Ontario Government Introduces Changes to Executive Compensation in School Boards

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In 2014, the Government of Ontario began the process of developing public sector compensation frameworks to ensure a consistent approach to executive compensation. The *Broader Public Sector Executive Compensation Act, 2014* (the "Act") introduced by the Ontario government, applies to all Ontario public sector designated employers, including universities, colleges, hospitals and school boards.

In compliance with the Act and Regulation 304/16 "Executive Compensation Framework" (the "Regulation"), the four trustee associations collaboratively developed a comprehensive proposed executive compensation program to support executive compensation management across the province. This work was completed in consultation with Mercer (Canada) Limited ("Mercer"), an independent consulting firm that specializes in executive compensation.

The introduction of this legislation has led to a number of complex issues. One significant question pertains to the respective roles and responsibilities between the relevant board executives and the board of trustees. Among other things, what is the role of the trustees in approving annual executive compensation for supervisory officers? What are the steps required under the legislation? When will the increases for executives come into effect?

Under earlier legislation, the salaries and other compensation for directors of education, supervisory officers and other designated executives have been frozen since 2010. This legislation, requiring public restraint, has significantly affected the past earnings and future pensions for these important senior administrators.

The proposed executive compensation program developed by the parties is intended to establish a rational compensation approach for executive positions across all Ontario school boards. It recognizes that in the education sector, a fair and responsible

executive compensation program is vital for attracting and retaining the innovative leadership required to ensure continued progress in student achievement.

It is also recognizes that there is a need to reduce the compensation compression that exists between executives and principals, as salaries negotiated through collective agreements continued to increase during the compensation freeze, making it difficult to attract individuals to take on executive-level positions.

Mercer reports that during the public sector executive compensation freeze, Canadian salaries typically increased by 2% to 3% annually. Research also indicates that over the past five years, there has been over a 5% change in the consumer price index.

Accordingly, the proposed executive compensation program recognizes that there is a need for internal equity and a common framework across the 72 Ontario school boards.

In applying standards of accountability and complexity, Mercer and other the parties, which included the four trustee associations and the Council of Ontario Directors of Education ("CODE"), developed seven school board levels, with salary ranges for directors, associated directors, and executives (which include supervisory officers) for each level.

The parties recognized the need for individual school boards to have the flexibility and accountability to determine the placement of their specific executives within the base salary range.

The required steps and timelines for this process are set out in the Act, the Regulation, and related directives, letters, and memoranda from the government.1

The Ontario Ministry of Education (the "Ministry") required that all school boards develop a proposed compensation program to be submitted to the Ministry for review and approval by September 29, 2017.

Salary and Performance-Related Pay Envelope

Amendments to the Regulation made on June 9, 2017 introduced a "salary and performance-related pay envelope". This pay envelope is an overall cap to the amount of salary (and performance-related pay) that the board may provide to all of its designated executives for a given pay year, which is a period of one year in which the Board determines the salary and performance-related pay to be paid to its designated executives.

The board may select a maximum rate of increase to that envelope, which must be approved by the Ministry, and must consider only the following factors:

- The financial priorities and the compensation priorities of the Ontario government, as indicated in a number of public sources;
- Recent executive compensation trends in the Canadian public sector and BPS industries in which the board competes for executives;
- A comparison between the proportions of the board's and the comparator organizations' respective operating budgets used for executive pay;

- The effect on attracting and retaining executive talent of the difference between the designated executives' salary and performance-related pay range and that of the positions reporting to them; and
- Any significant expansion in the operations of the board that is not the result of a significant organizational restructuring.

The maximum rate of increase may only be re-determined if a salary and performance pay cap for a designated executive is recalculated, or if the board provides a designated executive with any (permissible) additional element of compensation.

Increases to the salary and performance-related pay envelope are therefore based on the formula P + (P x R), where P is the total salary and performance-related pay that the board provided to all of its designated executives for the previous pay year (annualized for any vacated positions), and is a rate of increase that does not exceed the approved maximum rate of increase to the pay envelope.

The draft compensation program must include two items related to the salary and performance-related pay envelope: (1) the value of P for the previous pay year, and (2) a proposed maximum rate of increase for the salary and performance-related pay envelope.

The increase is not required to be distributed evenly among executives. Actual annual increases paid to each executive may be more or less than the proposed maximum rate of increase, as long as the board maintains the approved increase within the relevant pay envelope and each executive does not exceed his or her maximum salary range.

Salary and Performance-Related Pay Cap

The Regulation also includes a cap on individual designated executives' salary and performance-related pay, which is a second constraint in addition to the salary and performance-related pay envelope, described above. Any increases to compensation are still subject to the executive's individual pay cap. The pay cap is determined based on an analysis of compensation in appropriate comparator organizations, whereby the position's maximum salary and performance-related pay may not exceed the 50th percentile of the comparator organizations. Mercer conducted this analysis to create the seven school board levels and corresponding salary ranges.

The board of trustees is accountable for determining the appropriate placement of its designated executives within the base salary range. The following criteria will be considered when determining their placement in the base salary range:

- The scope of the executive work, including the accountabilities and complexities of the position;
- External public sector comparators and internal school board comparators; and
- The tenure, experience and other individual characteristics of incumbents.

Process to Finalize the Executive Compensation Program

The board of trustees is given considerable authority under the legislation to implement and enforce the executive compensation process. It is clear the Ministry may request further information after it reviews the draft compensation program.

The process that school boards are required to follow includes:

1. Following submission of the proposed executive compensation program and the additional data, the board of trustees must provide any further information requested by the Ministry based on its review of the draft compensation program. The Ministry has indicated that the submissions will be carefully assessed for completeness and compliance.
2. The Ministry will also provide feedback to the board, which will primarily focus on the board's proposed maximum rate of increase for its pay envelope. The board must address the government feedback, and obtain confirmation from the Ministry to proceed with public consultation. The Ministry may also direct the board to resubmit a proposed compensation program after addressing comments.
3. The board will notify the Ministry at least two days prior to posting the proposed program for public consultation.
4. The board must post the draft executive compensation program on its public-facing website for at least 30 days, allowing reasonable opportunity for the public to comment. The board should establish a process for collecting, tracking, and retaining comments.
5. The board will address relevant public feedback in its proposed executive compensation program, submit an updated draft of the executive compensation program to the Ministry, and provide a summary of the public feedback received. The summary should include the following:
    1. The total number of comments received;
    2. The number of comments that were generally supportive of the proposed executive compensation program and the number of comments that were not;
    3. The name of any organizations that commented;
    4. A summary of any common themes; and,
    5. If necessary, what the designated employer did to address the feedback.
6. The board must obtain the Ministry's approval of the executive compensation program, including the proposed maximum rate of increase to the compensation envelope.
7. The board of trustees will determine whether to adopt the final draft of the executive compensation program.
8. Once approved, the board must post the finalized executive compensation program on its public-facing website.
9. Once posted, the executive compensation program becomes effective.

Comment

Across the province, the Ministry will be providing directives to individual boards regarding the status of their proposed executive compensation programs.

Following the September 29, 2017 deadline for the submission of local board executive compensation programs, there has been ongoing dialogue among government, the four trustee associations and CODE, with all parties continuing to support the approved framework.

As a result of the discussions over the past few weeks, the government has signaled a willingness to commit to the following:

- Local executive compensation program that are approved, finalized and posted by February 28, 2018, will be retroactive to September 1, 2017.
- Boards will receive a written response to their proposed local executive compensation programs by November 3, 2017. Where a proposal is not approved, specific feedback should be provided.
- The government is committed to increasing the funding to the GSN benchmarks by up to 5% for this school year and intend to do so for the following two years as well.

School boards need highly skilled, thoughtful and engaged leaders to lead their organizations in providing, promoting, and enhancing publicly funded education. Many school boards in the province have recently faced challenges of recruitment in key executive areas of the organization. In this regard, a competitive and fair executive compensation program is vital for attracting and retaining talented leadership required to ensure student success in our schools.

1 These additional sources are as follows:

- the Executive Compensation Framework Compliance Report Directive, published on January 23, 2017;
- the Broader Public Sector Executive Compensation Program Directive, issued on June 9, 2017;
- the Broader Public Sector Executive Compensation Guide, updated on June 9, 2017;
- letter from the President of the Treasury Board, Minister Liz Sandals, dated June 9, 2017;
- letter from the Deputy Minister of Education, Bruce Rodrigues, dated June 15, 2017;
- letters from Minister of Education, Mitzie Hunter, to Presidents of School Board Trustee Associations, dated July 24, 2017, August 31, 2017, and September 20, 2017; and
- memorandum from Assistant Deputy Minister of Education, Joshua Paul, to Directors of Education and Senior Business Officials, dated September 20, 2017.

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