7,999	P75 8,815 P50 2,200 P25 1,799 Ave 5,914	HK 1 HK/China 4 Region 1 Global 1
Tier 3	8	\$2,000 - \$3,999	P75 2,350 P50 1,540 P25 1,093 Ave 2,205	HK 4 HK/China 3 Region 0 Global 1
Professional Services	20			
Tier 1	4	\$1,000 above	Ave > 2,000	HK/China, Regional
Tier 2	8	\$400 - \$999	P75 1,275 P50 715 P25 683 AVE 1,170	HK 0 HK/China 4 Region 4 Global 0
Tier 3	8	\$100 - \$399	P75 350 P50 245 P25 178 AVE 285	HK 1 HK/China 6 Region 1 Global 0
Public Sector	9			
Tier 1	2	\$8,000 above	Insufficient data	HK 1 Global 1
Tier 2	3	\$4,000 - \$7,999	Ave 13,282	HK 2 HK/China 1
Tier 3	4	\$500 - \$3,999	P50 625 Ave 1,737	HK 3 Global 1

25. As discussed in paragraph 16 above, the revenue ranges that define the tiers are much smaller for professional services firms than for private and public sector organisations. This is consistent with Hay Group's approach to recognizing differences in value added when comparing executive positions across different organisations. In the analyses that follow, professional firms will be clustered together with private and public sector corporations in the three tiers.
26. To preserve confidentiality of both corporate and individual pay information, the names of organisations in each tier will not be reported.

Methodology

Compensation information

27. Compensation information from participating companies was collected directly from the executive or from a person designated by the executive. Wherever possible, Hay Group sought exact information – current base salary and allowances, most recent payments of bonuses or grants of stock options.
28. Managing partners in some professional firms do not receive base salaries – only an annual distribution of profits based on the size of their holding in the company. These amounts were categorized as short-term incentive.

Long-term incentives

29. Long-Term Incentives (LTI) are incentive arrangements designed to reward an individual for performance over a period of more than one year. Generally, the compensation value of these plans is dependent upon future performance – of the individual, the company, or the stock price of the company.
30. Appendix 2 contains definitions of different forms of LTI. The most common form of LTI is the stock option, but the survey also identified executives receiving grants of restricted shares and performance units. Appendix 2 also contains definitions of terms such as grant, exercise and vesting that are important in understanding and valuing long-term incentives.
31. Long-term incentives may be valued in two ways - by assessing the actual gains received when the incentive is vested and exercised or received, or by estimating the value of the incentive at the time of grant. Because actual gains realised in a given time period can be affected by the state of the markets as well as individual choices, we recommend the second approach as being a more reliable, stable measure of the value of incentives.

32. The methodology for valuing long-term incentives is described in Appendix 2. Where possible, Hay Group obtained details about long-term incentive grant size, frequency of grants, and the vesting schedule from survey participants. Hay Group also supplemented this with information from annual reports when applicable. Where details were not available we have used standard assumptions for valuing the long-term incentives.

Retirement valuation

33. In most cases, respondents are able to provide a specific percentage for the employer's contribution to provident fund or contract gratuity. This amount is multiplied by base salary to determine the amount of contribution that is made on the executive's behalf. In defined benefit final salary schemes, Hay Group used a standard adjustment (shown in Appendix 3) to convert the final salary factor into an annualized employer contribution.

Treatment of Benefits and Perquisites

34. The focus of the survey is on cash and deferred cash elements of pay, including retirement schemes. Other benefits include medical insurance and life insurance, whilst major perquisites include cars, clubs, and leave allowances (including class of travel). Whilst these benefits and perquisites are important, it is relatively difficult for survey participants to provide information on the cost or value of these items and the added difficulty could reduce participation levels. Therefore the survey only asked information to establish prevalence of these benefits and, in some cases, policy levels (e.g., name of club, model of car, class of leave travel).
35. Prevalence information on these non-cash benefits is sufficient for the purposes of this study. Existing government policy on perquisites and benefits for principal officials, including days of annual leave, will likely prevail for appointed principal officials as well. Lack of competitiveness of perquisites, if any, is not expected to be a serious deterrent to qualified and interested candidates, and it is not anticipated that additional cash compensation in lieu of perquisites will be considered.

Dividends

36. Some CEOs have significant shareholdings in their companies. Hay Group have identified these cases and obtained the amount of these holdings and dividends paid from 2000 annual reports or from the respondents, where information is available. It was not possible to obtain this information for all participants in the survey, particularly where the participant is a controlling shareholder who exercises control through an unlisted company, or where the executive holds shares in an unlisted subsidiary.

Compensation Items and Aggregates

37. Information from the survey was analyzed for detailed remuneration items (base salary, allowances, short-term incentives, long-term incentives, retirement) as well as aggregates (total earnings, total direct compensation, and total remuneration). The aggregates are defined in Appendix 3.
38. Information from the survey was analyzed by percentiles and averages. These terms are also defined in Appendix 3, which also shows the minimum number of cases required to show results for a given percentile. To preserve confidentiality of individual pay information, Hay Group will not report remuneration information unless there are sufficient numbers of individuals in the analysis. For example, Hay Group will report average values of remuneration if there are at least three individuals in the analysis, and will report values of the 75th percentile if there are at least eight individuals in the analysis.

Results of Remuneration Survey

39. Exhibit 4 shows results of the remuneration survey for all sectors by tier. To minimise the impact of extreme values on the calculation of average, the highest and lowest paid individuals were excluded in calculating the average values. However, these cases are included in the percentile analysis, which is less sensitive to the impact of extreme values. Exhibit 5 shows a similar analysis for each sector.
40. Total Earnings represents the total cash income received as an employee of an organisation. It includes base salary, housing allowances or housing provided in-kind or as rental reimbursement, and annual variable bonuses. This amount also includes profits shared by a partner, such as a partner of a law firm or an accounting firm.
41. Total Direct Compensation includes Total Earnings plus the annualized value of long-term incentives, and Total Remuneration includes Total Direct Compensation plus retirement contribution.
42. Total Remuneration does not include the following factors, which are generally not differentiating factors in pay at the executive levels: medical and life insurance; cars and drivers; leave passage allowance; and other perquisites or benefits such as club membership or children's education. Hay Group has separately examined the prevalence of these items.
43. The amounts given in Exhibits 4 and 5 for each element or aggregate of compensation is based on all individuals in the analysis, whether or not they receive that element. The exhibit shows the number of individuals who receive a particular element. For example, only 42

out of 56 individuals participate in a retirement scheme – therefore the values for P25 and P10 are near or equal to 0.

Impact of Dividends

44. Hay Group was able to estimate that the chief executives of approximately 11 out of the 27 private sector firms received some amount of dividends through share ownership. In the nine cases that Hay Group was able to ascertain the amounts of the dividends, they ranged between HK\$18,000 and several hundreds of millions of dollars.
45. The average value of total remuneration including these dividends is more than three times the average value of total remuneration excluding dividends. Because of the high variability in the magnitude of dividends, interpretation of these results is difficult and Hay Group has therefore not reported these statistics.

Exhibit 4: Remuneration Analysis - All Organisations by Tiers

Statistics	Base Salary (HK\$000)	Housing (HK\$000)	Guaranteed Cash Compensation (HK\$000)	Short-Term Incentives (% of Base) (%)	Short-Term Incentives (HK\$000)	Total Earnings (HK\$000)	Long-Term Incentives (% of Base) (%)	Long-Term Incentives (HK\$000)	Total Direct Compensation (HK\$000)	Retirement (% of Base) (%)	Retirement (HK\$000)	Total Remuneration (HK\$000)
All Organisations											Total Orgs:	56
P90	5,450	1,800	6,486	158%	9,672	12,225	47%	1,178	12,225	24%	934	12,999
P75	3,790	1,326	4,436	76%	3,956	7,760	17%	593	9,028	18%	455	9,404
Median	2,370	474	3,500	34%	1,427	5,570	0%	0	6,045	10%	211	6,658
P25	1,785	0	2,084	0%	456	4,397	0%	0	4,397	4%	53	4,738
P10	0	0	350	0%	0	2,309	0%	0	2,615	0%	0	2,980
Average	2,819	667	3,486	101%	2,965	6,451	14%	438	6,889	10%	317	7,207
No. Orgs.	49	30	50	42	49	56	22	22	56	42	42	56
Tier 1 Organisations (Private/Public sector: Revenue > HK\$8b; Professional Services: Revenue > HK\$1b)											Total Orgs:	18
P90	7,393	1,970	7,770	423%	13,530	15,015	58%	1,675	15,015	23%	1,036	15,255
P75	4,190	1,725	5,840	103%	6,861	11,529	27%	699	11,954	20%	529	12,866
Median	2,320	1,260	3,681	54%	2,398	7,408	0%	0	8,523	10%	360	8,774
P25	2,089	0	3,040	16%	1,435	5,136	0%	0	6,367	5%	153	6,742
P10	0	0	924	0%	1,151	4,996	0%	0	5,256	0%	0	5,512
Average	3,092	1,055	4,147	92%	4,069	8,217	22%	708	8,925	11%	377	9,302
No. Orgs.	15	12	16	12	18	18	6	6	18	14	14	18
Tier 2 Organisations (Private/Public sector: HK\$4b < revenue < HK\$8b; Professional Services: HK\$400m < revenue < HK\$1b)											Total Orgs:	18
P90	5,090	1,006	5,090	112%	8,184	11,221	30%	1,156	11,376	22%	663	11,588
P75	3,870	574	4,320	56%	3,332	7,415	13%	567	7,716	12%	310	8,348
Median	2,690	0	3,667	39%	1,207	5,820	0%	0	6,284	8%	199	6,378
P25	2,028	0	2,240	16%	774	4,284	0%	0	4,309	1%	18	4,711
P10	490	0	490	0%	270	2,948	0%	0	3,005	0%	0	3,195
Average	2,942	342	3,284	129%	2,937	6,221	12%	393	6,614	9%	275	6,889
No. Orgs.	16	7	16	15	17	18	8	8	18	13	13	18
Tier 3 Organisations (Private/Public sector: HK\$2b/HK\$500m < revenue < HK\$4b; Professional Services: HK\$100m < revenue < HK\$400m)											Total Orgs:	20
P90	4,450	1,620	6,131	125%	5,550	7,960	37%	669	9,149	25%	884	9,562
P75	2,850	1,208	3,734	63%	2,057	5,798	17%	380	5,798	14%	342	6,690
Median	2,050	490	2,357	11%	716	4,819	0%	0	4,960	9%	205	4,998
P25	1,670	0	1,800	0%	0	2,311	0%	0	2,766	4%	57	3,144
P10	1,053	0	1,512	0%	0	2,027	0%	0	2,146	0%	0	2,149
Average	2,459	627	3,086	89%	2,005	5,091	10%	239	5,329	10%	304	5,633
No. Orgs.	18	11	18	12	14	20	8	8	20	15	15	20

Note: Highest and lowest paid individuals are excluded when calculating averages, but are included in calculating percentile values.

Exhibit 5: Remuneration Analysis - All Organisations by Sectors

Statistics	Base Salary (HK\$000)	Housing (HK\$000)	Guaranteed Cash Compensation (HK\$000)	Short-Term Incentives (% of Base) (%)	Short-Term Incentives (HK\$000)	Total Earnings (HK\$000)	Long-Term Incentives (% of Base) (%)	Long-Term Incentives (HK\$000)	Total Direct Compensation (HK\$000)	Retirement (% of Base) (%)	Retirement (HK\$000)	Total Remuneration (HK\$000)	
Private Sector												Total Orgs:	27
P75	4,264	1,550	5,030	102%	3,200	7,978	27%	1,008	9,222	18%	713	10,007	
Median	2,800	1,153	4,109	71%	1,725	6,387	9%	282	7,257	10%	281	7,539	
P25	2,206	0	3,487	29%	1,195	5,007	0%	0	5,189	7%	204	5,510	
Average	3,454	922	4,376	91%	2,483	6,859	24%	770	7,630	12%	408	8,038	
No. Orgs.	27	17	27	25	25	27	15	15	27	25	25	27	
Professional Services Sector												Total Orgs:	20
P75	1,950	582	2,385	41%	7,637	7,967	5%	150	7,967	10%	193	7,967	
Median	1,440	0	1,785	6%	2,298	5,281	0%	0	5,500	3%	35	5,638	
P25	0	0	0	0%	288	2,771	0%	0	2,924	0%	0	3,188	
Average	1,281	372	1,653	147%	4,479	6,132	8%	140	6,272	5%	108	6,380	
No. Orgs.	13	9	14	11	18	20	6	6	20	10	10	20	
Public Services Sector												Total Orgs:	9
P75	6,000	900	6,090	25%	1,100	6,090	0%	0	6,090	25%	578	7,050	
Median	3,640	0	4,400	19%	750	5,500	0%	0	5,500	23%	533	6,000	
P25	2,478	0	3,413	0%	0	4,128	0%	0	4,128	7%	210	4,697	
Average	4,220	577	4,798	17%	669	5,467	-	-	5,598	15%	496	6,095	
No. Orgs.	9	4	9	6	6	9	1	1	9	7	7	9	

Note: Highest and lowest paid individuals are excluded when calculating averages, but are included in calculating percentile values.

Analysis

46. Exhibit 6 summarizes the differentials in average Total Remuneration between the three tiers. The table shows the expected pattern of lower pay as size of organization decreases.

Exhibit 6: Comparison of Total Remuneration Averages

(All Sectors, All Size = 100%)

	All Organisations	Tier 1	Tier 2	Tier 3
All Sectors	100%	129%	95%	78%

47. Exhibit 7 shows the mix of compensation by tier and by sector, where average Total Remuneration in each category equals 100%. The exhibit shows that both short-term and long-term incentive payments increase in importance as size of organisation increases. Public sector organisations have significantly less compensation at risk than private sector organisations. The short-term variable compensation for professional services firms is very high because those organized as partnerships may not pay a base salary to managing partners at all.

Exhibit 7: Remuneration Mix by Tier and Sector

(Average Total Remuneration = 100%)

	All Organisations	Tier 1	Tier 2	Tier 3
All Sectors				
Base	39%	33%	43%	44%
Allowance + Rental	9%	11%	5%	11%
STI	41%	44%	43%	36%
LTI	6%	8%	6%	4%
Retirement	4%	4%	4%	5%
Private Sector				
Base	43%			
Allowance + Rental	11%			
STI	31%			
LTI	10%			
Retirement	5%			
Professional Services Sector				
Base	20%			
Allowance + Rental	6%			
STI	70%			
LTI	2%			
Retirement	2%			
Public Sector				
Base	69%			
Allowance + Rental	9%			
STI	11%			
LTI	2%			
Retirement	8%			

Note: Percentages may not add to 100% due to rounding.

48. Exhibit 8 shows the prevalence of different LTI schemes amongst all organisations. Stock options are by far most common, with performance units as the next most common scheme.

Exhibit 8: Prevalence of Long-Term Incentive Schemes

Plan Type	Prevalence
Stock Options	14
Performance Unit	2
Restricted Stock	3
Stock Option and Performance Unit	3

49. Exhibit 9 shows the prevalence of typical benefits and perquisites, by sector. Whilst medical and life insurance benefits are common, some companies do not provide these benefits, including professional service partnerships. Cars (almost always including driver for work-related trips) are very common, but some firms that take total remuneration approaches or partnerships who remunerate through profit distribution do not provide this perquisite.

Exhibit 9: Prevalence of Benefits and Perquisites

Benefit/Perquisite	All Sectors
<i>Total Participants</i>	56
Retirement (including gratuity)	42 companies
Contribution rate (excluding orgs providing only statutory MPF contribution)	0% (14) 5%-9% (14) 10%-14% (13) 15%-20% (4) 20%-25% (11)
Life Insurance	44
Medical	53
Leave Passage	26
Class of Travel	First (12), Business (9), Economy (3), Not Reported (2)
Car	45
Most Common Car Models	Benz S-class, BMW 7-series, Jaguar Sovereign, Lexus 400
Driver (work)	42
Driver (personal use)	21
Clubs	38
Number of clubs	1 (14), 2 (13), 3 or more (8), Not Reported (3)
Children's Education	18

Part II. Review of Overseas Practices

Selection of Countries for Inclusion in International Review

50. The purpose of the review is to understand practices for determining ministerial pay in other countries. Senior Hay Group consultants familiar with policies in each country have prepared reports for each country.
51. Hay Group recommended selecting countries on the following basis:
 - They represent a range of approaches to determining remuneration for ministerial positions
 - They have different political systems and arrangements
 - Information on the process and basis for determining pay levels is mostly available to the public
52. The potential list of countries is large. Hay Group has selected a number of countries with different practices for in-depth review. These countries include Australia, Canada, Finland, Netherlands, New Zealand, Singapore, United Kingdom and United States.

Overview of Practices

53. Exhibit 10 provides summary of the philosophy, policies, and practices applied by each country in determining remuneration of ministerial positions. Full reports are provided in Appendix 4.
54. The typical practice in countries such as UK, New Zealand, Canada, and Australia is that pay is recommended by an independent commission, who are concerned primarily with providing a reasonable remuneration when compared to members of parliament and other public sector jobs. In these countries, it is acknowledged that pay lags considerably behind private sector practices and it is viewed as politically infeasible to establish a closer relationship. It is also generally acknowledged that there are non-financial rewards to serving in government.
55. Finland and Netherlands have established a comparison either to civil service or even to a multiple of the minimum wage. The US does not have an established review system other than the political process.
56. Singapore is unique in targeting competitive levels of the private sector. The pay level for the entry level of minister is set by applying a discount factor to the median of a group of 48 top paid individuals from the private and professional services sectors. Remuneration progresses through the ministerial ranks up to the prime minister's pay level.

57. It is a common issue that politicians (and by extension, ministers) are viewed as too well paid for what they do, even though it is clear when assessed by professionals in the field that they are paid far less than private sector executives having similar or lesser responsibilities.

Exhibit 10: Summary of Country Practices

History	Process	Factors	Structure
<p>Australia</p> <p>The Remuneration and Allowances Act 1990 linked the salary for Senators and MPs to minimum award salary of a middle ranking senior executive in the Australian Public Service. In turn, the salary of Principal Executive Officers are determined by a Remuneration Tribunal.</p>	<p>The Remuneration Tribunal is an independent statutory body that determines remuneration for key Commonwealth offices. The Tribunal reviews salaries annually, though it does not always recommend changes. The recommendations of the Tribunal are noted by Parliament.</p>	<p>In considering remuneration and allowances of MPs, the Tribunal considers</p> <ul style="list-style-type: none"> • The nature of the jobs that they perform • The conditions under which the work is performed • How the job compares with similar jobs in other sectors (with particular emphasis on relativity between federal, state and local positions) • The principles governing workplace relations policies. 	<p>The package for PM and ministers is comprised of base salary and a complex system of allowances related to costs of operating an office and travelling between Canberra and the home constituency.</p> <p>Pay for PM and ministers is set equal to the MP pay plus a pay differential related to the relative complexity of the positions.</p>
<p>Canada</p> <p>Until the early 1990s, MPs reviewed and revised their own pay. Because of negative public reaction, reviews were infrequent and ad hoc.</p> <p>In 1993, the federal government commissioned an outside review of MPs remuneration resulting in recommendations on reference points and process for establishing remuneration levels.</p>	<p>Under law, an independent commission must be formed within six months of each general election to review compensation of MPs. The most recent review was completed in Spring 2001 after the November 2000 general election. The commission’s recommendations were approved by Parliament and establish a linkage between pay for PM and the Chief Justice.</p>	<p>The PM’s total remuneration is set equal to the Chief Justice total remuneration. All cabinet ministers will be paid 74% of the PM’s remuneration, and MPs will be paid 50% of the PM’s remuneration. Remuneration will be adjusted annually for inflation, equal to the Industrial Aggregate inflation rate – the same factor used to adjust the pay of the Chief Justice.</p>	<p>MPs receive a base salary, pension, insurance, and severance allowance upon leaving office based on service, as well as liberal free air and rail travel provisions to visit their constituents.</p> <p>The retirement arrangements are generous by comparison to private sector, since they are credited with 3% to 4% per year of service. No elected official receives any housing privilege, with the exception of certain government-owned residences set aside for the prime minister and others.</p>

Exhibit 10, continued: Summary of Country Practices

History	Process	Factors	Structure
<p>Finland</p> <p>Parliament provides the statutory basis for the State's personnel and labor-market policies and approves the basic guidelines and agreements on personnel policy. Pay for ministers is a combination of the system for civil servants and for members of parliament.</p>	<p>The salary schedules and other employment terms of State employees are agreed in the Collective Agreement for State Civil Servants and Employees under contract. Increases have usually followed the rate of inflation according to provisions set down by law. Annual adjustments of salary form part of the government's operating budget, which is subject to parliamentary approval.</p>	<p>In the State salary schedule, the ministers are positioned in grade 34 (of 36) and the prime minister's salary is 20 % higher. Salaries are increased if the collective agreement gives an increase in this grade.</p> <p>The pay practices in the private sector do not directly influence on civil servants' or ministers' salaries.</p>	<p>The remuneration of the civil servants and ministers are based on a ranking determined by Parliament and consists of:</p> <p>Basic salary and Age allowance</p> <p>Ministers also receive compensation of costs relating to expenses of performing the role.</p>
<p>Netherlands</p> <p>In the 1980s a rule was formulated that ministers, including the prime minister, should not earn more than six times the minimum wage. In fact, the ratio has been increased somewhat but the principle of the rule is still in place.</p>	<p>There is no independent review body for setting pay, and salary adjustments follow civil service collective bargaining agreements. Parliament is accountable for determining remuneration policies and practices, but it has not been discussed in many years.</p>	<p>For civil servants, a collective labour agreement is negotiated by the Ministry of the Interior with the labour unions. The negotiated pay rise is then also applicable to the MPs and ministers. Besides the rule on multiples of the minimum wage, there are no guidelines or policies about determination of remuneration for ministers.</p>	<p>Compensation for ministers consists of a fixed base salary and expense allowances. They are participants in the civil service retirement scheme.</p>

Exhibit 10, continued: Summary of Country Practices

History	Process	Factors	Structure
<p>New Zealand</p> <p>In 1973, the Royal Commission upon Parliamentary Salaries and Allowances established that the occupation of an MP is virtually full-time and professional, that the role of MP is the sole source of income, and that there are sacrifices made by the MP and his or her family that must be recognized in determining remuneration.</p>	<p>The Higher Salaries Commission is accountable for determining pay of ministers, MPs, and senior officials of the government. HSC comprises three independent commissioners appointed by the Governor-General for three-year terms. The HSC conducts reviews annually and its recommendations are implemented without parliamentary review.</p>	<p>The HSC must set remuneration having regard to the requirements of the job and the conditions and remuneration paid to those in comparable positions, taking into account:</p> <ul style="list-style-type: none"> • the need to achieve and maintain fair relativity with the levels of remuneration received elsewhere; • the need to be fair both- to the persons whose remuneration is being determined and to the taxpayer; and • the need to recruit and retain competent persons. 	<p>Pay consists of base salary plus a range of specific non-taxable allowances. Some of these allowances may be considered remuneration – housing for ministers, basic allowance, whilst some – constituency allowance - are intended to serve as reimbursements of costs incurred in the service of constituents.</p> <p>This structure is inconsistent with private sector practice as encouraged by government policy and is now subject of discussion.</p>
<p>Singapore</p> <p>The current system is based on a 1994 White Paper on Competitive Salaries for Competent and Honest Government. The system was established to ensure that Officers in key government positions are paid salaries that are competitive with those of professionals in the private sector.</p>	<p>A review is conducted by the Public Service Division every five years, with the last review being conducted in July 2000. The results of the review are debated at Parliament and a bill must be passed to implement the recommendations.</p> <p>Administrative Service salary levels are adjusted annually based on the recommendation of the National Wage Council. The NWC is made up of officials, industry leaders, and private sector representatives.</p>	<p>Pay is based on establishing a competitive position with the private sector, specifically top earners from six professions - Bankers, Engineers, Accountants, Lawyers, CEOs of Multinationals and CEOs of local manufacturing firms.</p> <p>Pay for the first level of minister is set at 2/3 the Median Principal income of the top eight individuals from each of the six professions. The pay for Administrative Service – Superscale G is set at the pay of the 15th highest paid person who is 32 years old and belongs to the six professions above.</p>	<p>Remuneration is comprised of Base Salary, GDP-Related Bonus and Performance Bonus. Base salary represents 60% of total remuneration, and the Annual Variable Component and the Performance Bonus represent 40% of Total Remuneration.</p> <p>Annual variable component is based on performance of the Singapore economy, and the Performance Bonus is based on individual performance rating.</p>

Exhibit 10, continued: Summary of Country Practices

History	Process	Factors	Structure
<p>United Kingdom</p> <p>The process and principles of remuneration for ministers in UK has been broadly stable for many years.</p> <p>Work in Government or Parliamentary office is considered to bring rewards other than salary. Nevertheless, ministerial pay should be reasonably competitive to public sector pay levels.</p>	<p>Every three years, the PM commissions the Senior Salaries Review Body (SSRB) to review ministerial and parliamentary pay allowances. The SSRB also reviews pay of senior civil servants, equivalent ranks in the armed forces, and the judiciary.</p> <p>Recommendations are provided to the PM who then decides when to publish the paper and present it to Parliament for debate. Pay levels and pension arrangements for ministers and members of Parliament have to be agreed by the House of Commons, as have MPs' office and staff support allowances.</p>	<p>The SSRB seeks to ensure that pay and pension levels are sufficient that suitable candidates are not deterred from entering public life and has attempted to ensure that ministerial pay remains broadly comparable to that of relevant positions in various parts of the public sector. It is accepted that tracking private sector practices, even on base salaries, is not practical in the UK.</p> <p>In the interim of major reviews, ministerial pay is adjusted according to inflation in line with civil service adjustments.</p>	<p>Pay is limited to a fixed base salary, a pension, and the use of facilities (including in many cases accommodation) which are 'attached' by custom and practice to specific offices.</p> <p>There is also a system of allowances which are intended to compensate for expenses related to performance of the duties of a minister or member of parliament. Examples of allowances include secretarial support, research support, office running costs, transportation to home constituency, and housing allowance if home constituency is not in London area.</p>

Exhibit 10, continued: Summary of Country Practices

History	Process	Factors	Structure
<p>United States</p> <p>Salaries of top-level Executive Branch officials of the U.S. Federal government are statutorily linked to the salaries of Members of Congress who are responsible for setting pay for these positions. The framers of the Constitution placed the responsibility of setting pay of the top-level Executive Branch officials, as well as its own and of the President, to Congress.</p> <p>Congress enacted the Ethics Reform Act of 1989 due to growing concern over the Federal government’s ability to recruit highly qualified replacements. The Act restored two cost-of-living adjustments, comparability pay adjustment, and amended the Federal Salary Act and the Adjustment Act in two respects:</p> <ul style="list-style-type: none"> • establishing a Citizens’ Commission on Public Service and Compensation and • revising the mechanism for fixing the annual pay adjustments for judges, Members of Congress and top-level Executive officials. <p>This process has never become functional because no funds have ever been appropriated.</p>	<p>Federal employees are classified into categories according to position. The top-level Executive Branch officials are under the Executive Schedule pay system, which is a five-tier structure from Level I (highest salary) through Level V (lowest salary). Their salary is linked to the salary of the Members of Congress who are responsible for setting the pay of these top-level officials.</p> <p>The President presents salary recommendations for the top-level officials and these are either approved or rejected by Congress. By law, Executive Schedule pay is supposed to rise each year at the same rate as other Federal government employees (who are on the General Schedule), but Congress has voted each year to block Executive Schedule raises since 1993, except for 1998, 2000 and 2001.</p>	<p>Under current law, there are three ways to adjust pay of top-level officials:</p> <ol style="list-style-type: none"> (1) allow automatic and annual pay adjustments based on changes in the Employment Cost Index (ECI); (2) adopt pay raises recommended by the President to Congress, based on the report of the Citizens’ Commission to review and consider salaries of high-level Federal officials; or (3) pass special legislation authorizing a pay raise. <p>Private sector pay practices are not reviewed nor do they influence the pay levels of top-level Federal officials.</p>	<p>There is no variable compensation or non-accountable allowances. In addition, these officials are not provided with housing or housing allowances and no other significant benefits are provided.</p> <p>Federal executives, including Members of Congress and Cabinet Secretaries, are covered by the benefits package that applies to all Federal employees. The most important parts of the package are:</p> <ul style="list-style-type: none"> • A contributory retirement plan that pays approximately two-thirds of salary for a full career (35 years of service). Officials can first retire from 55 to 62 depending on years of service. • A choice of health plans that reimburse about 80 percent of covered health care expenditures. The health plan eligibility is carried into retirement. • A life insurance plan providing a benefit approximately equal to salary. • Annual leave of up to six weeks a year depending on service.

International Ministerial Remuneration Comparisons

58. Exhibit 11 summarizes the pay levels of ministers, members of parliament or congress, and top levels of the civil service for the selected countries. The exhibit shows that, excluding Singapore, ministerial pay ranges from HK\$640,000 (Finland) to HK\$1,877,000 (UK prime minister) or HK\$3,120,000 (US President). Singapore is exceptional, with pay rates for the prime minister at over HK\$8.6m and for a cabinet-level minister at over HK\$6.1m.
59. The table indicates that, except for Singapore and the US, prime minister pay varies between 84% and 100% of the top civil servant's pay. Cabinet minister pay varies between 60% and 100% of this reference level. Among the selected countries, only Singapore and US pay higher for cabinet level positions than for top civil servants. In the other countries, most cabinet ministers are members of parliament. In US cabinet secretaries are appointed by the President and are not members of Congress. In Singapore, some ministers are members of Parliament but many are appointed from private sector, other public sector corporations, or from the civil service.
60. Besides receiving salaries, ministers in many of the countries also receive allowances. These allowances are intended to compensate for costs incurred in performance of duties of the job, so are not considered remuneration and are excluded in Exhibit 11. An example of a reimbursement-related allowance would be travel allowances to compensate an MP or minister for travel costs between the capital and his or her home area. However, some of the allowances paid to New Zealand ministers do not appear to be cost reimbursements and have been included as remuneration in the analysis.

Exhibit 11: International Comparison of Ministers' Remuneration to Top Civil Servants (HK\$000) (1)

	Australia	Canada	Finland	Netherlands	New Zealand	Singapore	UK	US
Prime Minister	1,031	1,326	768	812	1,018 (4)	8,658 (5)	1,877	3,120 (6)
Minister (2)	684	982	640	812	722 (4)	6,165 (5)	1,362	1,258
MP	396	663	480	619	333 (4)	732 (5)	588	1,132
Civil Servant	396 – 2,070 (3)	1,436	852	815	1,205	3,910 (5)	1,929	1,043
PM as % of Top Civil Servant	83% (7)	92%	90%	100%	84%	221%	97%	299%
Minister as % of Top Civil Servant	55% (7)	68%	75%	100%	60%	158%	71%	121%

Notes:

(1) Exchange rates as of August 30, 2001

(2) Minister – Cabinet level minister. Australia has higher level for Treasurer, Singapore has higher level for deputy prime minister. These levels not shown.

(3) Australia principal executive officer pay is set individually based on relative work value of jobs.

(4) New Zealand includes cash allowances that are viewed as remuneration (e.g., day allowances, housing allowances where it is not considered necessary to maintain two homes to serve a local constituency). For other countries, most allowances related to expenses of public service and are not included.

(5) Singapore remuneration includes targeted total earnings levels.

(6) US President base salary; also receive US\$50,000 expense allowance and US\$100,000 travel allowance in addition to official travel.

(7) Australia relative percentage based on midpoint of range for Australia Principal Executive Officers, or A\$300,000 per annum.

Appendix 1: List of organisations selected for invitation to survey

Private Sector Organisations

Organisation	Industry Group
A S Watson	Retail and wholesale distribution and trading
AIA	Insurance
Alcatel China	Telecom, IT/HT
Allianz	Insurance
Amway China	Consumer Product
AT&T Asia Pacific	Telecom, IT/HT
AXA China Region	Insurance
Bank of East Asia	Financial Services
BAT	Others
Caltex	Others
Cathay Pacific Airways Ltd	Transport
Chevalier Construction	Construction
CITIC Pacific Ltd	Diversified Companies
CLP Holdings Ltd	Utilities
CMG Asia Ltd	Insurance
Dah Sing Financial Group	Financial Services
Dairy Farm	Retail and wholesale distribution and trading
DHL International (HK)	Transport
DuPont China	Others
Edward Keller	Retail and wholesale distribution and trading
Esprit Holdings Ltd	Retail and wholesale distribution and trading
Gammon Construction	Construction
Giordano Intl	Retail and wholesale distribution and trading
Goldman Sachs	Financial Services
Great Eagle Properties Holdings Co. Ltd.	Property
HACTL	Transport
HAECO	Other
Hang Lung Development Co. Ltd	Property
Hang Seng Bank	Financial Services
Henderson Development Co. Ltd	Property
Hong Kong & China Gas	Utilities
Hong Kong & Shanghai Hotels	Other
Hong Kong Electric Holdings	Utilities
Hong Kong Exchanges and Clearing	Financial Services
Hong Kong Land Co., Ltd	Property
HSBC Holding	Financial Services
Hutchison Whampoa Ltd	Diversified Companies
Hysan Development Co. Ltd	Property
IBM China / Hong Kong	Telecom, IT/HT
i-CABLE Communication Ltd	Telecom, IT/HT
ING Asia Pacific	Insurance
Jardine Matheson	Diversified Companies
Johnson Electric Holdings Ltd	Retail and wholesale distribution and trading
JP Morgan	Financial Services
K.Wah Group	Construction/Architecture/Surveying
Kowloon Motor Bus	Transport
Lam Soon (HK) Ltd	Consumer Product

Appendix 1: List of organisations selected for invitation to survey

Private Sector Organisations

Organisation	Industry Group
Li & Fung Ltd	Diversified Companies
Manulife (Int'l) Ltd	Insurance
Merck Sharpe & Dohme	Others
Merrill Lynch	Financial Services
Modern Terminals Ltd	Transport
New World Services	Diversified Companies
New World Telephone	Telecom, IT/HT
Nortel Networks (Asia Pacific)	Telecom, IT/HT
OOCL (HK) Ltd	Transport
Pacific Century Cyber Works Ltd	Telecom, IT/HT
Pacific Century Insurance Co., Ltd	Insurance
Pepsi Asia Pacific	Others
Prudential Corporation Asia	Insurance
Quality Healthcare	Others
Shangri-la Asia Ltd	Others
Shell	Others
Shui On Properties Ltd	Property
Shun Hing Electronic Trading Co., Ltd	Retail and wholesale distribution and trading
Siemens	Telecom, IT/HT
Sime Darby Group	Diversified Companies
Sino Land Co., Ltd	Property
South China Morning Post H Ltd	Others
Standard Chartered	Financial Services
Sun Hung Kai Development (China)	Property
Swire Pacific Ltd	Diversified Companies
Television Broadcasts Ltd	Others
UPS Parcel Delivery Service	Transport
Wharf	Diversified Companies
Wheelock and Co. Ltd	Diversified Companies
Wing On Co., Ltd	Retail and wholesale distribution and trading

Appendix 1: List of organisations selected for invitation to survey

Professional Firms

Organisation	Industry Group
Accenture	Consulting (IT/Strategy/HR)
Allen & Overy	Legal
Andersen Business Consultants	Consulting (IT/Strategy/HR)
Arthur Andersen	Accounting
ARUP & Partners HK Ltd	Engineering/Architecture/Surveying
AT Kearney Asia Pacific	Consulting (IT/Strategy/HR)
Atkins China Ltd	Engineering/Architecture/Surveying
Bain & Company (Hong Kong)	Consulting (IT/Strategy/HR)
Baker & Mckenzie	Legal
BDO McCabe Lo & Co	Accounting
Binnie Black & Beatch HK Ltd	Engineering/Architecture/Surveying
Boston Consulting Group, The	Consulting (IT/Strategy/HR)
Burson-Marstellar	Communications
CB Richard Ellis	Real Estate
Centaline Properties	Real Estate
Chesterton Petty	Real Estate
Clifford Chance	Legal
Colliers Jardine (HK) Ltd	Real Estate
Deacons	Legal
Deloitte Touche Tohmatsu	Accounting
Ernst & Young	Accounting
Foster Partners Asia	Engineering/Architecture/Surveying
FPD Savills	Real Estate
Grant Thornton	Accounting
Halcrow China Ltd	Engineering/Architecture/Surveying
Hill & Knowlton	Communications
J Walter Thompson	Communications
Johnson Stokes & Master	Legal
Jones Long LaSalle	Real Estate
KPMG Consulting Asia Limited	Consulting (IT/Strategy/HR)
KPMG Peat Marwick	Accounting
Kwok & YIH	Legal
Leo Burnett	Communications
Linklaters	Legal
Maunsell Consultants	Engineering/Architecture/Surveying
McKinsey	Consulting (IT/Strategy/HR)
Ogilvy & Mathers	Communications
PA Consulting	Consulting (IT/Strategy/HR)
Parsons Brinckerhoff (Asia)	Engineering/Architecture/Surveying
Paul, Weiss, Rifkind, Wharton & Garrison	Legal
Pricewaterhouse Coopers	Consulting (IT/Strategy/HR)
PricewaterhouseCoopers	Accounting
Richard Butler	Legal
Scott Wilson	Engineering/Architecture/Surveying
Simmons & Simmons	Legal
Skidmore Owings & Merrill	Engineering/Architecture/Surveying
Vigers Hong Kong Ltd	Real Estate
Watson Wyatt	Consulting (IT/Strategy/HR)
William M Mercer	Consulting (IT/Strategy/HR)
Woo, Kwan Lee & Lo	Legal

Appendix 1: List of organisations selected for invitation to survey

Public Organisations

Organisation	Industry Group
Airport Authority Hong Kong	Public Sector
HK Trade Development Council	Public Sector
Hong Kong Housing Society	Public Sector
Hong Kong Jockey Club	Public Sector
Hong Kong Monetary Authority	Public Sector
Hong Kong Mortgage Corporation	Public Sector
Hospital Authority	Public Sector
KCR Corporation	Public Sector
Mandatory Provident Fund Schemes Authority	Public Sector
MTR Corporation	Public Sector
The Securities and Futures Commission of HK	Public Sector
Tung Wah Group of Hospitals	Public Sector
Urban Renewal Authority	Public Sector

Appendix 2: Overview of LTI Valuation Methodology

Long-Term Incentives (LTI) are incentive arrangements designed to reward an individual for performance over a period longer than one year. Generally, the compensation value of these plans is dependent upon future performance – of the individual, the company, or the stock price of the company.

Types of Plans

Stock Option Plans. Stock option plans provide an individual with the right to purchase a specified number of shares of company stock for a specified price.

Performance Unit Plans. These plans are awarded units usually equal to \$1.00 with payouts based on performance over a specified period. Awards are expressed as a “target” number and payout varies based on actual performance and is paid in cash.

Restricted Stock Plans. In these plans, awards are made in the forms of shares of company stock. Shares are actually transferred to the employee at no cost, but the shares carry restrictions such as prohibitions against disposition or rights of first refusal, and they be subject to substantial risk of forfeiture.

Other Terms

Exercise – using a stock option grant to purchase a specified number of stock shares for a specified price.

Grant Value – the total dollar value of a stock-based award (the number of shares multiplied by the per-share stock price at market value).

Grant – the act of transferring the potential value of a long-term incentive program from employer to employee, or the target value of such award at time of conveyance.

Vesting – conveying to an employee the legal right to receive the value of a long-term incentive award, regardless of employment status.

Methodology

Stock Options. Hay Group uses the Expanded Black-Scholes stock option valuation model. The model shows the impact of dividends, vesting schedules, exercise period, and grant frequency on value of options. The table shows inputs into the valuation model and their impact on value – up, down or indeterminate.

Phase I Report – Remuneration of Principal Officials

Model Inputs	Characteristics	Impact on Value
Stock Price	High	↑
	Low	↓
Exercise Price	At market value	–
	Discounted	↑
	Premium	↓
Volatility of Share	High	↑
	Low	↓
Dividends	High	↓
	Low	↑
Interest Rates	High	↑
	Low	↓
Option Term	Short	↓
	Long	↑
Vesting	Short	↑
	Long	↓

Restricted Stock. The restricted stock valuation begins as outright stock and is then discounted for probability of forfeiture. Probability of forfeiture is based on actuarial data for different types of termination. The table below shows the various inputs into the valuation model and their impact on the value.

Model Inputs	Characteristics	Impact on Value
Stock Price	High	↑
	Low	↓
Dividends	Paid	–
	Not Paid	↓
Vesting	Short	↑
	Long	↓

Performance Units. The performance unit valuation is discounted for the time value of money, as well as probability of forfeiture, volatility of performance, and limited upside potential. The probability of forfeiture is carried over the length of the performance period and disposition of grant upon termination. The table below shows the inputs into the valuation model and their impact on the value.

Model Inputs	Characteristics	Impact on Value
Maximum Payout	Above Target	↑
	At Target	↓
Volatility of Share	High	↓
	Low	↑
Performance Period	Short	↑
	Long	↓

The following table shows the actual valuation factors being used within this study.

LTI Features	Factor
<p><i>Standard Stock Option Assumption:</i></p> <p>Vesting schedule - 25% each year for four years (four-year ratable vesting), no performance hurdle, exercise price = 100% fair market value</p>	<p>0.35</p>
<p><i>Alternative Stock Option Assumptions:</i></p> <p>Performance hurdle - Example, Earnings per Share must grow by 3% more than inflation for a three-year period</p> <p>Infrequent Grants</p> <p>One-off grant</p> <p>Discount on exercise price: Exercise price = 80% of fair market value on date of option grant</p>	<p>Multiply above factor by 0.6</p> <p>Divide factor above by frequency (e.g., divide by 2 if granted every other year)</p> <p>Divide factor above by 4 (assume grant made every four years)</p> <p>Multiply factor above by 1.28</p>
<p><i>Performance Share Plan:</i></p> <p>Vesting schedule: 100% after four years</p>	<p>0.79</p>
<p><i>Performance Unit Plan:</i></p> <p>Vesting schedule: 100% after three years</p>	<p>0.59</p>

Small differences in vesting schedule such as three-year vesting or five-year vesting result in small differences in valuation factor, so it is sufficiently accurate for purposes of this study to use one valuation for all stock option schemes.

However, Hay Group will make adjustments where differences in schemes create large value in differences. For example, if there is a discount on the exercise price then the value of the option is much higher than the standard valuation of 0.35. When discounts are applied in Hong Kong, the exercise price is usually 80% of the Fair Market Value on the date of grant.

The option valuation of 0.35 also assumes that the grants are made annually. Where this is not the case, Hay Group divides by the frequency which significantly reduces the value of the long-term incentive scheme.

Using a similar theoretical approach, Hay Group can also apply a standard valuation factor for Performance Share Plans or Performance Unit Plans. These plans have higher values because the executive does not have to pay the exercise price to obtain the shares or cash payments made upon vesting in these schemes. The valuation factors reflect the probability of remaining an employee until the scheme matures as well as the risk of achieving the performance targets of the scheme.

The table below shows an example how the factors were used. In the example, the individual receives a one-off option grant of 1,000,000 shares with a vesting schedule of three years on a ratable basis. The fair market value at time of grant is \$10 per share, but the exercise price is set at 80% of the fair market value, or \$8 per share. We use the standard valuation factor of 0.35 even though the vesting schedule is slightly better than the standard assumption on vesting schedule. We multiply this factor by 1.28 to reflect the discount on the exercise price relative to the market price when the share was granted, and then divide the result by 4 because it is a one-off option grant (the standard valuation factor applies for an annual grant). The resulting factor of 0.112 is then multiplied by the grant size (\$10,000,000) to yield an annualized valuation of \$1,120,000. This amount would be included in the total remuneration results of the survey.

LTI Features	Value
<i>Plan features:</i> 33% each year for three years, no performance hurdle, exercise price = 80% fair market value, one-off grant	
Grant size – 1,000,000 shares at \$10 per share	Grant value = 1,000,000 x \$10 = \$10,000,000
<i>Option valuation factor:</i> Basic valuation factor:	0.35
times premium for discount to fair market value:	1.28
divided by frequency of grant (assume every four years for one-off grant):	4
Overall factor:	$0.35 \times 1.28 / 4 =$ 0.112
Annualized option value (as included in survey)	$\$10,000,000 \times 0.112 =$ \$1,120,000

Appendix 3: Definition of Remuneration Terms

Remuneration Components

Base Salary. The annual total of monthly base salary payments, including guaranteed bonuses such as 13th month.

Housing. Guaranteed cash allowances denominated separately from base salary or the amounts paid directly by the employer for renting accommodation.

Guaranteed Cash Compensation. The sum of base salary and housing. This amount represents the cash, or cash equivalent compensation, that the employee receives regardless of performance or other conditions.

Short-Term Incentive. Compensation that is paid in relation to performance of the individual or company over a period of one-year or less.

Total Earnings. The sum of guaranteed cash compensation plus short-term incentives.

Long-Term Incentive. Incentive arrangements designed to reward an individual for performance over a period longer than one year. The amount shown is the annualized value of the grant received in the current year based on a valuation model, not gains realized in the current year.

Total Direct Compensation. Total Earnings plus the annualized value of long-term incentives.

Retirement. The company cost of contributing to a retirement scheme. Schemes include defined contribution (provident fund), defined benefit (final salary scheme), and contractual gratuity. In cases where only the statutory minimum contribution to MPF is made, these amounts have been excluded.

Provident Fund. Company contribution percentage is used to multiply base salary.

Final Salary. Final salary schemes usually take the form of

Factor x Final Salary x Number of Years of Service.

Company contribution percentage is estimated according to the following table:

Final Salary Factor	Employer Contribution Rate
1.50	10.3%
1.75	12.0%
2.00	13.7%
2.50	17.2%
3.00	20.5%

Total Remuneration. Total Direct Compensation plus retirement contribution. Total Remuneration would normally include costs of providing other benefits and perquisites. These items are being considered separately in terms of prevalence.

Statistics

Compensation levels are defined in terms of percentiles and averages. To protect confidentiality of data, a minimum number of data points are required to calculate a particular percentile. These are also indicated below.

P90 (90th percentile, upper decile) – the value that separates the highest ten percent of values from the lower 90 percent of values. At least 13 data points must be present to calculate a decile.

P75 (75th percentile, upper quartile, 3rd quartile) – the value that separates the highest 25 percent of values from the lower 75 percent of values. At least 8 data points must be present to calculate a quartile.

P50 (50th percentile, median) – the value that separates the upper half of values from the lower half of values. At least 4 data points must be present to calculate the median.

P25 (25th percentile, lower quartile, 1st quartile) – the value that separates the lowest 25 percent of values from the higher 75 percent of values. At least 8 data points must be present to calculate a quartile.

P10 (10th percentile, lower decile) – the value that separates the lowest ten percent of values from the higher 90 percent of values. At least 13 data points must be present to calculate a decile.

Average – the arithmetic mean of all values. At least 3 data points must be present to calculate an average.

**Appendix 4:
Summary of Overseas Remuneration Practices for Ministers**

Summary of Practices on Ministerial Remuneration: Australia

History

The Remuneration and Allowances Act 1990 linked the salary for Senators and MPs to minimum award salary of a middle ranking senior executive in the Australian Public Service. In turn, the salary of Principal Executive Officers are determined by a Remuneration Tribunal.

The Remuneration Tribunal is an independent statutory body that determines remuneration for key Commonwealth offices. The tribunal consists of three part-time members appointed by the Governor-General. Its role is to report on or determine the remuneration of members of the Federal Parliament, additional salaries for ministers and Parliamentary office-holders, and Judges of federal courts, most full-time and part-time holders of public offices and principal executive officers.

The Remuneration Tribunal must meet every year to review pay levels, though there will not necessarily be increases in a given year. The Remuneration Tribunal's recommendations are "noted" by Parliament and could be rejected though that does not normally occur.

Factors

In considering remuneration and allowances of MPs, the Tribunal considers

- The nature of the jobs that they perform
- The conditions under which the work is performed
- How the job compares with similar jobs in other sectors (public sector, including state and local government as well as agencies majority funded by government; and private sector including CEO's and direct reports)
- The principles governing workplace relations policies

More specifically, factors considered include:

- Work value – the complexity of the work of senators and members, ministers and parliamentary office holders, their responsibilities and accountabilities, and their contribution to a better governed and more prosperous nation.
- Productivity – the range of duties undertaken by senators and members, ministers and parliamentary office holders and changes in the quantity and quality of the various key outputs they deliver, including legislative, executive and management outputs.
- Total remuneration – in considering the salaries of senators and members, ministers and parliamentary office holders, the Tribunal has taken into account their total remuneration package, which includes superannuation and a private-plated motor vehicle.
- Community wage and salary movements and remuneration trends in specific market segments, especially the public sector.

As of July 1, 2001, the tribunal set the minimum pay for a Band 1 principal executive officer at A\$95,600 per year and recommended that the pay for an MP be set at that level. This amount is subject to annual adjustment in accordance with the Average Weekly Ordinary Time Earnings index over the previous 12 months. Band 1 Principal Executive Officers are usually heads of Commonwealth Agencies, or in case of the largest agencies, may be found in the second level. Principal executive officers are on individual contracts. The total

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remuneration of a principal executive officer could range up to A\$500,000 per annum, depending on the value of work as determined by the Remuneration Tribunal.

Minister's pay is set relative to this level, taking into account pay and relative work value for other state and federal government officials:

Pay Levels (A\$)

Position	Fixed Remuneration (1)
Prime Minister	\$248,560
Deputy Prime Minister	\$195,980
Treasurer	\$179,250
Other Cabinet Minister	\$164,910
Other Ministers	\$150,570
MP	\$95,600
Top Civil Servant (2)	\$95,600 – about \$500,000

Note: (1) Fixed remuneration does not include allowances.

(2) For Top Civil Servant, amounts are total cash; a portion may be subject to performance

Structure

The package for PM and ministers is comprised of base salary and a complex system of allowances related to costs of operating an office and travelling between Canberra and the home constituency. Ministers receive a range of allowances that must be related directly to performance of the job. These allowances are not considered to be remuneration and include:

Uncapped entitlements	Capped/Restricted Entitlements		
	Dollar Limit	Occurrences Limit	Content Limit
<ul style="list-style-type: none"> • Travelling allowance (other than within own jurisdiction) • Scheduled travel • Car transport • Private vehicle allowance • Office and residential telephone services • Personalised letterhead stationery, newsletters and other printed material • Retirement travel (pre 1 Jan. 1994 entitlements) • Other non-salary entitlements (per the confidential Ministers of State Entitlements Handbook) 	<ul style="list-style-type: none"> • Salary • Electorate allowance • Charter transport • Information delivery services • Overseas study trips • Pooled spouse and dependant travel 	<ul style="list-style-type: none"> • Travelling allowance (within electorate) • Non-official spouse/nominee and dependent travel • Retirement travel (post 1 Jan. 1994 entitlements) • Newspapers & periodicals 	<ul style="list-style-type: none"> • Staff • Office accommodation, equipment, supplies • Privately plated vehicles • Photographic services • Constituents request program • Overseas delegations travel

Ministers are also entitled to the most generous defined-benefit superannuation scheme in Australia, paying up to 11.5% into the scheme compared to highest levels in private sector of 9%. MPs can receive an annual pension or a lump sum payment based on the

accumulated value of the superannuation scheme when leaving service after completing three terms or eight years.

Issues

Annual pay increases are set in accordance with wage inflation, but public criticism has been harsh whenever there are increases in parliamentary remuneration or allowances. The generous superannuation scheme also has been subject to much controversy.

Summary of Practices on Ministerial Remuneration: Canada

History

Until the early 1990s, MPs reviewed and revised their own pay. Because of negative public reaction, reviews were infrequent and ad hoc. The result was the erosion of pay levels relative to market practices over the 1970s and 1980s.

The federal government as well as the two largest provincial governments (Ontario and Quebec) decided to experiment with a process that would be less political by involving outside parties.

In 1993, the federal government commissioned an outside review of MPs remuneration resulting in recommendations on reference points for establishing remuneration levels:

1. An internal comparison with senior levels of the Federal Public Service (civil service)
2. A basket of reference positions in the Canadian market – mainly in the not-for-profit sector and a few in the private sector
3. A group of six developed countries, as an international comparison (US, Sweden, UK, France, Australia and Belgium).

The study also recommended that an independent commission be established to undertake further periodic reviews.

Process

Under law, an independent commission must be formed within six months of each general election to review compensation of MPs. The most recent review was completed in Spring 2001 after the November 2000 general election.

The commission's recommendations were approved by Parliament and establish a linkage between pay for PM and the Chief Justice. The pay for Chief Justice is reviewed every four years (next in 2003) by an independent commission consisting of

- One member appointed by the Minister of Justice
- One member appointed by the Judicial Council, and
- One member, who will serve as Chairman, selected by the other two appointed members.

The commission determining Chief Justice pay does not disclose the criteria used in reaching its decisions, nor does it disclose what market references may be used in the process. Parliament must approve the changes proposed for Chief Justice unless a concrete reason can be cited. If the package is rejected, then the issue would be settled in the courts.

As a consequence of these recommendations, the commission on minister's pay has passed accountability for setting the exact level of the PM's remuneration to the commission on remuneration for the judiciary.

Factors

The PM's total remuneration is set equal to the Chief Justice total remuneration. All cabinet ministers will be paid 74% of the PM's remuneration, and MPs will be paid 50% of the PM's remuneration. The relative levels of pay are the judgement of the commission and the precise factors leading to these recommendations are not public information. Remuneration will be adjusted annually for inflation, equal to the Industrial Aggregate inflation rate – the same factor used to adjust the pay of the Chief Justice.

Structure

MPs receive a base salary, pension, insurance, and severance allowance based on service, as well as liberal free air and rail travel provisions to visit their constituents. The severance allowance, which is equal to 50% of a year's salary, is paid to MPs or ministers upon losing their seats unless they have served more than six years, in which case they are eligible to receive a pension. The retirement arrangements are generous by comparison to private sector, since they are credited with 3% to 4% per year of service (depending on year they were originally elected). No elected official receives any housing privilege, with the exception of the government-owned residences set aside for the prime minister, official leader of the opposition, and the speaker of the House of Commons. The only other significant perquisite for PM and cabinet ministers is chauffeur-driven car and use of government-owned jets for official business.

Pay Levels (C\$)

Position	Fixed Remuneration	Performance-Related Pay
Prime Minister	\$262,900	-
Minister	\$194,600	-
MP	\$131,400	-
Top Civil Servant	\$209,300 - \$246,300	25% of base

Note: Fixed remuneration does not include allowances.

Issues

Whilst pay levels for politicians including ministers are much lower than private sector, public perception remains that they are overpaid. Despite the establishment of the independent commission, public perception has remained unfavorable. The new arrangement – reference to Chief Justice pay – may help to resolve some of those perceptions.

The province of Ontario is now reviewing legislation to give the Provincial Integrity Commissioner the complete and final authority for setting pay levels for the provincial premier, ministers, and MPs. These recommendations will not be subject to any political review and cannot be ignored or overridden. This experiment may serve as a model for determination of remuneration at federal levels as well.

Summary of Practices on Ministerial Remuneration: Finland

History

As the holder of legislative and budgetary powers, Parliament provides the statutory basis for the State's personnel and labor-market policies and approves the basic guidelines and agreements on personnel policy. Since the 1980's the Government has taken a more prominent role in drafting the central guidelines of State's employer and personnel policy. Successive Government programs have also occupied a more visible role in decision-making.

Pay for ministers is a combination of the system for civil servants and for members of parliament.

Process

The salary schedules and other employment terms of State employees are agreed in the Collective Agreement for State Civil Servants and Employees under contract. The contract is made between the State Employer's Office and the trade unions concerned. The state salary schedules are reviewed usually once a year. The increases have usually followed the rate of inflation and the government may also adjust taxation policies so that the level of real income is maintained.

The positions of senior civil servants in the ministries are based on legislation. When the position is established its title and the grade in the State salary schedule is determined. The State salary schedules, detailing also the age bonuses and cost of living compensation, are reviewed by grades.

The position of ministerial positions in the State salary schedule is set by law, whilst the annual adjustment process is set down in law. The contract agreed between the State Employer's Office and the trade unions forms part of the budget, which is reviewed by Parliament.

Factors and Structure

In the State salary schedule, the ministers are positioned in grade 34 and the prime minister's salary is 20 % higher. Their salaries are increased if the collective agreement gives an increase in this grade. Regardless of the period of the service in the public administration, the ministers receive automatically five age bonuses out of a maximum of six in the civil service system.

The pay practices in the private sector do not directly influence on civil servants' or ministers' salaries. Indirectly the private sector may cause pressures to bigger reviews in the State salary schedules but bigger changes take effect slowly. Civil service salary schedules and grades have been always public, only the pay increase based on the personal performance is confidential. The pay transparency is one of the factors that makes bigger reforms slow due to lack of public money, public positions and public opinion.

The salaries of the civil servants and ministers are based on the titles, which describe the demands of the position but not necessarily the contents of the work. When a new civil servant's position is established its title and the range in the State salary schedules is determined. The salary schedules include the following compensation elements:

Basic salary: The salary of a civil servant consists of a basic salary.

Age allowance: In addition to the basic salary age bonuses are paid in accordance with a six-stage scale on the basis of 3-18 years of service in the public sector or in a corresponding professional area. The age bonuses are determined as percentages of the basic salary and their maximum total amount is 25%. The first age bonus is added to

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compensation after 3 years of service (5% on top of base salary) and additional bonuses are added every three years thereafter.

Compensations of costs which are paid to the members of Parliament and to ministers (who are usually also MPs) represent a substantial part of their salary package. MP's who are living in the Capital area can receive 30% of their base salary as a compensation of costs. Maximum compensation is 55% of base salary, and it is paid to MP's who need an apartment in Helsinki. The compensations are almost completely tax-free. Ministers' compensation of costs is 50% lower than the standard MP allowance because they have use of car and driver whilst in Helsinki and their personal travel between Helsinki and home is usually paid by their political party.

Car benefits including the drivers are granted to ministers and Chief General Managers of State Agencies. The prime minister has a residence with the servants but otherwise housing benefit is not applied to other ministers.

Pay Levels (Finnish Markka)

Position	Fixed Remuneration	Cash Allowance (Compensation of Costs)
Prime Minister	FM 641,000 (1)	FM 96,000 – FM 176,000
Minister	FM 534,000 (1)	FM 80,000 – FM 147,000
MP	FM 338,000 – FM 401,000 (2)	FM 97,000 – FM 211,000
Top Civil Servant	FM 616,000 – FM 711,000	-

Note:

(1) PM and minister pay includes maximum of six age allowances. PM and minister automatically entitled to five of the six age allowances upon taking office.

(2) MP below 12 years of service receives minimum, over 12 years receives maximum.

Issues

The general view is that ministers are not highly paid – even less than top civil servants. However, much controversy was generated when MPs voted a raise for themselves. Because the state is a very large employer in Finland, reforms in salary systems have been slow but have not generated resistance.

Summary of Practices on Ministerial Remuneration: Netherlands

History

In the 1980s a rule was formulated that ministers, including the prime minister, should not earn more than six times the minimum wage. In fact, the ratio has been increased but the principle of the rule is still in place.

Because of Labor Market restraints in attracting top civil servants and politicians there is (some) pressure to change remuneration policies and practices (i.e. higher pay), but the issue is very politically sensitive.

Process

There is no independent review body for setting pay, and salary adjustments follow civil service collective bargaining agreements. Parliament is accountable for determining remuneration policies and practices, but it has not been discussed in many years. They also are accountable for reviewing their own salaries, and as a result of concern about public scrutiny, there has not been an adjustment other than for wage inflation in a number of years.

Factors

For civil servants, a collective labour agreement is negotiated by the Ministry of the Interior with the labour unions. The negotiated pay rise is then also applicable to the MPs and ministers. Besides the rule on multiples of the minimum wage, there are no guidelines or policies about determination of remuneration for ministers. Influence of private sector pay is only indirect, in that civil service unions refer to private sector collective bargaining agreements when negotiating on salary adjustments for civil service. Nevertheless, the rate of increase in civil service has been lower than in private sector, so gaps between the two sectors are expanding.

Structure

Compensation for ministers consists of a fixed base salary and non-accountable allowances for expenses incurred in carrying out duties. They are participants in the civil service retirement scheme.

Pay Levels (NLG)

Position	Fixed Remuneration	Cash Allowance
Prime Minister	NLG 251,515	-
Minister	NLG 251,515	-
MP	NLG 191,590	-
Top Civil Servant	NLG 252,400	NLG 11,400

Note: Fixed remuneration excludes allowances.

Issues

Compared to the private sector, ministers and top civil servants are poorly compensated compared to private enterprise, but the citizen's view is that they are well compensated compared to the average worker and that they are being paid with that worker's tax money. Because top civil servants pay is compressed by relation to politician's pay, attracting and retaining qualified civil servants is a major concern.

Attempts at reform, or studies of reform, have tended to fail because the public at large is not convinced of the need for pay raises, especially for ministers.

Summary of Practices on Ministerial Remuneration: New Zealand

History

From earliest times, MPs received an honorarium for serving as a representative. In the 1940s a system of salaries was established as well as a system of separate allowances. From the 1950s to the present, the structure of allowances has been modified and built up around particular purposes, creating the current categories.

In 1973, the Royal Commission upon Parliamentary Salaries and Allowances established the following principles:

- that the occupation of a member of Parliament should be regarded a virtually full time and professional in nature;
- that it should be assumed that a member of Parliament has no other income;
- that it should be accepted that members are married with family commitments; and
- that regard should be had to the sacrifices a member and his wife (or husband) have to make in their enjoyment of leisure and family life.

The Higher Salaries Commission (HSC) accepted these principles when it took over responsibility for parliamentary salaries and allowances in 1974.

Process

The HSC comprises three independent commissioners appointed by the Governor-General for three-year terms. The HSC conducts reviews annually but the process is long and there are sometimes two years between adjustments. There is no automatic adjustment mechanism linked to civil service pay adjustments or wage inflation in the market place.

Factors

The HSC must set remuneration having regard to the requirements of the job and the conditions and remuneration paid to those in comparable positions. And the HSC also has to take account of the following specific statutory criteria when setting levels of remuneration:

- the need to achieve and maintain fair relativity with the levels of remuneration received in the private sector and public sector;
- the need to be fair both- to the persons whose remuneration is being determined and to the taxpayer; and
- the need to recruit and retain competent persons.

Besides setting salaries, the commission also reviews the allowances, which are considered as reimbursement of costs incurred in the cost of employment – e.g., performing the duties expected by the members of the constituency.

The commission seeks input from commercially-available salary surveys, the State Service's Commission own salary survey unit, and responses to questionnaires issued by the commission to employers requiring remuneration information. The employers are bound by law to provide such information.

There is no stated policy on remuneration levels, but there are significant differences between private sector remuneration and ministerial remuneration. Instead, the ministerial remuneration levels are in closer alignment with government department Chief Executives.

Structure

Pay consists of a system of base salary plus allowances that are not taxed.

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Structure of Parliamentary and Ministerial Compensation (NZ\$)

	MP	Minister	Prime Minister
Salary	85,000	149,200	250,000
Basic Expense Allowance (not taxed) ¹	7,000	12,000	23,500
House & Grounds Maintenance Allowance (not taxed) ¹		1,500	
Constituency Allowance (not taxed) ²	14,000		
Day Allowance (not taxed) ¹	4,704		
House Allowance if not provided with a house (not taxed) ¹		2000	
Accommodation Allowance (not taxed) ²	16,000		
House (not taxed, estimate) ¹		25,000	50,000
Self drive car ¹		22,000	22,000
Chauffeured limousine ²		40,000	40,000
Total (all elements)	126,704	251,700	385,500
Total (remuneration elements only ³)	96,704	209,700	295,500

- 1 These elements considered remuneration – basic expense, day and house and grounds maintenance allowances are not accounted for against any job-related expense; house allowance is provided to those ministers who do not receive housing provided by virtue of already living in Wellington area; ministers not from Wellington area provided with housing; self-drive car is purchased for personal use of family in addition to chauffeured limousine.
- 2 These elements are not considered remuneration. Constituency allowance covers cost of secretarial support and other costs of providing constituency service; accommodation allowance covers cost of second home in Wellington, but is also given to MPs elected on party list who do not need to maintain home in a constituency; limousine is normal job requirement but also available for personal use.
- 3 Total of remuneration elements includes estimated value of housing, but not House Allowance as only one of these is received by a minister. As residence is traditionally reserved for prime minister in most countries, the house value has not been included as total remuneration for the prime minister.

Pay Levels (NZ\$)

Ministerial and Civil Service Pay Levels		
Level	Fixed Remuneration	Performance Related Pay (maximum)
Prime Minister	295,500	
Cabinet Minister	209,700	
Member of Parliament	96,704	
Top Civil Servant	350,000	50,000

Note: Fixed remuneration includes basic allowance and housing for ministers but excludes job-related allowances for MPs and housing for prime minister.

MPs including ministers may contribute up to 5% of salary to the superannuation scheme, which is matched 2:1 by the government – up to a maximum of 10%.

Issues

Over the past 15 years, government policy and tax laws have influenced all employers to move away from provision of benefits or perquisites in-kind. Instead, these benefits and perquisites have been “encashed” into the base salary. However, parliamentary and ministerial remuneration remains a system of salaries, allowances and benefits. In recent months, a report by the Auditor General has signaled the need to review this system, both from a matter of tax fairness and transparency.

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The public perception is that MPs and ministers are overpaid and have low standards of performance. The average wage in New Zealand is around \$35,000 per annum and the MP base salary of \$85,000 is in the top quartile of all salaried positions. Despite the disparity in remuneration compared to complexity of the job, there is no shortage of candidates seeking election as an MP.

Summary of Practices on Ministerial Remuneration: Singapore

History

The current system is based on a 1994 White Paper on Competitive Salaries for Competent and Honest Government. The system was established to ensure that Officers in key government positions are paid salaries that are competitive, in line with professionals in the private sector.

Process

A review is conducted by the Public Service Division, which is charged with the responsibility to review the pay policy and structure of government. The review of the remuneration structure is implemented every five years, with the last review being conducted in July 2000. The results of the review are debated at Parliament and a bill must be passed to implement the recommendations.

Administrative Service salary levels are adjusted annually based on the recommendation of the National Wage Council. The NWC is made up of officials, industry leaders, and private sector representatives.

Factors

Pay is based on establishing a competitive position with the private sector, specifically the eight highest-paid individuals from six professions (48 individuals in total):

Bankers, Engineers, Accountants, Lawyers, CEOs of Multinationals and CEOs of local manufacturing firms.

The minimum targeted pay for a Staff Grade I (MR4) minister – the entry point for minister – is set to be 2/3 the Median Principal earned income of the top eight individuals from each of the six professions. That is, 2/3 of the median income of the 48 individuals drawn from the six professions.

The pay for Administrative Service – Superscale G is set to be equal to the pay of the 15th highest paid person who is 32 years old and belongs to the same six professions above (banker, engineer, accountant, lawyer, or employee in a multinational or local manufacturing firm). Superscale G is the first level of director in the civil service.

These two pay points serve as anchors and the rest of the structure from Superscale G to A and then from MR4 to MR1 and prime minister's pay is set by an estimated progression of 17% to 20% between levels. Superscale B is typically the top level within the civil service; Superscale A is essentially equivalent to MR4.

The information is obtained from the Inland Revenue Authority, and would have a time lag of about 1.5 to 2 years. Since 2000, Principal Earned Income is defined to include value of stock options as exercised. It is assumed that options exercised in a given year will have been accumulated over two years, and the gains are thus halved when calculating the level of earnings.

Structure

Remuneration is comprised of Base Salary, Annual Variable Component and Performance Bonus. Base salary represents 60% of total remuneration, and the Annual Variable Component and the Performance Bonus represent 40% of Total Remuneration. The Annual Variable Component is based on economic results of the Singapore economy. The Performance Bonus is based on individual performance rating. Effective in 2000, half of the performance bonus is paid in the year earned, and the remaining half is paid over the next two years.

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This pay structure is common to both civil servants and ministers.

The government is considering replacing the Annual Variable Component with a GDP-Related Bonus that would vary linearly with GDP growth, thus making this component of remuneration more transparent. However, this is not yet implemented. If the GDP-Related Bonus is eventually implemented, the individual Performance Bonus would remain in place.

The Administrative Service has an active pension plan separate from the Central Provident Fund. The terms of this scheme are secret. Neither civil servants nor ministers receive education allowances, housing allowances, or other benefits, except a very limited medical scheme (S\$350 per year). Ministers would be entitled to a car, but only top level ministers would have full-time drivers and security detail.

The salary scales are adjusted according to the recommendations of the NWC. The salary ranges below represent the opportunity for monthly fixed remuneration. How much an officer or minister is paid within these ranges depends on individual performance.

Pay Levels (S\$)

Position	Monthly Fixed Remuneration	Annual Performance-Related Pay	Targeted Annual Total Cash (Note 2)
Prime Minister	\$85,300	\$831,000	\$1,940,000
MR1 (Deputy PM and Minister 1) (Note 1)	\$60,000 - \$75,900	\$582,000 - \$736,200	\$1,500,000 - \$1,897,500
MR2 (Minister 2) (1)	\$49,000 – \$61,500	\$475,300 – \$596,550	\$1,225,000 - \$1,537,500
MR3 (Minister 3)	\$44,600 – \$55,700	\$558,200 – \$697,900	\$1,138,000 - \$1,422,000
MR4 (Minister 4)	\$37,900 – \$47,400	\$475,000 – \$593,000	\$968,000 – \$1,210,000
Superscale B (SR5)	\$28,800 – \$39,800	\$361,000 – \$498,600	\$736,000 – \$1,016,000
Superscale C (SR 6) (1)	\$24,000 – \$31,200	\$259,200 – \$337,000	\$612,000 – \$795,600
Superscale G (SR 9)	\$17,500 – \$18,800	\$135,500 – \$145,600	\$363,000 – \$393,000
MP	\$11,900	\$21,300	\$176,000

Notes:

(1) MR 1, MR2 and Superscale C are estimates, as figures are not made public.

(2) For MR4 and above, targets are based on June 2000 recommendations and are being phased in. For Superscale B and below, targets are currently implemented.

Issues

It is widely recognized that top civil servants and ministers in Singapore are well-compensated. Concerns have been expressed about rising income inequality between the poor and the rich, and also that increases in variable compensation are being used as a device to camouflage the true extent of pay rises accruing to ministers.

With recent downturns in the economy, there have been pressures to cut salaries of key officials, but no official statement has been issued regarding this issue.

Summary of Practices on Ministerial Remuneration: United Kingdom

History

The process and principles of remuneration for ministers in UK has been broadly stable for many years. The same principles have recently been extended to cover the newly devolved Parliament in Scotland and the Assemblies in Wales and Northern Ireland. Key features of the approach are:

- Work in Government or Parliamentary office is considered to bring rewards other than salary and does not attract 'full market rates' of pay. Nevertheless, it is thought that ministerial pay should be reasonably competitive to public sector pay levels, where comparisons can be established. Current pay levels are considered by the appropriate Review Body (see below) to 'represent the minimum that ministers should be paid'.
- Pay is limited to a fixed base salary, a pension, and the use of facilities (including in many cases accommodation) which are 'attached' by custom and practice to specific offices. There is no element of variable or performance related pay.
- Pay levels and pension arrangements for ministers and members of Parliament have to be agreed by the House of Commons, as have MPs' office and staff support allowances, which are also payable to those ministers who are MPs. Currently all cabinet-level ministers are MPs except the Lord Chancellor and Lord Privy Seal, who are members of the House of Lords. Salaries and allowances are approved on the recommendation of the prime minister, although there have been several examples of MPs approving higher figures than those suggested by the SSRB.
- Housing is provided only for the prime minister, chancellor of the exchequer and foreign minister at no cost to the office holder, and no other housing allowances are provided for other ministers.
- Pay and allowances are formally reviewed every three years. Within that period, annual increases are geared to the median of pay movements for the Senior Civil Service (in respect of pay) and the Retail Price Index (in the case of allowances).
- Pay determination is, as far as possible, 'de-politicised' through an independent review process.

Process

Every three years, the PM commissions the Senior Salaries Review Body (SSRB) to review ministerial and parliamentary pay allowances. The SSRB is composed of senior industrialists, retired public servants, academics and other professionals. The SSRB also reviews pay of senior civil servants, equivalent ranks in the armed forces, and the judiciary. The SSRB follows a standard process:

- It invites written or oral evidence from interested groups
- It asks an external consultant to advise on base pay for jobs of comparable weight to ministers in both the public and private sectors
- On some occasions, the SSRB commissions external research into international practice
- On pensions issues, it draws on advice from the Government Actuary and specialist consultants

Recommendations are provided to the PM who then decides when to publish the paper and present it to Parliament for debate.

Factors

The SSRB seeks to ensure that pay and pension levels are sufficient that suitable candidates are not deterred from entering public life and has attempted to ensure that ministerial pay remains broadly comparable to that of relevant positions in various parts of

Phase I Report – Remuneration of Principal Officials

the public sector. It is accepted that tracking private sector practices, even on base salaries, is not practical in the UK.

It has long been recognized that some positions in the ministerial hierarchy are more complex than others. For example, the chancellor of the exchequer bears a much higher level of accountability than some of the other cabinet ministers. Nevertheless, differential pay has never been seriously considered.

Pay Levels

Members of Parliament	<i>House of Commons</i> ¹		
	£51,822		
	Ministerial/ Office Holders Salary	Parliamentary Salary	Total Salary
Ministers' Salaries	£	£	£
Prime Minister ²	110,287	51,822	165,418
Cabinet Minister ²	66,172	51,822	119,979
Minister of State	34,326	51,822	87,178
Parliamentary Under Secretary	26,053	51,822	78,657
Top Civil Servant (Cabinet Secretary)			170,000

¹ Pay for cabinet ministers in House of Lords is somewhat lower because they do not have constituency accountabilities.

² The prime minister and cabinet ministers in the House of Commons have elected not to draw all of the ministerial salaries to which they are entitled.

Issues

It is typical for the SSRB review to be met with some amount of public controversy. Public opinion would tend to view MPs as overpaid in relation to what they do, though this analysis would not be shared by the SSRB. The SSRB is instead concerned that current levels of ministerial pay are the bare minimum that can be justified by relation to any external comparators. Fearing public reaction, governments have pursued cautious policies in implementing SSRB recommendations and until recently the Cabinet itself, at the request of the PM, did not draw their full salaries.

The recent increase was implemented in the days immediately following the last election, thus attracting a minimum of attention.

Summary of Practices on Ministerial Remuneration: United States

History

Salaries of top-level Executive Branch officials of the U.S. Federal government are statutorily linked to the salaries of Members of Congress who are responsible for setting pay for these positions. The framers of the Constitution placed the responsibility of setting pay of the top-level Executive Branch officials, as well as its own and of the President, to Congress.

In 1816, Congress' first attempt to raise their salary met with negative public reaction. As a result, Congress tried to insulate itself from public criticism by linking its pay to top-level Executive Branch officials and Federal judges.

In 1967, Congress passed the Federal Salary Act which created an independent commission (commonly referred to as Quadrennial Commission) on Executive, Legislative and Judicial Salaries. The Commission; composed of private sector members appointed by the President, leaders of the Senate and House Representatives, and Chief Justice of the United States; was designed to insulate Congress from the politically sensitive task of setting its own salaries. Every four years, the Commission would convene and make salary recommendations for top-level Executive Branch officials, Members of Congress and Federal judges. These recommendations would be sent to the President for final recommendations to Congress. The President's recommendations would become effective unless rejected by Congress. The process was intended to serve the public interest and minimize political interference. The process worked in 1969, but then top-level Executive Branch officials were denied salary adjustments for the next six years.

Then in 1975 to address the salary erosion, Congress enacted the Executive Salary Cost-of-Living Adjustment Act. This legislation was intended to grant certain positions, including top-level Executive Branch officials, the same automatic cost-of-living adjustment (COLA) given to rank-and-file Federal employees. Pay adjustments made under the Act were to be automatic, unless specifically rejected by Congress. These adjustments were to be in addition to the salary raises granted through the Quadrennial Commission review process. However, Congress frequently rejected or reduced the COLA available under the Act for political reasons.

Then Congress enacted the Ethics Reform Act of 1989 due to anticipated mass departures of top officials and growing concern over the Federal government's ability to recruit highly qualified replacements. The Act restored two cost-of-living adjustments, comparability pay adjustment, and most notably, amended the Federal Salary Act and the Adjustment Act in two respects:

- (1) it replaced the Quadrennial Commission with a Citizens' Commission on Public Service and Compensation and
- (2) it revised the mechanism for fixing the annual pay adjustments for judges, Members of Congress and top-level Executive Branch officials.

The new Commission was to be comprised of 11 members: six members to be appointed by leaders of the Executive, Legislative and Judicial branches and five members to be selected from the public at large. Under the Ethics Reform Act, the Employment Cost Index (ECI), a quarterly index measuring the change in wages and salaries paid to private sector employees, was adopted as the basis for determining the amount of annual pay adjustment. It was Congress' intention that ECI provide top government officials with regular pay increases to alleviate future need for major "catch-up" adjustments.

The review commission, the Citizens' Commission on Public Service and Compensation, has never become functional because no money has ever been appropriated for the Commission and Congress and the President have not appointed its members. As a result,

there has been no systematic review of salaries of top executive officials since 1988 (date of last Quadrennial Commission).

Current Process

Federal employees are classified into categories according to position. The top-level Executive Branch officials are under the Executive Schedule pay system, which is a five-tier structure from Level I (Cabinet Secretary) through Level V (lowest salary). Their salary is linked to the salary of the Members of Congress who are responsible for setting the pay of these top-level officials.

The President presents salary recommendations for the top-level officials and these are either approved or rejected by Congress. By law, Executive Schedule pay is supposed to rise each year at the same rate as other Federal government employees (who are on the General Schedule), but Congress has voted each year to block Executive Schedule raises since 1993, except for 1998, 2000 and 2001. The salary levels of these positions are capped based on the Vice President's salary, which currently is \$186,300.

Under current law, there are three ways to adjust pay of top-level officials:

- (1) allow automatic and annual pay adjustments based on changes in the Employment Cost Index (ECI);
- (2) adopt pay raises recommended by the President to Congress, based on the report of the Citizens' Commission to review and consider salaries of high-level Federal officials; or
- (3) pass special legislation authorizing a pay raise.

As a matter of practice, it is this third approach that has been taken, such that determination of pay levels is subject to political considerations. Private sector pay practices are not reviewed nor do they influence the pay levels of top-level Federal officials.

Structure of the pay package

Top-level Executive Branch officials receive only base salary, under a five-tier pay structure, Level I (highest) through Level V (lowest). There is no variable compensation or non-accountable allowances. In addition, these officials are not provided with housing or housing allowances and no other significant perquisites are provided.

Top-level Executive Branch officials, as well as Members of Congress, are also covered by the benefits package that applies to Federal civil servants. The most important benefits are:

- A contributory retirement plan that pays approximately two-thirds of salary for a full career (35 years of service). Officials can first retire from 55 to 62 depending on years of service. The plan for officials entering the government since 1983 is a combined defined benefit/defined contribution plan. All Federal employees are also covered by Social Security.
- A choice of health plans that reimburse about 80 percent of covered health care expenditures. The health plan eligibility is carried into retirement. At age 65, the benefits are coordinated with Medicare.
- A life insurance plan providing a benefit approximately equal to salary.
- Annual leave of up to six weeks a year depending on service.

Remuneration for Cabinet and Other Top Appointed Positions (US\$)

Level	Base Salary
President	\$400,000
Vice President	\$186,300
Level I – Cabinet Secretary	\$161,200
Level II – Deputy & Directors of Agencies	\$145,100
Member of Congress	\$145,100
Top Civil Servant (SES 6)	\$133,700

Issues

The system has been under much public and political scrutiny for many years. Pay of top-level Executive Branch officials (as well as Federal judges) is a politically sensitive issue. Increasing the pay of these top-level Executive Branch officials will affect the pay levels of other Federal employees because salary caps are set at the level of the top-level officials. If Members of Congress approve salary raises for top-level officials, they will have to approve raises for themselves in addition to other Federal employees who are on different pay systems from Congress and top-level officials, such as Senior Executive Service employees.

This new pay system created under the Ethics Reform Act of 1989 is not working well. Congress has permitted only three COLA adjustments since 1993:

- 2.3% in 1998
- 3.4% in 2000
- 2.7% in 2001

Past attempts at reform, such as delinking pay of the top-level Executive Branch officials with Members of Congress, have failed mainly for political reasons. Congress' reluctance is largely due to the concern over adverse public reaction to pay increases for themselves. Congress is hoping to force a consensus on the need for across-the-board salary increases.

The current pay system and the reluctance of Congress to vote for Congressional pay raises are hindering the recruitment of highly qualified potential candidates from seeking appointments as Cabinet Secretaries, as is the intensive vetting and confirmation processes to which candidates are subject. Potential candidates prefer to remain in the private sector where compensation is higher and there are regular salary reviews.

Phase II Report

Remuneration Packages for Principal Officials of HKSAR Government Appointed Under the New Accountability System

Conclusions and Recommendations

March 25, 2002

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Constitutional Affairs Bureau

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Part I. Introduction

1. All principal officials holding Secretaries of Department and Directors of Bureau positions in the HKSARG are currently civil servants. They are remunerated according to the relevant civil service pay scale and enjoy fringe benefits that the civil service system provides. They are subject to the civil service management system and the civil service disciplinary mechanism.
2. There have been views expressed that as senior officials are involved in policy making and play a leading role in public affairs, they should be held accountable for the outcome of their policies. In his 2000 Policy Address, the Chief Executive of the HKSAR undertook to examine how, under the leadership of the Chief Executive, the accountability of principal officials for their respective policy portfolios could be enhanced. In his 2001 Policy Address, the Chief Executive outlined the initial thinking on enhancing accountability of principal officials. The idea is to introduce a new system of appointment applicable to the Chief Secretary, the Financial Secretary, the Secretary for Justice, and most Directors of Bureaux. They would be appointed on terms different to those in the civil service. Their term of office would not exceed that of the Chief Executive who nominated them for appointment.
3. An important component in this consideration is determining the remuneration of the principal officials. The HKSARG thus commissioned Hay Group to conduct a study for this purpose.
4. The study includes a review of the approaches taken in a number of economically advanced nations to determine reward practices for appointed, ministerial-level positions. These countries included Australia, Canada, Finland, Netherlands, New Zealand, Singapore, United Kingdom and United States. In addition to understanding current practices, the study offers an opportunity to discern the current thinking or likely trends in remunerating ministerial positions.
5. The study also encompasses a survey of pay practices for top executives in private, public and professional services sectors in Hong Kong. The survey was conducted to identify the levels and components of remuneration of holders of jobs broadly comparable to principal officials of HKSARG and to discern the alternative remuneration opportunities of prospective appointees assuming that they could otherwise be employed as top executives in the sectors surveyed.
6. The Phase I Report explains the methodologies employed and the results of the review of international practices and the Hong Kong top executive remuneration survey.

7. This Phase II Report summarizes conclusions from the Phase I surveys and provides recommendations on remuneration for appointed principal officials. The contents of this report include:
- conclusions drawn from the review of ministerial remuneration in the selected countries in light of the unique institutions and governance of Hong Kong;
 - fundamental principles that guide the formulation of the recommended remuneration package; and
 - taking reference to the above and the results of the pay practices for Hong Kong's top executives, detailed recommendations on the structure and level of remuneration for principal officials of the HKSARG.

Part II. Review of Practices of Selected Countries—Conclusions and Implications for HKSARG

Summary of Findings

8. Based on the review of the policies and practices for determining pay for ministerial level positions in the selected countries, several conclusions may be drawn:
- The determination of ministerial pay, including the process of recommending and approving the specific amounts, reflects the political system's characteristics and is strongly influenced by societal values.
 - Some countries, including Australia, Canada, New Zealand, and the United Kingdom have established independent commissions to recommend or determine pay for ministers, and the United States has from time to time sought to emulate that model. These commissions ensure appropriate relativity to civil service, public sector, and private sector remuneration practices. The commissions were formed in part to ensure that pay for top civil servants and ministers is reasonable, whilst enhancing objectivity and reducing political influences in decision making.
 - Others (Finland and Netherlands) have established more direct links to civil service pay levels, such that ministers would be paid at or near the top of the civil service pay scales.
 - Uniquely, Singapore has established a process to ensure that ministerial pay levels are competitive with those of top executives in the private sector, in recognition that ministers are highly capable executives who provide value to society that is at least comparable to the value of private sector executives. Furthermore, Singapore's use of merit-based salary adjustments and variable pay is intended to reinforce an orientation toward individual as well as government performance.
 - While it is generally recognized that ministerial jobs are highly complex in both scope and responsibility, the pay levels of these positions is much lower than that of comparable positions in the private sector, with the exception of Singapore. Though the independent commissions in United Kingdom and other countries periodically undertake private sector remuneration comparisons, the recommendations made by the commissions are not intended to match pay levels that prevail in the private sector.
 - The structure of ministers' remuneration packages in most countries (except United States and Singapore) reflects the fact that they are politicians and usually members of parliament who have to provide service to constituencies that are often located some distance from the seat of government. Besides salaries, the packages usually consist of a number of allowances to cover costs of providing constituent services and expenses incurred directly as a result of holding a ministerial

position or serving as a member of parliament. These allowances may include housing, if the minister must maintain a second home, travel, and other expense allowances. These allowances are often non-accountable, though they usually have limits.

- Ministers also are entitled to a range of benefits that are typical of and comparable to those provided to civil servants. These include retirement schemes, medical coverage, life insurance and similar. Most countries do not provide perquisites to ministers, except perhaps access to car and driver for spouses of ministers. As a matter of job requirements and perhaps security, ministers are typically provided with a car and driver, sometimes for personal use.

Implications for Hong Kong

9. As in other countries, principles for remuneration of principal officials should be aligned with sociopolitical and cultural values but balanced against economic reality and the institutional needs of the HKSAR.
10. Approaches taken in countries where ministers are professional politicians may not be appropriate in Hong Kong where principal officials may be drawn from different sectors and backgrounds. On the other hand, there are non-financial rewards associated with top level public offices. Financial rewards should not be the sole consideration of a candidate for a principal official position. Incentives such as honour and the opportunity to contribute to the improvement of society should also be considered when setting remuneration.
11. Taking reference to remuneration practices of private and other sectors in determining the remuneration packages for principal officials should have merit. Candidates for these positions may come from non-government sectors, and principal officials may move to or return to these sectors after service in government. As they take up public office, they may still have personal or family financial obligations that must be maintained. Accordingly, there should be minimal financial or economic barriers in attracting and retaining these individuals for their term of service. .
12. The independent process for recommending or determining ministerial pay adopted in other countries merits consideration for Hong Kong. To prevent conflict of interest, principal officials should not be involved in reviewing, recommending or determining their own remuneration packages. Furthermore, independent commissions can also protect the process from excessive political influences and consideration should be given to establishing a commission to review remuneration of principal officials in the future.

Part III. Summary of Results of Remuneration Survey

13. A total of 77 private sector corporations, 13 public sector organizations, and 50 professional services firms were invited to participate in the survey. Among those who responded within the given timeframe, 27 private sector corporations, 9 public sector organizations, and 20 professional services firms met the criteria of business size for inclusion in the analysis. Besides size and complexity the participating organizations had to provide accurate and timely information on cash compensation and long-term incentives that reflects the earnings opportunities enjoyed by their chief executives or managing partners.
14. Table 1 summarizes the key market statistics for total remuneration of private, professional services and public sector CEOs as found in the survey.

Table 1: Market Reference: Fixed Compensation, Total Direct Compensation and Total Remuneration for All Organizations

(as of August 2001; Thousands of HK\$)

	Fixed Compensation	Total Direct Compensation	Total Remuneration
Q3	4,436	9,028	\$9,404
Median	3,500	6,045	\$6,658
Q1	2,084	4,397	\$4,738
Average	3,486	6,889	\$7,207

Note: Fixed Compensation = Base Salary + Cash Allowances and Rental Reimbursements
 Total Direct Compensation = Fixed Compensation + Variable Bonus + Annualized Value of Long Term Incentive
 Total Remuneration = Total Direct Compensation + Retirement

15. As shown in Table 1, the median total remuneration of chief executives in the organizations analyzed is \$6.658 million. Statistically, half of the surveyed organizations have higher remuneration than the median, and half have lower remuneration. The median is a fair indication of the market value of remuneration for CEOs in major private and public sector organizations in Hong Kong.
16. The Phase I report includes more detailed breakdown of the remuneration packages in the private sector. This Phase II report emphasizes the value of total remuneration, which encompasses all forms of cash and near-cash compensation regardless of structure of individual packages. For example, the composition of executive remuneration packages may or may not include housing allowances, which are often structured for individual tax advantage. Many companies do not pay any cash allowance, others directly provide housing. Therefore, amounts designated as housing, or cash allowance, may bear little relationship to actual housing costs and market statistics derived for value of housing are representative of neither those who receive an allowance nor the case of those that do not receive any form of provision for housing.

Part IV. Principles of Remuneration of Principal Officials

The Context

17. Principal officials will be appointed to responsible positions that formulate policies that influence the livelihood and living conditions of all people in Hong Kong as well as the economic environment in which Hong Kong businesses operate. They may also be responsible for multiple bureaus and departments with substantial and diverse operations involving the effective expenditure of billions of Hong Kong dollars. Therefore, the scope and complexity of their jobs are comparable to those of chief executive officers of Hong Kong's major private and public sector organizations.

18. In determining the remuneration of the principal officials, it should also be recognized that:

- compensation is an important tool for communicating and reinforcing values and behaviors, supporting accountability for results, and rewarding the achievement of performance goals;
- the positions of the principal officials are full time and professional in nature;
- the prospective appointees could be leaders or top executives of leading corporations or organizations and the HKSARG;
- the appointees have no other income from employment during the tenure of service;
- the appointees may have personal or family financial commitments and obligations to maintain; and
- appointment to public office is associate with rewards — such as personal satisfaction, honor and respect — that have social and cultural values that cannot be measured financially.

Principles and Recommendations

19. Having regard to the foregoing, we recommend that the following principles be adopted as bases to develop the remuneration packages for the principal officials:

Principle 1: Remuneration for principal officials should be determined with reference to remuneration for CEOs of major private and public sector organizations in Hong Kong.

20. Principal official positions are highly responsible positions. These positions are responsible for the formulation and execution of Government policies that have far-reaching and long-term implications for a prosperous, secure, and harmonious society in Hong Kong. They also have substantial executive responsibilities similar to those in large and complex private organizations.
21. The roles of principal officials are by nature different than those of CEOs of public and private sector organizations, and direct comparisons of complexity of these positions in terms of executive management, decision-making authority, or financial accountability are difficult. Nevertheless, it is reasonable to construe that the levels of responsibility or complexity are broadly comparable between principal officials and CEOs.
22. Taking reference to non-government practices in determining the remuneration packages for principal officials should have merit. Apart from communicating the values and behaviors that will be desired, it also recognizes that candidates for principal official positions may come from non-government sectors, and they may move to or return to these sectors after service in government. Therefore, comparability of remuneration of principal officials to remuneration practices for CEOs in the public and private sectors of Hong Kong is an important consideration when assessing the reasonableness of principal officials' remuneration.
23. On the recognition and basis of that principal officials will hold positions that are comparable to those of CEOs in major private and public organizations, we recommend that:

▪ Pay for principal officials should be set in *reference* to remuneration practices for comparable private and public sector positions;

▪ The *median* should be established as a reasonable market reference as it reflects the middle of the range of compensation values for the comparison group of CEOs.

Principle 2: The remuneration package should be simple in structure and easy to administer.

24. The remuneration structure should encompass the elements of remuneration that are likely to be considered by a potential candidate in evaluating his or her acceptance of a position as a principal official. These include cash or near cash elements such as base salary, variable bonuses, cash housing allowances or provision of rented or company-owned accommodation, contributions to retirement schemes or contractual gratuities, and value of long-term incentives such as stock options. Benefits such as medical insurance and life insurance could be considered as well but are very small in comparison to total remuneration levels of chief executives.
25. Housing allowances are often established in the private sector as a means of limiting amounts designated as base salary that may be subject to pension, variable pay formulas, or annual salary reviews. Housing allowances are established to secure a tax advantage for the employee at little or no cost to the employer. The amounts designated as housing allowance in the private sector may therefore bear little relationship to actual expenditure on housing. As the aforementioned purposes are not within the interest or concern of the HKSAR Government and expenditure on housing is a personal choice of the appointed principal official (except as noted in the next paragraph), it is unnecessary or inappropriate to designate a certain amount as a “housing allowance”.
26. The appointed Secretary for Justice, Financial Secretary and Chief Secretary are required to live in designated government quarters that provide an appropriate environment for conducting meetings and entertaining important guests. As the Government, not the appointed Secretary, requires and chooses the housing, it would be inappropriate to require the appointed Secretary to accept a substantial reduction in cash remuneration in consideration of the housing that is provided.
27. It is common in private and public sectors to provide a gratuity for executives who are employed on a contract basis. These gratuities are offered in lieu of a retirement scheme, and may or may not be subject to completion of the contract period. Appointed principal officials are not included in Government retirement scheme because that scheme is intended for career civil servants and is inappropriate for individuals serving on an appointed basis. Nevertheless, it is neither necessary nor appropriate to provide a contract gratuity for appointed principal officials, because any amount set aside as gratuity could be encashed into monthly pay anyway.

28. The nominal contractual period of service for principal officials extends to the end of the term of the Chief Executive who appointed them. Given the nature of service as an appointed principal official and the purpose of the accountability system in which the principal official serves, it is unreasonable to withhold a portion of remuneration subject to satisfactory completion of the term of service. Any gratuity provided for appointed principal officials would therefore be paid in proportion to time of service. If paid proportionately to length of service, the gratuity is effectively equivalent to part of the base salary, and no purpose is served by designating a portion of remuneration as a gratuity and deferring its payment.

29. Hence, we recommend that:

▪ Principal officials should be remunerated in the form of an all-embracing encashed salary without itemization of components such as housing allowances, or gratuity.

▪ The Secretary for Justice, the Financial Secretary and the Chief Secretary will be provided suitable housing at the discretion of the Government, but there should not be any adjustment or reduction of compensation for this purpose.

Principle 3: The remuneration package should consist of a fixed, encashed salary, with no element of variable performance-based pay or merit-based salary adjustment.

30. Under the new accountability system principal officials are accountable for results. The Chief Executive retains the discretion to dismiss or request the resignation of any principal official who does not meet the expectations for performance in the position. Thus, there is a presumption that a principal official is meeting the expected standard of performance so long as he or she remains in the position and further judgements on variable payments or merit increases are inappropriate. Conversely, if the Chief Executive reduces the variable pay of a principal official, it would be difficult for that official to retain the credibility to perform effectively in the future. Thus, variation of pay between individual principal officials is impractical, if subject to public disclosure.
31. In the private sector, variable compensation schemes for top executives are closely tied to financial results of the organisation. Well-designed variable compensation schemes align the executive's incentives with shareholders' interests. These schemes reflect strong commercial, profit-oriented values that are incompatible with the nature of principal official positions. Further, appropriate financial or non-financial measures that can be used to assess the end results of their efforts are simply non-existent. Motivation of principal officials should be based on a sense of accomplishment and the continuing development of Hong Kong, not on financial incentives.
32. An alternative approach such as a "GDP" bonus (under consideration in Singapore) would not necessarily measure the performance of the principal officials but rather economic performance of Hong Kong during the tenure of the principal officials. This approach has the merit of tying the remuneration of principal officials to the overall wealth of the Hong Kong people, but would at the same time violate other principles outline here – that remuneration should reference practices for remuneration of top executives in other sectors.
33. Private sector compensation for chief executives is either directly or indirectly based on incentives. Because the compensation package should be fixed, compensation levels for the principal official are inherently less risky. Therefore, it is not necessary for the targeted compensation of principal officials to fully match the level of total compensation for chief executives.
34. Therefore we recommend:

<ul style="list-style-type: none">▪ Remuneration for principal officials should not include an element of variable compensation whether on individual or collective basis, nor will adjustments be made to fixed compensation on the basis of individual performance.

<ul style="list-style-type: none">▪ Variable compensation prevailing in market practices should not be fully converted to fixed pay in determining the principal official remuneration package.

Principle 4: The differences in ranking among the principal officials should be acknowledged and reflected in their remuneration.

35. Principal officials comprise two groups: (1) directors of bureaux and (2) the secretaries of departments, including the Chief Secretary, Financial Secretary and Secretary for Justice. Traditionally, the pay of directors of bureaux has not been differentiated by portfolio. This practice should be extended to the appointed Directors of Bureaux.
36. Traditionally, remuneration for Secretaries of Departments has been set higher than remuneration for Directors of Bureaux, with Secretary for Justice, Financial Secretary and Chief Secretary receiving successively higher levels of pay according to their ranks. This practice should also be extended to appointed Secretaries of Departments.
37. These nominal increments align with the acknowledged ranking of the positions and are not intended to reflect differences in the breadth of responsibilities. Hence, we recommend that:

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|--|
| <ul style="list-style-type: none">▪ Nominal increases of up to 5 percent should be applied between Directors of Bureaux and Secretary for Justice, between Secretary for Justice and Financial Secretary, and between Financial Secretary and Chief Secretary. |
|--|

Principle 5: The remuneration of principal officials should take into account non-financial rewards or intangible benefits that are derived from service as a top public official whilst ensuring that remuneration is commensurate with the responsibilities of their positions.

38. Service as a principal official is expected to be motivated primarily by a desire to serve the Hong Kong society and the honour conferred on the official through this service. Monetary remuneration or perquisites should not be a primary motive for serving as a principal official. As they move into public office, appointed principal officials still have personal or family financial obligations that must be maintained. Compensation should be set at a level that does not impose a barrier for qualified candidates to serve as principal officials.
39. The appropriate level of remuneration, in absolute terms and relative to competitive market pay levels for chief executives, is finally a political decision that must be acceptable to the people of Hong Kong, in consideration of the circumstances, culture and social values of Hong Kong.
40. The non-financial reward of service as an appointed principal official should be reflected through a differential between the competitive market pay levels for a CEO. It should be recognised that this differential is a value judgement and is not based on a specific methodology or process. There should be a differential between principal official remuneration and competitive market pay levels but such differential should not create financial barriers to service as a principal official.
41. As the differential is a matter of value judgement, Hay Group's recommendation takes the form of a range. We recommend that:

- | |
|--|
| <ul style="list-style-type: none">▪ The differential between market remuneration levels for chief executives and remuneration for principal officials should be chosen within a range of 40 percent to 45 percent. |
|--|

Part V. Recommendations on Remuneration of Principal Officials

42. On the basis of the principles and recommendations above, we recommend the following policies be adopted in formulating the remuneration packages of the principal officials:

Market Reference

- The market reference for principal officials shall be based on the pay levels of all surveyed CEO positions.
- Remuneration for principal officials shall be compared to the *median* value of CEO total remuneration, which includes base salary, housing, variable bonus, long-term incentives and retirement.

Intangible Rewards

- As service of a principal official is not motivated solely by remuneration, remuneration for principal officials shall be set with a differential relative to the market reference.
- The suggested differential is between 40% and 45%.

Remuneration Structure

- Directors of Bureaux shall be paid an all-embracing encashed salary as well as in-kind benefits such as medical coverage. No separate allowances should be paid for housing or other purposes.
- The Secretary for Justice, Financial Secretary and Chief Secretary are required to live in government-owned housing as a job requirement. No other adjustment or reduction of compensation shall be made.

Levels of Compensation

- The pay differential between the Directors of Bureaux and the Secretary for Justice and the successive differentials between Secretary for Justice, Financial Secretary and Chief Secretary shall be observed to acknowledge rankings of their positions.
- Successive increments in base salary shall be applied between Directors of Bureaux and the Secretary for Justice, between Secretary for Justice and Financial Secretary, and between Financial Secretary and Chief Secretary. The maximum increment shall be 5%.

Calculation of Total Remuneration for Principal Officials

43. Table 2 shows the calculation of total cash remuneration for principal officials, applying the proposed differential of 40 percent to 45 percent from market total remuneration.

Table 2: Calculation of Total Remuneration for Directors of Bureaux

		Lower Bound	Upper Bound
1.	Market Reference (Median)	\$6,658,000	\$6,658,000
2.	Differential percentage	45%	40%
3.	Differential (Line 1 x Line 2)	\$2,996,000	\$2,663,000
4.	Total Encashed Compensation (Line 1 - Line 3)	\$3,662,000	3,995,000

Note: Amounts rounded to nearest thousand dollars.

44. Applying the proposed range of differentials to the market median total remuneration of \$6.658 million results in a lower bound \$3.662 million and an upper bound of \$3.995 million. Remuneration within this range should represent a balanced approach to providing reasonable financial compensation whilst recognising that the motivation for public service is not primarily financial in nature. This range is near the 15th percentile of the market practice. In our considered view, this level of remuneration will not deter a motivated candidate from accepting appointment as a principal official even in cases where the candidate would be accepting a substantial reduction in remuneration.

45. In consideration of the level of responsibility of the principal officials, the significantly higher alternative compensation that may be available to candidates for these positions, and the reasonable expectation of the candidates that they should not face substantially reduced standards of living, this proposed compensation level should gain public support.

Remuneration for Directors of Bureaux and Secretaries of Departments

46. Table 3 shows the remuneration package for Secretaries of Departments and Directors of Bureaux according to the approach described above.

Table 3: Remuneration for Principal Officials

Level	Encashed Salary (Lower Bound)	Encashed Salary (Upper Bound)
Directors of Bureaux	\$3,662,000	\$3,995,000
Secretary for Justice	\$3,845,000	\$4,195,000
Financial Secretary	\$4,037,000	\$4,404,000
Chief Secretary	\$4,239,000	\$4,625,000

Note: Assuming maximum differential of 5% between each successive rank.
Amounts rounded to nearest thousand dollars.

Other Terms and Conditions

47. These amounts above shall be divided and paid on a monthly basis 12 times per year.
48. In administering the remuneration package for principals officials, we recommend that the following, taking references to private sector practices, be also considered:

Retirement Scheme

As the principal officials are not participants in any other approved retirement scheme, the HKSAR Government will contribute the minimum statutory amounts to an MPF scheme in addition to the remuneration outlined above. The principal official will also be required to contribute out of the encashed remuneration such amounts as are required by statute. There is no other retirement scheme or gratuity.

Medical and Insurance Benefits

As appointed principal officials are not civil servants, the Government would need to make special arrangements to provide medical and other insurance benefits for appointed principal officials. The terms of coverage can be the same as for senior civil servants.

Annual Leave

Each principal official will be entitled to 22 working days of leave annually, with leave for working Saturdays being charged at ½ day. Leave should be used within the calendar year in which it is earned.

Sick Leave

Statutory provisions for sick leave shall apply. The Chief Executive may at his discretion grant additional leave of absence considering the nature of illness and the length of leave required.

Use of Car and Driver

Each principal official should be provided with a car and driver.

Duration of Contract

Subject to the discretion of the Chief Executive, principal officials may be appointed or re-appointed to terms that shall not exceed the length of the term of the Chief Executive who appointed them.

Termination of Contract Without Cause

To effect a smooth transition for a principal official in case of termination, and considering that principal officials may have left well-established positions to take up these roles, some provision for a notice period, or payment in lieu, is appropriate. Whilst private sector practices of anywhere between 3 months and 12 months for top executives are typical, these long periods are not appropriate for principal officials. Therefore, the Chief Executive may at his or her discretion terminate without cause the contract with the principal official upon one month of advance notice. In lieu of notice, the Chief Executive may terminate the contract upon payment of one month of salary. All accrued benefits are forfeited.

Termination of Contract With Cause

In cases of non-performance of duties, malfeasance, insubordination, or other cause, the Chief Executive may terminate a principal official's contract without notice or payment in lieu of notice, and all accrued benefits are forfeited.

Voluntary Termination

A principal official may voluntarily terminate his or her contract at any time upon one month prior written notice to the Chief Executive whereupon his or her employment will terminate at the end of the notice period or payment of one month of salary. At his discretion, the Chief Executive may waive the notice period or payment in-lieu. All accrued benefits are forfeited.

Confidentiality

It is typical for private sector chief executives to be bound by confidentiality clauses that prevent them from revealing their company's confidential information during or after their service with the company. A principal official would be privy to considerable confidential information about the Government or parties. The release or use of that information, whether or not intended for personal gain of the principal official, may cause damage to the Government or affected parties.

During the term of the contract or following termination of contract, the principal official is not allowed to directly or indirectly disclose to any individual, corporation, or other entity or use for the official's own or another's benefit any information, whether or not reduced to written or other tangible form, which has been treated by the HKSAR Government as confidential or proprietary or in the confidentiality of which the HKSAR Government has a legal prosecutable interest. Similarly, information that is confidential to any individual, corporation or other entity and was provided to Government in confidence cannot be used or disclosed.

Conflict of Interest: Employment and Lobbying

In some other countries, there are ethics rules that restrict the ability of government officials from working for organizations that they had regulated for a specified period of time. These rules may also forbid the official from lobbying the department in which he or she worked for a specified period of time.

Rather than creating a contractual restriction on the employment opportunities of principal officials after they leave service, we recommend that the HKSAR Government consider establishing an independent committee to advise principal officials and the HKSAR Government about the propriety of post-service employment opportunities. That advice would be made public.

To prevent actual or apparent conflicts of interest, a former principal official shall not engage in the direct lobbying of any Government department or bureau to influence formulation of Government policies, regulations, rules or legislation on behalf of any individual, corporation or other entity for a period of 24 months following termination of service as a principal official.

Periodic Reviews of Remuneration

49. The level and structure of remuneration of appointed officials should be reviewed thoroughly at least one in every five years. At the Chief Executive's discretion, more frequent reviews can be conducted.
50. Remuneration of principal officials is a sensitive political issue. There is need to treat this issue rationally, fairly and equitably. Hence, the level and structure of remuneration should be reviewed periodically to ensure that they reflect market conditions. Countries such as United Kingdom, Australia, New Zealand and Canada have established independent commissions to review salaries of ministers, members of parliament and senior civil servants. We recommend that the HKSAR Government consider establishing a similar commission to conduct the periodic reviews of remuneration of principal officials.