

To whom it may concern,

I am writing to you in relation to an idea I have to help ensure long term business viability and reasonable executive remuneration packages. Obviously with the financial meltdown, there has been significant downturn in the economy, affecting companies and their viability, which has in turn led to further economic instability.

During this time, there has been some discussion over the appropriateness of executive salaries and whether there has been a shift away from directors ensuring the long term viability of the company for shorter term gains. Firstly, I don't propose to be an expert in this area, but make general comments and suggestions that you may choose to expand on, if you find this idea useful.

Observation:

Company executives are paid (ridiculous) remuneration packages for short term results, which may not necessarily lead to the long term viability of the company. In fact, in some cases it could be argued that the remuneration packages (including severance and gold handshake pays) motivate the directors to take aggressive growth and leverage options to improve short to medium term outcomes, with little planning for long term risks. For example, high leveraging against the equity of the company (or similar measures which aim to "crystallise" the share value of the company). This measure is fine until the share price falls, such as in the case of the ABC Learning Centre. There are numerous examples of companies aggressively pursuing growth in good economic times, only to have the carpet pulled from underneath them once conditions turn even slightly sour.

Implication:

Short to medium term focus by directors does not guarantee the long term viability of the company. Obviously, when large companies fail it is the short term displacement that is the economic issue (money withdrawn from the economy, unemployment, economic confidence). It is the long term viability of the company that will ensure Australia's economy will continue to grow sustainably.

I believe business's ability to handle large one-off events such as a prolonged recessions, natural disasters and serious legal action (except at the very biggest end of town) is limited. An example of a legal action case might be CSR or a mining company disaster. The implications of large businesses failing is obvious.

Recommendation:

I believe there should be incentive to reduce executive remuneration packages and ensure the long term growth and viability of companies.

I propose this could be done by establishing, by law, a Sinking Fund type arrangement for companies (similar to the Community Titles Legislation in QLD).

The Sinking Fund contribution would be based on the remuneration packages (including severance pay) of the company executives. I suggest a percentage (whatever that might be) say 5% of the total remuneration package of directors should be contributed to a Sinking Fund. This Sinking Fund amount must be invested in a high interest account and only available to the company on meeting certain criteria - For example, natural disaster declared in area, unforeseen legal action from product more than 10yrs ago (i.e. CSR & Asbestos), an official recession is declared or by application to the Australian Taxation Office (or like Government Department).

The company could access the funds to ensure the company survives the threat, or at least has the funds to meet more of its legal obligations (i.e. compensation, employee benefits).

The primary goal of this legislation would be to ensure a company is planning for one off events and is viable in the long term. The secondary goal is to ensure the remuneration packages are reasonable. By linking the Sinking Fund contribution percentage to the executive salaries, the directors must now weigh up how much of the current working capital of the business they want to put aside in the sinking fund vs how much they want to be paid. At the very least, if it didn't decrease salary packages (or limit increases), it would be assisting to ensure the long term viability of the company which I believe would improve Shareholder confidence.

Logistics:

The Government has the ability to implement this by utilising the existing Corporations Law. I propose it only apply to listed companies (ASX). This would cover the majority of big businesses and the largest employers and contributors to GDP. It would be easy to analyse and predict the possible affects on business, as Annual Reports for listed companies are freely available to the public and Government. Accordingly, the Government could easily estimate the impact on business and the funds it would raise via such a measure.

I believe this proposal would be widely rejected by business executives who would argue they already have 10 year plans and that it limits the companies ability to grow by tying up working capital. Firstly, very few directors sit on the board for that long and it is the once in a 25 year event that the Sinking Fund should be aimed at resolving. Not the one in 10 year event. Secondly, it would be like any other tax or restriction imposed by Government, it is a short term one off negative, that is quickly absorbed by the market. Not that I propose over regulation, in fact, I am against it. However, I believe like superannuation, it has long term benefits to the Australian economy.

The legislation should be phased in similar to the Superannuation Guarantee legislation, with a starting percentage, a goal percentage and a phase in period. Companies should have the ability to contribute existing emergency funds to the accounts, thereby reducing their requirements to contribute in the 1st year.

On wind up of a company, the funds would be available for a special dividend to shareholders.

There is obviously more work to be done on the above, but is an idea I thought was worth sharing.

Other:

In addition to the above, I believe there is merit in the suggestion that all golden handshakes or severance pays larger than 1 years remuneration must be approved by a majority of the shareholders.

Should you have any queries, please do not hesitate to contact me on the email address provided.

Regards,

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