

LEGISLATIVE COUNCIL BRIEF

REVIEW OF REMUNERATION OF SENIOR EXECUTIVES OF STATUTORY AND OTHER BODIES

INTRODUCTION

At the meeting of the Executive Council on 25 June 2002, the Council took note of the findings of the consultancy study of remunerations of senior executives of major statutory and other bodies.

BACKGROUND

General Background

2 In response to increasing public concerns about the perceived lack of transparency and impartiality in the remuneration policies governing executives in some major public bodies, the Chief Secretary for Administration (CS) announced on 4 January 2002 that the Government would commission a consultancy study on the remunerations of the senior executives of selected statutory and other bodies. A steering committee, chaired by CS, was subsequently set up to oversee the exercise.

Consultancy Study

3. We appointed the Hay Group Limited to conduct the consultancy study. The Final Report submitted by the consultant is at Annex A. The scope of the study covered 11 bodies and two of their subsidiaries, as set out in Annex B. The positions under study included mainly the top three tiers of senior executives in the 11 bodies and the chief executive officers of the two subsidiary companies. These organizations were selected for review because all of them had to compete with the private

sector for managerial staff with special experience and expertise. Many of them are also required to operate under prudent commercial principles.

4. The main tasks of the consultancy study are to determine whether the existing remuneration packages of the senior executives in the bodies under study are in line with those holding comparable positions in the private sector in Hong Kong; establish for them comparable and competitive remuneration packages; formulate different sets of guidelines on remuneration policy and practices for use by these bodies and advise on effective adjustment mechanisms and suitable arrangements of “disclosure” of remuneration information for these bodies.

5. As the Government is separately reviewing the role, mission and range of services of Hong Kong Productivity Council, details of the consultant’s findings pertaining to the Council are not included in the Final Report but forwarded to the Secretary for Commerce and Industry for reference. Hence the report covers 10 selected bodies and two of their subsidiaries.

Analysis of Remuneration Packages

6. The approach and methodology of the study are explained in Parts 2 - 5 of the report. In brief, the consultant invited about 160 private firms in Hong Kong to participate in a survey on the remunerations of their senior executives. Data were subsequently collected from about 80 of them which agreed to take part in the study. Different comparison groups were then proposed for the selected bodies under review. The number of private firms chosen for comparison with each of the bodies varies from ten to 25. The selection of comparison companies for each body under study took into consideration:

- (a) the talent pool from which the body draws its executive talents;
- (b) the industry in which the body operates, or the characteristics of the operating environment of the business; and
- (c) the relevance of general executive and managerial capabilities, where specific comparison companies could not be identified.

7. The consultant has calculated various remuneration aggregates such as base salary, fixed remuneration, short-term incentive, total earning, long-term incentive and total direct compensation for each senior position in these comparison companies. Statistics on the median of the total remunerations were then determined for each tier of the comparison groups. By introducing appropriate adjustments to these medians, the consultant was able to derive different recommended remunerations for the senior executives at different tiers of the selected organizations. The rationale for the adjustments is explained in Part 5 of the report. The major principles are:

- (a) the median of the total remuneration of the relevant tier of the comparison group should provide a reasonable and competitive benchmark for the relevant position under review;
- (b) qualitative factors pertaining to the position under review such as prestige, job security and degree of public scrutiny should apply in determining an appropriate adjustment of the median, if any;
- (c) the prevailing mix (i.e. percentage of fixed pay versus variable component) of remuneration packages applicable to the relevant tiers of the comparison companies should provide the basis for deriving the mix for the relevant body under study. If the consultant does not consider it appropriate for a certain position under review to follow the market remuneration mix, it will recommend a different mix for the post; and
- (d) the governing board or committee of the concerned organization will have the flexibility to use the consultant's recommended conversion factor to derive an equivalent remuneration package with its preferred mix should it wish to have a more significant portion of fixed pay versus the variable pay or vice versa.

8. As far as qualitative adjustment is concerned, the consultant has assessed a number of factors including the size and complexity of the organizations under review, their certainty of availability of resources, job security, exposure to public scrutiny, and prestige and honor of the senior

positions. The consultant came to the view that some of these factors could be justifications for higher salaries while others could work to reduce the remuneration levels. The impacts of these factors should more or less neutralize one another for most of the positions reviewed. The only two positions for which the consultant has proposed a downward adjustment of 10% are the Chief Executive of Hong Kong Monetary Authority and the Chairman of Securities and Futures Commission. There is general perception that these two positions are most influential in that they would affect the functioning of Hong Kong's financial markets, which are among the largest in the world. The two positions enjoy relatively high prestige both locally and internationally.

9. As for the conversion factor for enabling the conversion of some variable portion of a package into fixed remuneration, the consultant has adopted an across the board conversion factor of 1.5 in its calculation. The consultant explained that some private firms have used conversion factors ranging from 2 to 3.5 when they sought to replace a certain portion of the fixed pay of their staff by short-term variable pay. Taking into consideration the nature of the bodies under study and the limit to the reasonable extent of trade-off between certainty of remuneration and variability of total earnings, the consultant considered the use of the factor of 1.5 reasonable.

10. A summary of the consultant's proposed remunerations for the senior executives of the bodies reviewed is at Annex C. The tables contain the following detailed information for each position/ tier of positions reviewed:

- (a) the median level of remuneration of the comparison companies;
- (b) the prevailing market mix;
- (c) the adjustment for qualitative factors; and
- (d) the proposed remuneration level and proposed mix for the position/ tier under review.

Regular Adjustment Mechanism and Disclosure Arrangements

11. On the annual or regular adjustment of remuneration, the consultant has proposed that each of the bodies under review should track the levels and trends of its designated group of comparison companies following a consistent and defensible methodology. It should focus on ensuring that the total direct remunerations of the concerned positions are competitive, with a mix consistent with market practices or as adjusted in line with the characteristics of the organization concerned. Each body should have a committee designated to deal with remuneration issues. The committee should set the remuneration policy for the senior executives, determine the organization's budget for salary adjustments and variable incentive awards, review the market pay levels and trends, and recommend to the governing board or committee the actual salary levels, revisions and bonus payments particularly for the chief executive officer. Where specific legislative provisions apply, the governing board or committee should seek the final approval of the statutory authority as required.

12. The consultant has not included in the Final Report the current remunerations of the senior executives of the bodies under review. Publication of such data would require the consent of the concerned individuals. It will be for the governing boards or committees of these bodies to consider whether and how to address public enquiries about the comparison of their employees' existing remunerations with the consultant's recommended packages. Nevertheless, the consultant has proposed that in the longer run, details of the remuneration of the chief executive of a body should be made public, as well as the aggregate information on the remunerations for the other senior executives. Such arrangement is in line with the trend in overseas countries such as UK. Details of the consultant's recommendations on the adjustment mechanism and disclosure arrangements are in Part 5 of the report.

Assessment

13. The consultant's recommendations on the remuneration levels and mixes of the bodies under review are based on its analyses of the remunerations of the comparison companies and application of the

adjustment principles explained above. The methodology is acceptable. We also consider the concept of introducing adjustments for qualitative factors and enabling conversion between the fixed and variable components of a remuneration package agreeable. The consultant has exercised its professional judgment in the selection of the comparison companies, determination of the percentage figure as the adjustment factor, and calculation of the conversion factor.

14. The governing boards or committees of the concerned organizations should continue to have the discretion to take into account other factors in determining the remunerations of their senior executive appointments. These factors may include:

- (a) the market pay condition for special functional areas;
- (b) the competence, qualification and performance of a particular individual; and
- (c) differences in job nature for positions at the same tier and in levels of accountability for positions at different tiers.

If an organization considers the background, capability or performance of a particular individual serving as the chief executive should justify a higher or lower remuneration than the market median, it could offer him or her a correspondingly different package from what the consultant has recommended. In these circumstances, we expect the governing board or committee of the organization to say so when it discloses information on the remuneration of the individual concerned in future. For the second and third tier positions, we generally consider variations within the range of plus or minus 25% from the consultant's recommended remuneration levels acceptable, particularly to take account of the diverse functions and responsibilities that individual division heads may carry out at these levels. In other words, the remunerations proposed by the consultant should be regarded as indicative rather than absolute references.

15. As for the adjustment and disclosure arrangements, the key principles should be objectivity and transparency. The consultant's

suggestions provide a useful framework for the selected bodies to review their existing policies and mechanisms.

The Way Forward

16. The concerned governing boards or committees play an important role in overseeing the propriety and transparency of the remuneration policies and arrangements, and formulating their recommended remuneration packages to the relevant authority for approval. We will send a copy of the consultant's Final Report, together with the detailed findings and recommendations pertaining to individual organizations to the respective governing boards or committees for consideration of adoption. We will invite the governing bodies to report to the responsible Directors of Bureaux the outcome of their deliberations and the implementation of the consultant's relevant recommendations in six months. We will make it the Administration's policy and require each of these bodies to report annually to its Director of Bureau the detailed remuneration arrangements for each of the three layers of its senior executives, the compliance of the remuneration arrangements with the established principles set out in the consultancy report, any deviations from the principles with justifications, together with a full list of comparison companies used in coming up with the remuneration packages. The Director of Bureau should also be kept informed whenever adjustments to the remuneration policy or packages are made. The concerned boards or committees will also be reminded that their decisions to modify existing remuneration packages should not affect on-going contracts of the senior executives. Rather, they should apply only upon renewal of the contracts of the incumbents or appointment of new executives. We will also remind the governing boards or committees of the need for public disclosure of their remuneration packages and compliance with the established guidelines on an annual basis. In respect of those bodies that are receiving recurrent subvention from Government, they should also give due regard to the subvention guidelines, particularly if they were to consider an increase in the remuneration levels.

FINANCIAL AND STAFFING IMPLICATIONS

17. Implementation of the consultant's recommendations will have no financial or staffing implications for the Government.

ECONOMIC IMPLICATIONS

18. Setting the remunerations of senior executives of statutory organizations and other relevant public bodies with due regard to the respective remuneration structure and trend in the corresponding segment of the manpower market, as well as the particular characteristics and requirements of each of the organizations involved, will enable those organizations to continue to attract and retain the appropriate managerial and professional expertise at the senior level required for conducting their proper functions. In this respect, the recommendations should be positive for both the local manpower market and for the roles such organizations are expected to play for the economy.

SUSTAINABILITY IMPLICATIONS

19. The consultancy study and its recommendations should have no major sustainability implications. Implementation of the study recommendations should in the long run enhance the objectivity and transparency of the remuneration policies and adjustment mechanisms of the bodies under study, whilst maintaining their competitiveness in terms of attracting and retaining well qualified and experienced personnel from the private sector.

PUBLICITY

20. We shall arrange to brief Legislative Council Members and the media. A press release will be issued and a spokesman will be available to answer the media and public enquiries.

ENQUIRY

21. Enquiries to this Legislative Council Brief may be directed to

Mr Sidney Chan, Assistant Director of Administration (Review) at
telephone no. 2810 2205.

Administration Wing
26 June 2002

Annex A

**Final Report:
Review of Remuneration of Senior Executives in
Statutory and Other Bodies**

June 17, 2002

Submitted to:
Government Secretariat

Prepared by:

Hay Group Limited
27/F, 3 Lockhart Road
Wanchai, Hong Kong

HayGroup

Table of Contents

<i>Section</i>	<i>Page</i>
Executive Summary	2
Part 1: Introduction	12
Part 2. Criteria for Selection of Companies to be Surveyed	14
Part 3. Selected Comparison Companies	20
Part 4. Analysis of Remuneration Information	32
Part 5. Principles for Formulating Remuneration Recommendations	34
Part 6. Remuneration Recommendations	52
Part 7. Summary of Findings	63
Appendix 1. Definition of Terms	65
Appendix 2. Valuation of Long-term Incentives	67
Appendix 3. Practices in Overseas Financial Regulators and Central Banks	69
Appendix 4. Application of Qualitative and Conversion Factors	73
Appendix 5. Adjustment for Annual Leave	75
Appendix 6. Adjustment for Retirement Scheme Contributions	77

Executive Summary

The Government has undertaken to conduct a review of the remuneration of senior executives of selected statutory and other bodies. These bodies play the roles of market regulators or service providers, and many of them are required to operate under prudent commercial principles. These bodies are managed by their own senior staff under the guidance of a governing board or advisory committee as appointed by the Government. As far as the terms and conditions of appointment of chief executive officers of most of these bodies are concerned, the final authority of approval is with the Government. Nevertheless, the concerned governing boards still play an important role in overseeing the propriety and transparency of the remuneration policies and arrangements, and formulating their recommended remuneration packages to the relevant authority for approval. The bodies initially included in this review are:

Airport Authority Hong Kong (AAHK)
Hong Kong Monetary Authority (HKMA)
Hong Kong Productivity Council (HKPC)
Hong Kong Science and Technology Parks Corporation (HKSTP)
Hong Kong Tourism Board (HKTB)
Hong Kong Trade Development Council (TDC)
Kowloon-Canton Railway Corporation (KCRC)
Mandatory Provident Fund Schemes Authority (MPFA)
Mass Transit Railway Corporation Limited (MTRCL)
Securities and Futures Commission (SFC)
Urban Renewal Authority (URA)

Also included in this review are two subsidiaries of the HKMA – the Hong Kong Mortgage Corporation (HKMC) and Exchange Funds Investment Limited (EFIL). These subsidiaries were included because they operate with their own executive teams while most subsidiaries of the other bodies do not have separate management teams at the senior executive levels. The Government is currently reviewing the role and mission of HKPC. Therefore the preliminary findings were forwarded to the Secretary for Commerce and Industry for references but are not included in this report.

The scope of the review generally includes the top three layers of each body, including positions such as Chief Executive Officer (CEO), Deputy CEO, Executive Directors, and Directors. Exceptions include the HKMC and EFIL, where the review is focused on the top position only.

This remuneration review has several purposes:

- Establish a consistent set of principles to guide the governing boards of each body in determining remuneration of their senior executives and conducting periodic reviews of remuneration packages in the future.
- Establish a sound basis for determining remuneration with regard to private sector practices in the relevant sectors of the economy.

- Assess the reasonableness of the existing packages of the senior executives against relevant organizations in the private sector, and considering the unique circumstances of these bodies, determine an appropriate level and mix of remuneration for the senior executives.

The recommendations resulting from this review are intended to guide the boards in determining remuneration in the future. Neither the findings nor the recommendations are intended to be prescriptive. Each body should take into account situations or circumstances that may be outside the scope of this study and act on the recommendations accordingly.

Recommendations in this review will be based on several sources of information:

- a survey of remuneration practices of senior executives in private sector companies, with at least 10 comparison companies for each body or subsidiary;
- a review of compensation practices for selected central banks and financial regulators in other countries, relative to private sector practices; and
- background information from each body about their organization, nature of business and operations and their existing policies and strategies for senior executive remuneration.

Remuneration Survey: Data Collection and Analysis

The purpose of the remuneration survey is to provide an indication of compensation levels and the mix of fixed and variable remuneration for chief executives and senior executives in the private sector. The results of the survey form the basis for determining the level and mix of remuneration for senior executive positions in the selected bodies.

Each of the statutory and other selected bodies is unique in terms of their respective purposes and missions. Therefore, precise private sector comparisons may not exist. In compiling the list of comparison companies, emphasis is given, where possible, to organizations in the same or similar industries or sectors. When feasible, an industry- or sector-specific approach was taken rather than a general market survey approach.

For bodies such as HKMA, SFC and MPFA, comparison groups included mainly commercial and retail banks, investment banks, asset management firms, and insurance companies. For other bodies, comparison companies included property developers; infrastructure developers and operators, transport firms, and companies specialized in consumer products, industrial products, trading, communications, and those others as appropriate to the purpose and nature of the bodies. A total of eighty companies participated in the survey and provided remuneration information.

Remuneration information was collected for the top three levels (where relevant) of executives in each of the companies participating in the survey. The information was collected in March 2002 and reflects rates of pay at that time and actual variable remuneration received within the previous twelve months.

Information provided by the company, including the geographic and business unit information, was used as the basis for classifying the jobs as appropriate comparisons for each tier of executive in the selected bodies. Specifically, the following factors were considered:

- Revenues of the company.
- Geographic scope, considering whether the positions were responsible for their respective functions in Hong Kong, China, regionally, or globally.
- Range of businesses or activities, including the variety of product lines or services.
- Organizational structure, considering whether there was a simple hierarchical structure or matrix reporting relationships.

The remuneration comparison group for the chief executive officer(or equivalent) of each selected body was developed by identifying positions of similar scope and responsibility drawn from the relevant comparison group. These comparison positions may or may not be CEOs in the comparison companies but are selected by considering the size of the organization, and the scope and nature of the operations. The median value of remuneration was then calculated for this group of comparison positions.

Second and third tier positions in the selected bodies were analyzed in a similar fashion.

Remuneration Principles

A number of principles were developed to guide the formulation of remuneration recommendations for senior executives of the selected bodies. The fundamental principles applied to develop the recommended remuneration levels and mix for each body are outlined below:

- *Principle 1. Target position in market:* The median of total remuneration of the relevant private sector comparison group represents a reasonable and competitive positioning in the market for senior executives in the selected bodies.

- *Principle 2. Adjustments for qualitative factors:* The business nature and standing of a public body may confer non-financial rewards on the executives that are more substantial than those in private sector companies. These rewards include the opportunity to serve Hong Kong and recognition, honour, and respect. There may also be offsetting disadvantages, such as increased public scrutiny and loss of privacy. If the non-financial rewards are indeed more substantial, it may be possible to attract top talent at levels of remuneration lower than those prevailing in the private sector.
- *Principle 3. Remuneration Mix:* Bodies should adopt a mix of fixed and variable remuneration that is appropriate to their business nature, having regard to the prevailing market practices.
- *Principle 4. Conversion of Variable to Fixed Remuneration:* The appropriate level and mix of remuneration are interrelated. A body should not target its total remuneration at the median of the private sector unless it also follows the mix of remuneration in the private sector. If, per Principle 3, the body chooses to have a higher proportion of fixed remuneration, it must also target a lower level of total remuneration. That is, variable remuneration in the private sector should not be converted into fixed pay in these bodies on a dollar-for-dollar basis. A certain amount of variable remuneration should be converted into a lesser amount of fixed pay.
- *Principle 5. Transparency:* As these bodies are owned, or majority-owned, by the public, the public has a legitimate interest in knowing how remuneration, including level, annual adjustments, and variable pay, is determined. Remuneration should be reasonable and seen to link to the performance of the individual, the organization and its contribution to Hong Kong.

More details about the principles are provided in the following table.

Table 1: Summary of Principles

Area	Principle
Target remuneration level	The median of total direct compensation is used as the starting point for determining the level of remuneration.
Adjustment for qualitative factors	Qualitative factors such as the opportunity to serve Hong Kong, enhanced recognition, honor and respect may attract candidates to the position even with lower remuneration levels. On the other hand, qualitative factors such as higher levels of public scrutiny and the loss of privacy can offset these rewards. An adjustment is made to the remuneration if indicated, having regard to the net effect of these qualitative factors and taking into account the differences in the nature of the selected body and the private sector comparison group.

Table 1: Summary of Principles - continued

Remuneration mix	The prevailing remuneration mix (i.e., fixed and variable remuneration), based on comparison group practices, serves as the benchmark. If performance measurement is generally qualitative or non-financial, and resource acquisition is stable, a mix that favours more fixed remuneration than the benchmark may be appropriate.
Conversion factors	A conversion factor will be used to determine the adjustment between the fixed and variable pay to achieve the recommended mix and the recommended total direct remuneration for the senior executive. The governing board or approving authority of the body may use this conversion factor to arrive at a different remuneration mix with, say, a higher fixed pay and a lower total direct remuneration level.
Total remuneration policy	<p>Each body should adhere to a consistent compensation policy. It should monitor levels and trends of remuneration in relevant or related sectors to ensure that the total remuneration package remains competitive (by adjusting either up or down with market trends). Variable remuneration will be maintained as a targeted percentage of the total remuneration policy.</p> <p>The total remuneration target does not necessarily represent a maximum remuneration level – individual executives may be paid higher or lower depending on special skills or responsibilities required, experience, capabilities, and performance.</p>
Adjustment process	Each body is expected to track levels and trends in relevant and related sectors following a sound and consistent methodology. The intent is to track trends over one or more years and adjusts the fixed and variable remuneration targets accordingly.
Objectivity of process	<p>Each body should have a committee designated to deal with remuneration issues. The remuneration committee will review performance and pay of the chief executive officer of the body subject to endorsement of the full board (or HKSAR Government official when required).</p> <p>The committee will also be expected to endorse the budget for salary increases and variable compensation for other senior executives, but the actual distribution may be delegated to the chief executive.</p>

Table 1: Summary of Principles - continued

<p>Transparency of process</p>	<p>At a minimum, all bodies should follow the levels of disclosure provided for in the Companies Ordinance and as shown in annual reports of companies listed on the Hong Kong Stock Exchange. However, to be consistent with trends in countries such as UK, full disclosure of remuneration of top executives is to be encouraged. Remuneration details of the chief executive officer should be made public, as well as aggregate or average information (or at discretion of the governing board, individual information) of executives in the second and third tiers. Disclosure should include salary and salary adjustments, variable remuneration, and major benefits and perquisites.</p>
<p>Flexibility in implementation</p>	<p>The recommended remuneration mix and levels are based on analysis of the selected comparison groups and application of the principles outlined above. However, the boards or approving authorities of the selected bodies remain accountable and hence should retain the discretion to implement the recommendations appropriately for their organizations.</p> <p>The methodology of this study already determines a “rate for the job” at normal performance level. In the case of the chief executive, the governing board or approving authority of the body could exceed this level of remuneration but does so only where the background, capability or performance of the chief executive officer clearly justifies the higher level of remuneration.</p> <p>In the case of executives in the other tiers, recommendations are presented as target policy levels but each body retains flexibility to determine pay for jobs or individual executives within reasonable bounds. A range of plus or minus 25% is common market practices. Remuneration can therefore vary within this range by having regard to factors such as:</p> <ul style="list-style-type: none"> ▪ market pay conditions for specific functional areas ▪ individual performance and competency ▪ differences in levels of accountability between positions as determined by the internal processes of the body

Remuneration Recommendations

The summary of recommendations for remuneration levels and mix are shown in the following table which shows:

- The median total direct compensation (which includes base salaries, allowances including housing, short-term variable compensation and long-term incentives) for the comparison group of each body;
- The qualitative adjustment factor made with respect to considerations such as enhanced recognition, honor, and respect, after offsetting disadvantages such as increased public scrutiny and lack of privacy. In this review, an adjustment is applied only to the chief executives of HKMA and the chairman of SFC;
- The mix of variable remuneration in the relevant comparison group, measured as a percentage of the total direct compensation;
- The proposed mix of variable remuneration for each body, considering the body's mission and its nature of business; and
- The proposed remuneration for each body, considering the proposed mix of variable remuneration.

The proposed remuneration is determined by applying the conversion factor, which is set at a value of 1.5. This conversion factor value denotes that the senior executive in the body will receive \$1 in fixed remuneration for every \$1.5 in comparison group variable remuneration converted, whereas the total remuneration will consequently be reduced by \$0.5.

If the body chooses to adopt the market level of variable remuneration, then there is no need to make any conversion. Likewise, if the body chooses a different level of variable remuneration than is proposed here, the total remuneration and mix would be varied using the same conversion factor.

Table 2: Summary of Recommendations: Remuneration Level and Mix

	HKMA	SFC	MPFA	MTRCL	KCRC	AAHK	URA	STP	HKTB	TDC
Tier 1: Chief Executive Officer or Equivalent										
Comparison Group Median	9,558	9,558	5,292	6,934	5,941	5,941	4,920	3,875	3,800	5,084
Qualitative Factor	-10%	-10%	0%	0%	0%	0%	0%	0%	0%	0%
Market Mix (% variable)	64%	67%	36%	48%	40%	40%	40%	46%	37%	27%
Proposed Mix (% variable)	20%	15%	15%	40%	40%	40%	25%	25%	20%	25%
Total Remuneration (at Proposed Mix)	7,250	7,033	4,902	6,721	5,941	5,941	4,652	3,579	3,569	5,047
Second Tier Executives										
Comparison Group Median	5,011	4,734	3,654	4,074	4,074	3,299	2,963	2,094	2,157	3,075
Qualitative Factor	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Market Mix (% variable)	42%	46%	34%	33%	33%	32%	32%	20%	16%	26%
Proposed Mix (% variable)	15%	15%	15%	30%	30%	30%	20%	20%	15%	20%
Total Remuneration (at Proposed Mix)	4,536	4,219	3,410	4,029	4,029	3,275	2,836	2,094	2,149	3,009
Third Tier Executives										
Comparison Group Median	3,280	2,734	2,469	N/A.	3,299	N/A.	2,093	1,565	1,472	2,184
Qualitative Factor	0%	0%	0%	N/A.	0%	N/A.	0%	0%	0%	0%
Market Mix (% variable)	45%	34%	29%	N/A.	32%	N/A.	20%	21%	26%	20%
Proposed Mix (% variable)	15%	15%	15%	N/A.	30%	N/A.	20%	20%	15%	20%
Total Remuneration (at Proposed Mix)	2,935	2,552	2,348	N/A.	3,275	N/A.	2,093	1,559	1,415	2,184

Notes: (1) Total Remuneration consists of fixed and variable remuneration in the proportion indicated by proposed mix.

(2) Second and third tier remuneration levels may vary within a range of 25% around the total remuneration indicated.

(3) Further adjustment may be required, at the discretion of governing board or approving authority, for jobholders serving as Chairman in addition to CEO.

(4) Total remuneration (at Proposed Mix) based on the conversion factor of 1.5.

Findings

Remuneration information was provided to Hay Group by the selected bodies with the understanding that it would not be disclosed without the consent of the bodies and the concerned executives. Therefore we instead provide a brief summary of the findings of the comparisons of remuneration of executives of the bodies to their respective private sector comparison groups. The following table summarizes the position of each tier or level across the bodies relative to (a) the median of the respective comparison groups and (b) the proposed remuneration level which has taken into account adjustments for qualitative factors, differences in remuneration mix, retirement policies and annual leave policies.

Table 3: Comparison of Remuneration in the Selected Bodies to Market Median and Proposed Remuneration (at Proposed Mix)

Tier	Comparison to Market Median	Comparison to Proposed Remuneration
CEO	<p>70% of CEOs (or equivalent) within 15% of median of their respective comparison groups. The remaining are more than 15% below median.</p> <p>In several cases, CEOs of these bodies did not receive variable remuneration in the past 12 months but are eligible for consideration of such variable remuneration in the future under the terms of existing remuneration policies. If these CEOs were able to receive all the potential variable payments, almost all of them would be within 15% of the median.</p>	<p>60% of CEOs are currently paid within 15% of the proposed remuneration level after taking into account qualitative adjustments, the impact of differences in proposed and market remuneration mix, and the impact of adjustments for retirement and annual leave policies. Most of those outside this range are higher. However, the current mix of remuneration includes, in most cases, a much higher proportion of fixed remuneration than is proposed in this study.</p> <p>If potential variable payments under the terms of existing remuneration policies are included, one other CEO would fall within 15% of the proposed remuneration level.</p>
2	<p>The average level of Tier 2 remuneration in each body is within 15% of the comparison group median, except for one body. That body is more than 15% below the median.</p> <p>Consideration of potential variable payments would not change these conclusions.</p>	<p>In 70% of cases, the average level of Tier 2 remuneration in each body is within 15% of the proposed remuneration level after adjusting for differences in the proposed and market remuneration mix as well as for annual leave and retirement policies. If potential variable remuneration (under terms of current policies) is included, then all but one body would fall within 15% of the proposed level. The exceptional case is higher than this range.</p> <p>Again, the current mix of remuneration includes a substantially higher proportion of fixed remuneration than is proposed in this study.</p>
3	<p>The average level of Tier 3 remuneration is within 15% of the median for most bodies; there are two exceptions where average Tier 3 remuneration is above this level.</p> <p>Consideration of potential variable payments under current remuneration policies would produce the same aforementioned conclusions.</p>	<p>The average level of Tier 3 remuneration is within 15% of the proposed remuneration level for most bodies after similar adjustments as for Tier 2. There are two exceptions that are above this level.</p> <p>Consideration of potential variable payments under current remuneration policies would produce the same aforesaid conclusions.</p>

Other findings include:

- *Level of remuneration:* For most bodies and most levels within each body, the current level of remuneration is within 15% of the respective comparison group median.
- *Mix of remuneration.* With only a very small number of exceptions, the remuneration packages of senior executives in the selected bodies include a substantially higher proportion of fixed remuneration compared to the private sector, and much lower short-term and long-term variable remuneration. The proposed variable remuneration for each body is usually less than that in the private sector, but in most cases the proposed mix includes a higher proportion of variable remuneration than called for in the current policies of the bodies.
- *Retirement schemes.* These also varied across bodies. Some provided only minimal MPF contributions, whilst others provided for high contribution rates or gratuities applied to levels of fixed remuneration higher than those prevailing in the private sector. The proposed adjustment ensures that total remuneration is competitive after considering the impact of retirement schemes. Most adjustments were positive (increases in cash remuneration levels in cases where a minimal MPF contribution is made), and there was only one case where a substantial negative adjustment was required.
- *Annual leave.* Some bodies were in line with market practices on level of annual leave, but some others had high annual leave entitlements, and more had high accrual limits. Adjustments for high accrual limits were made for half of the bodies in this study.
- *Comparison of current remuneration and proposed remuneration.* According to the principles set out in this study, median remuneration is the starting point for establishing the proposed level and mix of remuneration. The market median level has been adjusted to take into account qualitative factors, differences in mix of fixed and variable remuneration, and retirement and annual leave policies that deviate significantly from market practices. As shown in the table above, most bodies current remuneration levels are within 15% of the proposed level, but the current mix of remuneration contains a much higher proportion of fixed remuneration than called for in the recommendations.
- *Salary adjustment mechanisms.* Most of the bodies had regular processes for reviewing senior executive remuneration involving use of formal remuneration surveys with review by either the chairman of the organization or a remuneration committee.
- *Transparency.* Most bodies had been disclosing or already plan to begin disclosing remuneration of senior executives in annual reports, as is required for companies listed on Hong Kong's stock exchange. Several, however, have not been doing so.

Part 3. Selected Comparison Companies

14. Comparison groups for each body were selected from the participating companies having regard to the criteria outlined above and the industry sectors described in Table 1. The comparison groups for each body are presented below with brief explanation.
15. The major factors considered in forming the comparison groups are the relevance of the sectors in which the comparison companies operate as well as the scope of the responsibilities of senior executive positions in the comparison companies relative to the responsibilities of senior executives in the selected body. For example, the CEO of a comparison company may be comparable to a second-tier executive in the selected body. Alternatively, the CEO of the selected body may be compared to second-tier executives in the comparison company. Therefore, not all companies included in the comparison group are used as comparisons for every level of executive in the selected body.
16. The number of comparison companies varies by selected body. The minimum number of comparison companies is 10 but usually larger numbers of companies were selected to provide a more representative basis of comparison.

HKMA

The comparison companies comprise a representative group of nine banks, which are regulated by HKMA; five asset management firms, as HKMA is engaged in substantial asset management activities; and two professional services firms, from which some executives may also be recruited. The commercial banks (including two additional banks, for a total of eleven) also serve as the comparison group for Chief Executive - HKMC, whilst ten asset management firms form the comparison group for Chief Executive - EFIL.

Table 3 (a): Comparison Table for HKMA

Comparison Companies	Nature of Business
Asset management	
Citigroup Asset Management	Asset management
Dresdner RCM Global Investor	Asset management
INVESCO Asia Limited	Asset management and sales
Schroder Investment Management	Asset management and sales
Templeton Investment Management	Asset management and sales
Corporate and retail banking	
ABN-Amro ¹	Corporate banking, equities, and investment banking
Bank of America ¹	Corporate and retail banking
Bank of Bermuda ²	Trustee and custodial
Bank of East Asia ¹	Corporate and retail banking
BNP Paribas ¹	Corporate banking, equities, and investment banking
Citibank ¹	Corporate, retail and private banking
Fortis ¹	Corporate, retail, private banking and capital markets
HSBC ¹	Corporate, retail and private banking, trustee
JP Morgan Chase ¹	Corporate and investment banking
Shanghai Commercial Bank ²	Commercial and retail banking
Standard Chartered Bank ¹	Corporate and retail banking
Professional Services	
KPMG	Accounting firm
Kwok & Yih	Law firm
EFIL Comparison Group – Asset Management	
ABN Amro Asset Management	Asset management and sales
AXA Investment Managers	Asset management
Citigroup Asset Management	Asset management
Credit Agricole Asset Management	Asset management
Dresdner RCM Global Investor	Asset management
Fortis Asset Management	Asset management
INVESCO Asia Limited	Asset management and sales
Manulife Financial	Asset management and sales
Schroder Investment Management	Asset management and sales
Templeton Asset Management	Asset management and sales

¹ Member of comparison group for HKMC

² Member of comparison group of HKMC but not HKMA

Summary of Principles

72. Table 5 summarizes the principles that will be used in determining remuneration targets and mix for the selected bodies.

Table 5. Summary of Principles

Area	Principle
Target remuneration level	The median of total direct compensation is used as the starting point for determining the level of remuneration.
Adjustment for qualitative factors	Qualitative factors such as the opportunity to serve Hong Kong, enhanced recognition, honor and respect may attract candidates to the position even with lower remuneration levels. On the other hand, qualitative factors such as higher levels of public scrutiny and the loss of privacy can offset these rewards. An adjustment is made to the remuneration if indicated, having regard to the net effect of these qualitative factors and taking into account the differences in the nature of the selected body and the private sector comparison group.
Remuneration mix	The prevailing remuneration mix (i.e., fixed and variable remuneration), based on comparison group practices, serves as the benchmark. If performance measurement is generally qualitative or non-financial, and resource acquisition is stable, a mix that favours more fixed remuneration than the benchmark may be appropriate.
Conversion factor	A conversion factor will be used to determine the adjustment between the fixed and variable pay to achieve the recommended mix and the recommended total direct remuneration for the senior executive. The governing board or approving authority of the body may use this conversion factor to arrive at a different remuneration mix with, say, a higher fixed pay and a lower total direct remuneration level.

Table 5. Summary of Principles - continued

<p>Total remuneration policy</p>	<p>Each body under review should adhere to a consistent compensation policy. It should monitor levels and trends of remuneration in relevant or related sectors to ensure that the total remuneration package remains competitive (by adjusting either up or down with market trends). Variable remuneration will be maintained as a targeted percentage of the total remuneration policy.</p> <p>The total remuneration target does not necessarily represent a maximum remuneration level – individual executives may be paid higher or lower depending on special skills or responsibilities required, experience, capabilities, and performance.</p>
<p>Adjustment process</p>	<p>Each body is expected to track levels and trends in relevant and related sectors following a sound and consistent methodology. The intent is to track trends over one or more years and adjusts the fixed and variable remuneration targets accordingly.</p>
<p>Objectivity of process</p>	<p>Each body should have a committee designated to deal with remuneration issues. The remuneration committee will review performance and pay of the chief executive officer of the body subject to endorsement of the full board (or HKSAR Government official when required).</p> <p>The committee will also be expected to endorse the budget for salary increases and variable compensation for other senior executives, but the actual distribution may be delegated to the chief executive.</p>
<p>Transparency of process</p>	<p>At a minimum, all bodies should follow the levels of disclosure provided for in the Companies Ordinance and as shown in annual reports of companies listed on the Hong Kong Stock Exchange. However, to be consistent with trends in countries such as UK, full disclosure of remuneration of top executives is to be encouraged. Remuneration details of the chief executive officer should be made public, as well as aggregate or average information (or at discretion of the governing board, individual information) of executives in the second and third tiers. Disclosure should include salary and salary adjustments, variable remuneration, and major benefits and perquisites.</p>

Table 5. Summary of Principles - continued

<i>Area</i>	<i>Principle</i>
Flexibility in implementation	<p>The recommended remuneration mix and levels are based on analysis of the selected comparison groups and application of the principles outlined above. However, the boards or approving authorities of these selected bodies remain accountable and hence should retain the discretion to implement the recommendations appropriately for their organizations.</p> <p>The methodology of this study already determines a “rate for the job” at normal performance level. In the case of the chief executive officer, the governing board or approving authority of the body could exceed this level of remuneration but does so only where the background, capability or performance of the chief executive officer clearly justifies the higher level of remuneration.</p> <p>In the case of executives in the other tiers, the recommendations are presented as target policy levels but each body retains flexibility to determine pay for jobs or individual executives within reasonable bounds. A range of plus or minus 25% is common market practices. Remuneration can therefore vary within this range by having regard to factors such as :</p> <ul style="list-style-type: none"> ▪ market pay conditions for specific functional areas ▪ individual performance and competency ▪ differences in levels of accountability between positions as determined by the internal processes of the body

Part 6. Remuneration Recommendations

73. Tables 6(a) – 15(a) show the market median remuneration levels corresponding to each level of executive in each body in this study. The tables show the median values of each aggregate and component of total direct compensation. Note that the sum of median values of each component of remuneration do not equal the median of the aggregate.
74. Tables 6(b) – 15(b) show the proposed remuneration level and mix for each body. The median (after adjustment for any qualitative factor) represents the targeted level of remuneration, if the market mix of fixed and variable remuneration is applied. The proposed remuneration reflects the proposed mix (as shown in Table 4), and results from the application of the conversion factor to the market median total remuneration.
75. In accordance with the terms of reference for this study, Hay Group have compared the current remuneration practices of each body to the remuneration practices of the respective private sector comparison groups. The bodies have been fully cooperative in providing the necessary information to Hay Group. However, these bodies provided information to Hay Group on the understanding that it would not be publicly disclosed without the consent of the bodies and the concerned executives. Those bodies that adopt our recommendations on transparency will, in due course, make the information available. Accordingly, the current remuneration practices of the bodies are not disclosed in the following tables.
76. Further adjustments to the remuneration recommendations in Tables 6(b) – 15(b) would be required with respect to annual leave or retirement schemes. These adjustments are not shown as they also relate to the confidential remuneration packages of the jobholders.
77. The recommendations shown in these tables are illustrative of the application of the principles presented in this report. The implementation of these principles, including the timing of implementation, is left to the discretion of the governing boards of these bodies, according to the specific contractual and other circumstances that may influence their decision-making.

Table 6(a). Median Remuneration for Comparison Group of Hong Kong Monetary Authority

Comparison Group Median:	Base Salary (HK\$000)	Allowances (HK\$000)	Fixed Remuneration (HK\$000)	Short-Term Incentives (HK\$000)	Total Earnings (HK\$000)	Long-Term Incentives (HK\$000)	Total Direct Compensation (HK\$000)
Chief Executive Officer – HKMA	2,262	600	3,463	3,639	6,780	1,363	9,558
Deputy Chief Executive Officer	1,907	834	2,854	1,357	4,697	343	5,011
Executive Director	1,568	272	1,810	601	2,382	373	3,280
Chief Executive Officer – HKMC	1,823	876	2,585	1,336	3,927	317	3,986
Chief Executive Officer – EFIL	2,015	686	2,640	947	3,369	380	4,170

Table 6(b). Remuneration Recommendations - Hong Kong Monetary Authority

	Chief Executive Officer	Deputy CEO	Executive Director	CEO - HKMC	CEO - EFIL
Comparison Group Median	9,558	5,011	3,280	3,986	4,170
Qualitative Factor	-10%	0%	0%	0%	0%
Adjusted Median (at Market Mix)	8,602	5,011	3,280	3,986	4,170
Market Mix (% variable)	64%	42%	45%	35%	37%
Proposed Mix (% variable)	20%	15%	15%	25%	25%
Total Remuneration (at Proposed Mix)	7,250	4,536	2,935	3,841	3,988
Fixed Remuneration (at Proposed Mix)	5,800	3,856	2,495	2,881	2,991
Variable Remuneration (at Proposed Mix)	1,450	680	440	960	997
Maximum Remuneration (+25%)	N/A.	5,670	3,668	4,801	4,985
Minimum Remuneration (-25%)	N/A.	3,402	2,201	2,881	2,991

Appendix 3: Practices in Overseas Financial Regulators and Central Banks

Hay Group have collected information about remuneration practices from central banks and financial regulators in United States, United Kingdom, and Japan. The primary source of information is Hay Group based on its experiences working with these organizations, as well as publicly available data and some information provided directly by the organizations concerned.

Table A3.1 summarizes information regarding the competitiveness of remuneration relative to the private sector and civil service (including ministerial salaries), as well as use of variable remuneration.

The table shows, in general, that remuneration practices may be similar to or above civil service pay levels, but in no way reach to competitive pay levels when compared to international financial sector practices. The tables also indicate that use of variable remuneration is sparse.

Bank of Japan is somewhat of an exception in that remuneration may be similar to executive remuneration for major Japanese banks. Because of the banking crisis and government support to the industry, the banking sector has significantly reduced pay relative to earlier practices, at the request of the government. It is expected that in several years, these salaries may be raised again at which point Bank of Japan pay may not be as competitive. We also note that executive remuneration in Japanese banks is significantly lower than the pay levels that prevail in the US and UK.

The explicit qualitative adjustment of 10% recommended for the chief executive officer of HKMA and the chairman of SFC appears to be smaller than the implicit differential between remuneration practices in US and UK relative to the financial sector pay practice. We believe that the higher remuneration levels that result can be justified by considering the needs of these Hong Kong-based bodies.

Arguably, the scope of responsibilities of the executives of these American, British and Japanese organizations are broader, but the nature of expertise required is similar and the required calibre of executive is the same. Hong Kong's need for expertise is not significantly lower simply because Hong Kong's markets are smaller. The Hong Kong bodies must either recruit from a much smaller local market than in other countries, or, alternatively, must attract overseas talent to come to, or remain in, Hong Kong. Given the need to compete for a small talent pool, and the high cost of living, it is appropriate for Hong Kong to consider higher levels of remuneration than may prevail in these other countries.

Table A3.1. Remuneration Practices in Overseas Central Banks and Financial Regulators

Organization	Practices
<p>Securities and Exchange Commission (US)</p>	<p>Unlike other financial regulators like Federal Reserve Bank of Federal Depository Insurance Corporation, SEC currently pays at civil service levels. Commissioners are paid less than US\$140,000 per annum, according to a scale that establishes relativities between Vice President, cabinet secretaries, members of Congress and commissioners in independent agencies.</p> <p>The current pay scale for other executives follows the civil service practice. However, Congress has approved the introduction of higher pay scales that would be more in line with practices at other regulators. However, the funding for the new pay scales has not in fact been approved and are therefore not implemented. In the proposed pay scale, the top pay would reach to about US\$184,000 per annum. This new pay scale would not affect commissioners, who would remain at the same, lower pay level.</p> <p>While the new pay scale would be competitive with other regulators, these pay levels are known to be significantly lower than prevail in the private sector (banks, exchanges, securities firms, law firms). Retention is a major issue, hence the effort to implement the new pay scale. However, service in SEC and other regulators is viewed by many as a positive career step that increases the value of the employee within financial services industry as well as with law firms.</p> <p>SEC does not use variable remuneration at this time.</p> <p>All pay scales are public.</p>
<p>Federal Reserve (US)</p>	<p>The Chairman of the Federal Reserve bank is paid less than US\$140,000 per year. Other employees are paid on a scale that is higher than the civil service, but significantly lower than market practices. The pay scale is roughly competitive with the new scale being proposed for SEC.</p> <p>Federal Reserve does not use variable remuneration at this time. All pay scales are public.</p>

Table A3.1. Remuneration Practices in Overseas Central Banks and Financial Regulators - continued

<p>Financial Service Authority (UK)</p>	<p>This is the super-regulator of banks, securities firms and the insurance industry. It is a private company, but government owned. They do not view their pay as fully competitive with the private sector, and many of their executives took pay cuts to serve with FSA.</p> <p>The Chairman's remuneration (2000-2001) was £290,000, whilst the Managing Directors were paid £235,000. They are eligible for bonuses of up to 15% on generally qualitative measures. The next level of executives are paid around £155,000.</p> <p>Pay of the three top executives is published in detail in annual reports.</p>
<p>Financial Services Agency (Japan)</p>	<p>This financial regulator pays on civil service terms and conditions. The head of the agency would be paid below the level of a minister so Hay Group's estimate of the remuneration would be in the area of US\$200,000 or more. There is no variable remuneration.</p> <p>Transparency of remuneration information is low.</p>
<p>Bank of Japan</p>	<p>The Bank of Japan in the past paid competitively with major Japanese banks. It is Hay Group's estimate that, in the past, CEOs of Japanese banks were paid approximately US\$600,000 - US\$700,000 per year, and that this would have been the remuneration of the Chairman of the Bank. However, due to the banking crisis in Japan, it is believed that salaries of top executives in the banking sector have been cut by approximately half.</p> <p>Three years ago, a new law was introduced that set the pay for the Chairman of the Bank of Japan to be equivalent to the pay of a minister such as Finance Minister, or about US\$300,000. Pay for other levels of executives must be lower than this amount but competitiveness should be maintained with Japanese banks to the extent possible within this limitation.</p> <p>Because of the reduction in banking salaries, current Bank of Japan remuneration is probably competitive with the private sector. However, this may not remain the case once pay of Japanese banking executives is restored to earlier levels.</p> <p>There is no variable remuneration, and transparency of remuneration information is low.</p>

**Review of Remuneration of
Senior Executives of Statutory and Other Bodies**

Scope

1. Airport Authority Hong Kong
2. Hong Kong Monetary Authority*
3. Hong Kong Productivity Council
4. Hong Kong Science and Technology Parks Corporation
5. Hong Kong Tourism Board
6. Hong Kong Trade Development Council
7. Kowloon-Canton Railway Corporation
8. Mandatory Provident Fund Schemes Authority
9. Mass Transit Railway Corporation Limited
10. Securities and Futures Commission
11. Urban Renewal Authority

* The study also covers two subsidiaries of the Hong Kong Monetary Authority, viz. the Exchange Fund Investment Limited and the Hong Kong Mortgage Corporation Limited.

Summary of Proposed Remuneration

	HKMA	SFC	MPFA	MTRCL	KCRC	AAHK	URA	STP	HKTB	TDC
Chief Executive										
Comparison Group Median*	9,558	9,558	5,292	6,934	5,941	5,941	4,920	3,875	3,800	5,084
Market Mix (% variable)	64%	67%	36%	48%	40%	40%	40%	46%	37%	27%
Qualitative Factor	-10%	-10%	0%	0%	0%	0%	0%	0%	0%	0%
Proposed Mix (% variable)	20%	15%	15%	40%	40%	40%	25%	25%	20%	25%
Total Remuneration (at Proposed Mix)*	7,250	7,033	4,902	6,721	5,941	5,941	4,652	3,579	3,569	5,047

(*in HK\$000)

Summary of Proposed Remuneration

	HKMA	SFC	MPFA	MTRCL	KCRC	AAHK	URA	STP	HKTB	TDC
Second Tier Executives										
Comparison Group Median*	5,011	4,734	3,654	4,074	4,074	3,299	2,963	2,094	2,157	3,075
Market Mix (% variable)	42%	46%	34%	33%	33%	32%	32%	20%	16%	26%
Qualitative Factor	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Proposed Mix (% variable)	15%	15%	15%	30%	30%	30%	20%	20%	15%	20%
Total Remuneration (at Proposed Mix)*	4,536	4,219	3,410	4,029	4,029	3,275	2,836	2,094	2,149	3,009

	HKMA	SFC	MPFA	MTRCL	KCRC	AAHK	URA	STP	HKTB	TDC
Third Tier Executives										
Comparison Group Median*	3,280	2,734	2,469		3,299		2,093	1,565	1,472	2,184
Market Mix (% variable)	45%	34%	29%		32%		20%	21%	26%	20%
Qualitative Factor	0%	0%	0%		0%		0%	0%	0%	0%
Proposed Mix (% variable)	15%	15%	15%		30%		20%	20%	15%	20%
Total Remuneration (at Proposed Mix)*	2,935	2,552	2,348		3,275		2,093	1,559	1,415	2,184

(*in HK\$000)