

MEDIA RELEASE

Regnan Governance Research and Engagement

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Productivity Commission report on Executive remuneration welcomed but heavy lifting only now starting

Regnan welcomes the final report of the Productivity Commission Inquiry into executive remuneration and commends the thorough consideration of a wide range of issues. Regnan notes however that the report marks the beginning and not the end of shareowner attention to executive remuneration.

“In delivering this report Messer’s Banks, Fels and Fitzgerald and the Commission staff have loaded up the bar, but it is now up to policy makers and investors to perform their roles in heavy lifting” said Regnan Managing Director, Erik Mather.

Regnan notes with some disappointment that initial reactions to the report have focused upon narrow and often remote issues, while substantive matters of delivering better alignment of rewards to executives and shareowners have been given the appearance of being second order.

Noted within the report are key facts that signal an ongoing problem of remuneration short-termism in Australia:

- The continuing majority of executive payments are base salary and Short Term Incentives (down from 89% in 2003/4 but still 75% in 2008/9)¹. This means that the majority of executive remuneration is paid within 12-24months², and
- The reality that “Long Term Incentives”, in practice, are only a three-year experience³

These issues of short termism need to be reviewed against the long term superannuation investment experience of working Australians who with a median age of 37 years can expect to be investing in listed companies for at least the next 23 years, if not longer.

Recommendation 13, proposing tax barriers to post-departure vesting be removed, is therefore a key reform proposal that risks being under-emphasised.

It is worth noting that during the period of the Commission’s deliberations, the maximum period that company directors can align executive rewards with their shareowners has been reduced from 10 years down to seven. This means that directors have had their available tools reduced at a time when investment markets, globally, have been calling for a more long term perspective to executive remuneration.

The heavy lifting to address these ongoing issues lies both with policy reform and the investment community represented by its company directors.

¹ Table 1

² See Box 4 where STI is “typically one year”

³ See Box 4



It is therefore suboptimal to have disproportionate distraction created out of the Commissions 'No Vacancy' rule and 'Two Strikes' reforms announced in the final draft.

“Effective company boards have nothing to fear from either of the Commission’s proposed reforms. Some of the reactions and fears bear remarkable similarity to the initial reaction to the non-binding vote on the remuneration report – which today is widely acknowledged as having promoted director-shareowner engagement.” Mr Mather continued.

In the case of the proposed 'No Vacancy' reform directors have the choice of allowing board vacancies to be tested by all of the shareowners under normal voting processes before they are required to specifically seek shareowner permission to employ their No Vacancy power under a company constitution.

In the case of the proposed 'Two Strikes Rule', in practice directors would need to receive two 25% votes against their remuneration report in successive years, followed by a more than 50% vote on a proposal to hold an extraordinary general meeting followed then by a 50% vote against their directorship at that EGM. Any director who was unable to reasonably engage their shareowner-base during this period might reasonably be expected to consider their suitability for their role. Furthermore, as the Commission itself notes, there are much simpler mechanisms available to shareowners being the 5% rule (to propose a resolution to a company meeting) and the 1/3 rotation rule, that sees one third of the Board rotated for election each year. The Commission notes that there is little or no evidence that these alternative provisions have created difficulty for Boards and their directors.

“The time for debating has passed and its now time for these recommendations to be made available so that the investing community can work with its directors to ensure best-practice alignment between executive and shareowner rewards alike” said Mr Mather.

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About Regnan

Regnan was formed in 2007 out of the proven engagement model and resources of BT Financial Group’s Governance Advisory Service. Regnan is owned by eight major institutional investors: ARIA; BT Investment Management; Hermes UK; HESTA Super; NSW Local Government Superannuation Scheme; Vanguard; VicSuper; and VFMC. Regnan provides company engagement services to institutional investors and quantitative data on company Environmental Social and Corporate Governance performance for mainstream funds management.