STATE SERVICES COMMISSION
Te Komihana O Ngā Tari Kāwanatanga

Executive Pay in the State Services

Annual reporting of chief executive remuneration

Cabinet has agreed that remuneration paid to Public Service and Crown entity chief executives should be disclosed annually in one location. This provides transparency for the taxpaying public around the level of remuneration received by senior State servants.

The information disclosed each year presents the total remuneration actually received by each chief executive for the financial year in $10,000 bands. Total remuneration includes any benefit received by the chief executive that is specified in their employment agreement, such as performance pay, employer contributions to superannuation, the value of the use of a vehicle, any annual leave in excess of the 20 days per annum, and any end of term entitlements paid.

Chief executives' reported remuneration may vary significantly from year to year. This may reflect:

- The timing of pay periods during the year, which may result in a chief executive receiving 27 fortnightly pays during the year. This occurred in 2014/15.
- The timing of performance and remuneration reviews and performance payments can result in one or more than one performance payment being made during the year, and back-pay of any remuneration increases. In 2014/15 performance payments for Public Service chief executives covered a performance period of six months only and were pro-rated accordingly.
- Measured job size increases leading to an increase in remuneration (chief executive job sizing is undertaken by independent consultants).
- Entitlements on the last day of duty, which may include retiring leave, annual leave not taken, employer superannuation payments owing on end of term entitlements.

The report on the remuneration received by State sector chief executives in 2014/15 is available here.

Remuneration movements in 2014/15

Remuneration increases for the Public Service and Crown entity chief executives for the 2014/15 year were as follows:

Crown entities

Crown entity chief executives have their performance and remuneration reviewed annually by their Board/Chair, on a date specified in their employment agreement (usually their anniversary date).

District Health Board (DHB) and Tertiary Education Institution (TEI) chief executive remuneration requires the concurrence of the State Services Commissioner (the Commissioner). Chief executive remuneration for other statutory Crown entities requires consultation with the State Services Commission (SSC) and, in cases of disagreement with SSC, with Ministers.

The Commissioner provides all board chairs with guidance when considering increases to chief executive remuneration which is consistent with remuneration movements in the broader State sector workforce. This indicates the Commissioner's expectations for reasonable increases, taking into account individual performance, and a chief executive's position in a remuneration range. The guidance indicated increases for chief executives meeting expectations of between 2% and 3%.

- Overall actual remuneration movements were in line with the Commissioner's guidance. The median percentage increase for all **Crown entity chief executives** in 2014/15 was 2.5%, which was similar to increases in 2013/14, and in line with the combined effect of salary progression and collective agreement settlements during the period.

- Chief executive remuneration is based on job sizing measured by independent consultants. As is the case every year, some chief executives receive additional increases to recognise job size increases. This was the case for eight chief executives during 2014/15. When these additional increases are excluded, the median increase overall is reduced to 2.2%. The increases for the different types of Crown entities are summarised in the table below.

By comparison, Strategic Pay Limited measured a 7% median increase in fixed remuneration for New Zealand private sector chief executives (same incumbents) in the 12 months to June 2015.

Public Service

Under the State Sector Act 1988, the Commissioner is the employer of most Public Service chief executives and is responsible for their appointment and performance management, and the setting and reviewing of their terms and conditions of employment. This excludes those chief executives whose remuneration is set by the Remuneration Authority, which includes the chief executives of the State Services Commission, the Crown Law Office and the Government Communications Security Bureau.

The framework for remuneration for Public Service chief executives is also set with a view to the movements in the rest of the State sector workforce. This provided for increases of between 1% and 5%, depending on performance and position in range. Public Service chief executives in general only have their remuneration reviewed once during a term of more than three years.

- In 2014/15, the median increase to Target Remuneration for **Public Service chief executives** (excluding those whose remuneration is set by the Remuneration Authority) was 2.0%, and the average was 1.7%. This is based on movements ranging from 0% to 4% for the 10 chief executives who received a remuneration review during the year, which translates to an average increase of 0.7% across all chief executives. This compares to an average increase in remuneration in the 2013/14 year of 2.8%.
- In addition, in 2014/15 chief executives received the following portion of their at risk components (based on performance in the 2013/14 year):
  - 17 of the 23 eligible chief executives (74%) received their full 10% earn back component, and
  - Only five chief executives received a portion of the 15% exceptional performance component, ranging from 3% to 5%.

The appropriation for Public Service chief executive remuneration is capped by the Government and the Commissioner allocates within this. Appropriation and actual spend are at around the same level as they were in 2008/09. In 2014/15 the spend was $12.189m, $1.413m below the cap.

As at 30 June 2015, the base salary of a Public Service chief executive was, on average, 5.7 times the average pay for staff of the department. This has remained relatively stable over the last four years.

Some chief executive roles will receive lower remuneration than second tier managers (often in larger departments) because remuneration is based on the size of the job and the individual's overall level of responsibility.

State sector workforce

The Government has set expectations for pay and employment conditions in the State sector, which sets the framework for bargaining and remuneration decisions. The expectations can be viewed here**.**

- The Statistics NZ survey, the Labour Cost Index is a measure of wage inflation. The movements for the 2014/15 financial year show that the **Public Service wage** moved 0.9%, compared to 1.2% for the broader Public sector, and 1.8% for the private sector.
- Typically the combined effect of salary progression and **Public Service collective agreement settlements** in 2014/15 resulted in average remuneration increases of between 1.5% and 2.5%.

For more information about the remuneration paid in the Public Service, read the Remuneration chapter of the Human Resource Capability report at www.ssc.govt.nz/hrc-survey-2015.

Remuneration movement guidance for 2014/15

State sector chief executive remuneration is lower on average than remuneration for equivalent sized private sector roles. Public Service chief executive remuneration is lower on average than remuneration paid to chief executives in the wider State sector with similar sized roles.

The Commissioner takes a conservative approach around increases to remuneration for Public Service and Crown entity chief executives. However, there are instances where larger increases to remuneration are supported by the Commissioner, for example, where there has been a significant increase in a chief executive's job size.

Crown entity chief executive remuneration is set by Crown entity boards after consultation with the Commissioner. The Commissioner provides all board chairs with guidance when considering increases to CE remuneration which is consistent with remuneration movements in the broader State sector workforce. This indicates the Commissioner's expectations for reasonable increases, taking into account individual performance, and a chief executive's position in a remuneration range. The guidance, summarised in the table below, indicated increases for CEs meeting expectations of between 2% and 3%.

		Crown Entity Chief Executive Matrix 2014/15			
		Position against range midpoint			
		< 90% – 95%	96% - 100%	101% - 105%	106% - > 110%
Performance Rating	Exceeded expectations	3.5%	3%	2.5%	2%
	Met expectations	2.5%	2%	2%	1.5%
	Developing in the role	2%	1.5%	1%	1%
	Not meeting expectations	0%	0%	0%	0%

The Commissioner uses a similar method for determining increases to Public Service chief executive remuneration which is also set with a view to the movements in the rest of the State sector workforce. The approach used for determining Public Service increases in 2014/15 is summarised in the table below.

		Public Service Chief Executive Matrix 2014/15			
		Position against zone effective midpoint			
		<90% - 96%	96% - 100%	100% to 104%	104% - >110%
Performance Rating	Exceeds expectations	5%	4%	3%	2%
	Exceeds in some expectations	4%	3%	2%	1%
	Meets expectations	3%	2%	1%	0%
	Partially meets expectations	2%	1%	0%	0%
	Does not meet expectations	0%	0%	0%	0%

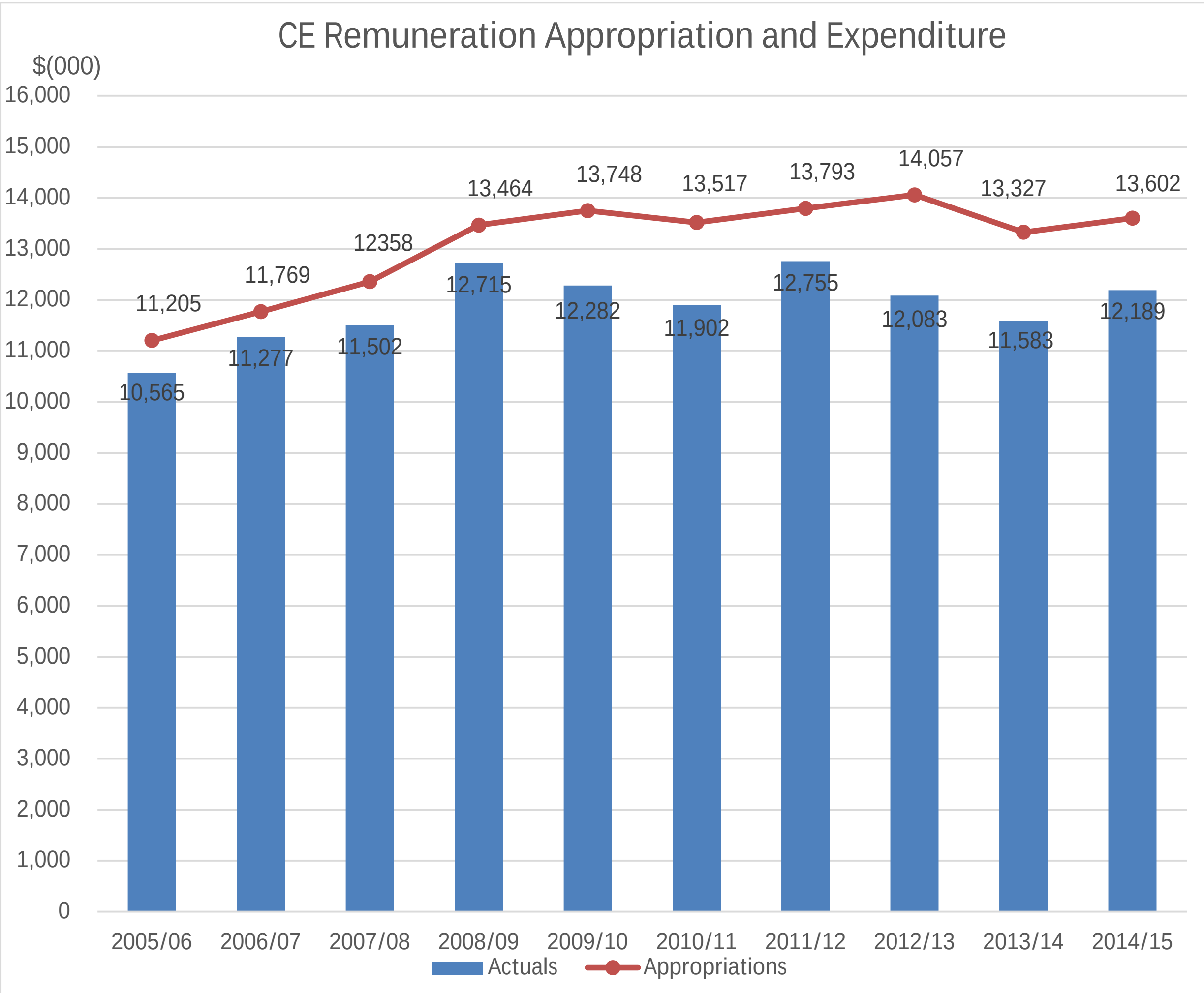
This is structured slightly differently to the guidance for Crown entity chief executives, as it recognises that Public Service chief executive remuneration lags behind that of Crown entity chief executives in similar size roles. However, steps to align the Crown entity and Public Service guidance more closely have been taken as part of the 2015 review process.

Public Service chief executive remuneration expenditure

The appropriation for Public Service CE remuneration is capped by the Government and the State Services Commissioner allocates within this. Appropriation and actual spend are at around the same level as they were in 2008/09, reflecting a consistently conservative approach to the use of taxpayer money.

- In 2014/15 the total amount spent on Public Service chief executive remuneration was $12.189 million, which was $1.413 million below the cap. The expenditure was $0.606 million up on 2013/14, reflecting the appointment into the long-vacant Ministry of Health position and the payment of a higher number of end-of-term leave and performance pay entitlements for the outgoing chief executives of the Canterbury Earthquake Recovery Authority, Ministry for Culture and Heritage, Ministry for the Environment and the Ministry of Foreign Affairs and Trade.

Figure 1: Appropriation and Actual Expenditure for Remuneration and Related Employment Costs of Chief Executives



Notes:

- Figure 1 shows the appropriation for remuneration and related employment costs and actual expenditure on remuneration, training and development, relocation costs and end of term payments for Public Service chief executives.
- Both the appropriation and the expenditure increased during the period 2006/07 to 2008/09, reflecting more buoyant labour market conditions and to allow some catch-up of Public Service chief executive remuneration with other parts of the State sector.
- Decreases in appropriation and expenditure occurred in 2009/10 and 2010/11, reflecting an environment of fiscal restraint and modest remuneration expectations.
- The increase in expenditure for 2011/12 reflected payments to chief executives with untaken leave at the end of their terms, and relocation costs for newly appointed chief executives.
- The decrease in expenditure for the 2012/13 year reflected an environment of continued fiscal restraint, a reduction in the number of Public Service departments and reduced relocation costs for newly appointed chief executives.
- The decrease in expenditure in 2013/14 reflected that two chief executive positions were vacant for a significant portion of the year.
- The increase in expenditure in 2014/15 reflected the appointment into the long-vacant Ministry of Health position, and the payment of a higher number of end-of-term leave and performance pay entitlements for the outgoing Chief Executives of the Canterbury Earthquake Recovery Authority, Ministry for Culture and Heritage, Ministry for the Environment and the Ministry of Foreign Affairs and Trade.

How NZ Public Service chief executive pay rates compare

This is an area of significant interest to the public who want to be assured they are getting value for money from their public services, including remuneration paid to chief executives.

We all want high performing government departments delivering high quality public services. To do that we need our departments to be led by highly competent, highly qualified people.

Government departments are generally large, complex organisations with significant responsibilities and often large numbers of staff.

The remuneration paid to Public Service chief executives is lower than would be paid in the private sector for a job of a similar size. While this is the reality and is unlikely to change, the Commissioner has to make sure chief executives' remuneration does not get too far out of step with private sector chief executive remuneration.

If that happens we run the risk of the talented and qualified people New Zealand needs to run the Public Service taking up other employment, either here or overseas. This could lead to deterioration in the standard of public services available to New Zealanders.

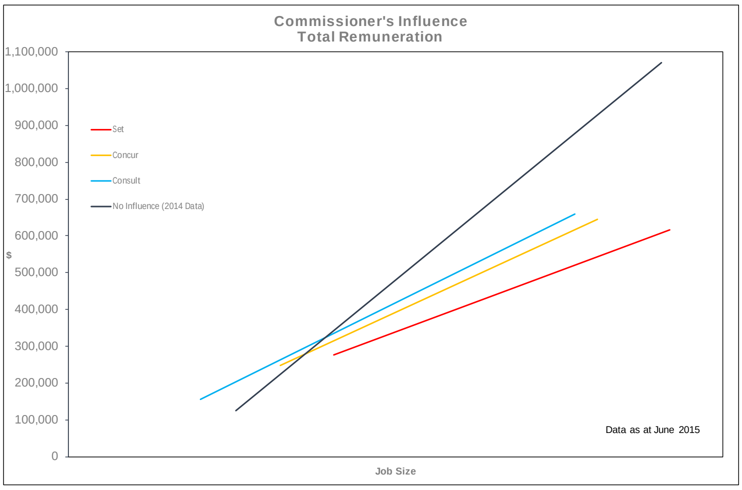
Ensuring we can attract and retain the people we need has to be carefully balanced against also making sure there is good value for the taxpayer.

How Public Service chief executive pay rates compare across the State sector

Public Service chief executives are paid less than chief executives in the wider State sector based on comparable job size

A comparison of Public Service chief executives remuneration with remuneration for chief executives in State-Owned Enterprises (SOEs), local government, Crown companies and council controlled organisations shows that the remuneration received by Public Service chief executives is less than the remuneration received by chief executives within the wider public sector based on comparable job size, and sometimes significantly so.

The graph below plots remuneration by job size for public sector chief executives (including SOEs, local government and the larger council controlled organisations (CCOs) and locally owned trusts) split into four groups. The graph clearly shows the inverse relationship between remuneration and the Commissioner's influence, with the lowest remuneration by job size paid to Public Service CEs for whom the Commissioner's influence is greatest.



Red line:	Public Service CEs - the Commissioner *sets* remuneration for this group
Yellow line:	CEs of Tertiary Education Institutions and district health boards - the Commissioner *consents* or *concurs* to remuneration for this group
Light blue line:	CEs of other Crown entities - the Commissioner is *consulted on* remuneration for this group
Dark blue line:	CEs of other public sector organisations (largely local government bodies and some SOEs) – the Commissioner has *no influence* on remuneration for these CEs

The measure used is "total cost", defined as the sum of total fixed remuneration and any performance payment received in the last year.

Notes on the graph:

a) The data for the red, yellow and light blue lines comes from the State Services Commission's records:

- note that the recent changes to setting remuneration for Public Service chief executives are not expected to have any impact in terms of this comparison.
- for the yellow and light blue lines, a standard percentage of the performance component in chief executives' remuneration packages was used.

b) Summary data for the dark blue line was purchased from remuneration consultants Strategic Pay Limited.

How Public Service chief executive and senior management pay rates compare

A comparison of New Zealand Public Service chief executive and second tier senior management remuneration shows a strong correlation between the size of the job and the individual's overall level of responsibility.

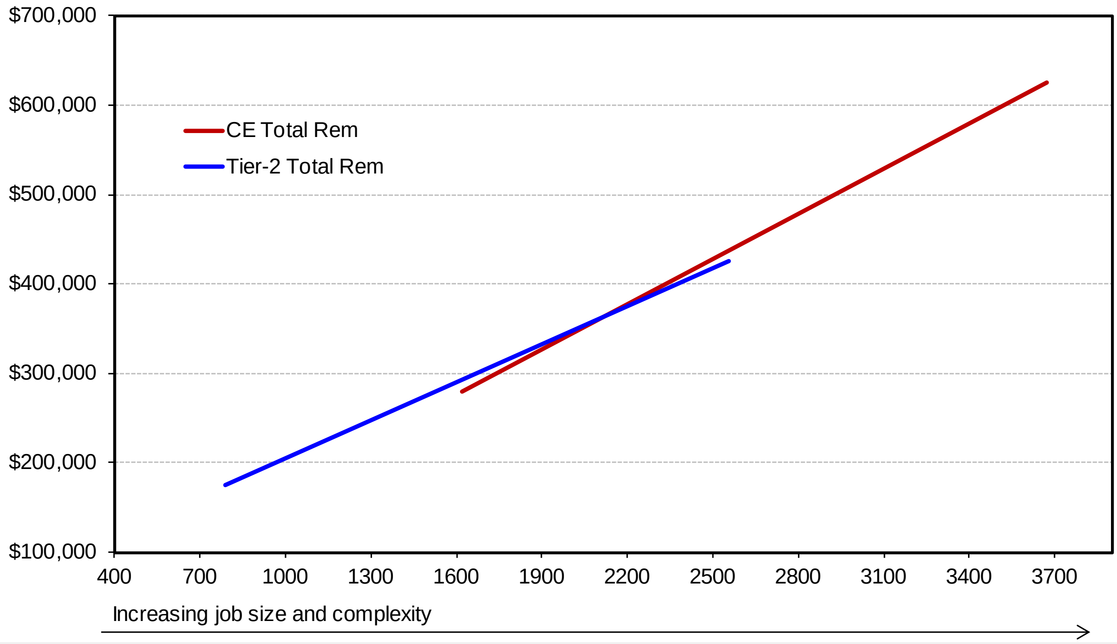
The State Services Commissioner sets the remuneration of most Public Service chief executives; the chief executives in turn set the remuneration of their managers.

As job size increases, chief executive remuneration increases at a greater rate than remuneration for second tier managers. This is because chief executives generally receive more at-risk performance pay, reflecting the greater complexity of chief executive roles.

Where the second tier managers receive higher remuneration than chief executive which similar sized roles, the second tier managers are likely to be in large agencies, compared to chief executives in small agencies.

It is important that remuneration for the two groups is broadly similar where job size/complexity overlaps between the two groups. This is so that people in large second tier roles can progress to smaller chief executive roles (and vice versa) as part of senior leadership career development.

2015 Public Service CE & Tier-2 Remuneration by Job Size



Notes on the graph:

- the chart shows the relationship between the remuneration lines for Public Service chief executives and managers at the second tier for total remuneration (i.e. base salary, fringe benefits plus any performance pay).
- the remuneration lines are based on data for Public Service chief executives and 167 second tier managers collected by SSC in March 2015.
- the remuneration lines represent median pay at particular job sizes, not specific remuneration for any particular role.

Pay ratios as a means of comparison

A measure which is gaining currency internationally is the ratio between a chief executive's remuneration and the average pay of the rest of the employees working in the organisation.

In August 2015, the United States Securities and Exchange Commission (SEC), the regulator charged with overseeing America's public companies, adopted a new rule on executive pay. Under the Dodd's-Frank Act passed in 2010, public companies must now publish a ratio which compares the pay of their chief executive to the median pay of employees. Commencing in 2017, it is estimated that around 3,800 companies will have to start disclosing their CEO pay ratio.

The move follows increasing concern over expanding executive compensation packages in the United States and the widening gap between CEO remuneration and the average pay of workers. The CEO-to-worker compensation ratio has grown from 20-to-1 in 1965, peaked at 376-to-1 in 2000 and was 303-to-1 in 2014 **(Economic Policy Institute, Issue Brief #399, June 2015)**.

To give some context, in the 2013 Fairfax annual survey of pay rates at listed companies in New Zealand, the average ratio was 26-to-1, up from a ratio of 22.5-to-1 since 2011 (the survey covered 39 companies on the NZX50, of which 23 had consistent data available for the previous three years.)

Pay ratios are affected by the pay rates that apply in different industries, as well as the chief executive's remuneration. Companies with a high average staff wage (such as Telecom, Air New Zealand, NZ Refining and Xero) had some of the lowest chief executive pay ratios in the 2013 survey with NZ Refining on 7-to-1, and Xero on 2.6-to-1. Similarly, pay rates in the IT, oil and gas industries were amongst the highest in New Zealand in 2013 with correspondingly low ratios, while retail and aged care were amongst the lowest paid with correspondingly high ratios (reported in the Sunday Star Times, October 2013).

In the United Kingdom, the Government Financial Reporting Manual (FReM) requires the disclosure by public sector entities of pay multiples (ratios) of top pay to median pay for employees. For the 2014/15 year, pay ratios for ministerial departments were similar to the New Zealand Public Service, ranging from 2.7-to-1 to 10.8-to-1. The median ratio of the 20 ministerial department ratios published in 2014/15 was 5.33-to-1.

NZ Public Service chief executive pay ratios

In 2015, the average pay of a chief executive in the New Zealand Public Service was 5.7 times the average pay of employees (including managers). The ratio refers to a comparison of average chief executive salary to the average Public Service employee salary, and has remained relatively stable over the past four years with some annual variation (source: Human Resource Capability Survey, State Services Commission).

Pay ratios vary amongst agencies, with the highest in 2015 being 7.7-to-1 and the lowest 2.2-to-1. The range of ratios reflects differences in the size and complexity of agencies (and therefore, differences in chief executive job size and pay), and the different mix of occupations in their workforce that influence average staff pay rates.