

The Secretary
Inquiry into Regulation of
Director and Executive Remuneration
Productivity Commission
Locked Bag 2
Collins Street East
MELBOURNE VIC 8003

Dear Sir,

This submission approaches the problem of board and executive remuneration from two perspectives:

FIRST PERSPECTIVE---THE BROAD VIEW

This perspective argues that excessive director and CEO remuneration is not the central problem—it is one of many symptoms of a larger and deeper problem. We should be curing the sickness not treating the symptoms. The “sickness” is that shareholders, the owners of the listed public companies, no longer have any control or influence over the companies that they “own”. If shareholders had control then excessive remuneration would instantly disappear; as would most of the other symptoms which are currently dragging down our public companies.

Time and time again the interests of shareholders, employees and clients are trampled underfoot in the greed-crazed stampede by directors and senior executives to transfer company wealth into their own bank accounts.

Time and time again we see decisions that are completely contrary to the interests of shareholders and to the welfare of the business. By way of examples:

- The employment of CEOs with histories of failure.
- The remuneration of CEOs at levels which are beyond belief.
- The takeover of quite inappropriate targets at inappropriate prices.
- Inappropriate levels of debt.
- Backdoor raising of capital at heavily discounted prices.
- The retrenchment of highly skilled workforces.
- Restructurings which achieve nothing but turmoil and increased executive salaries.

All of these poor decisions, though they may adversely affect shareholders, are never discussed with shareholders. That is quite acceptable provided the old standards of accountability are followed. In the old days if poor decisions were made, those responsible would immediately fall on their swords, or be sacked or, at best, be demoted. Not today. Failures and poor decisions draw even bigger bonuses or untenable termination payments. **SHAREHOLDERS HAVE NO SAY IN THESE MATTERS. THEY ARE IGNORED. THEY ARE INCAPABLE OF PUNISHING THE FAILURES, THE INCOMPETENTS AND THE GREEDY.** How long ago did we last witness a shareholder revolt in which the small shareholders ousted the whole board? Today the instructional shareholders would rally behind their “mates” who are under scrutiny and would use their voting power [for once] to retain the status quo.

Again and again shareholders vote down remuneration reports. Again and again their legitimate complaints about mismanagement raised at AGMs are ignored. Boards arrogantly dismiss shareholder demands about remuneration and about basic management issues.

How can power be restored to ordinary shareholders? That is for others more expert than me to advise. However I do make a few recommendations:

- The Government to regulate a list of matters upon which institutional shareholders must vote. Furthermore those institutions would be required to report to their stakeholders as to how they cast their vote on each matter. "Stakeholders" is the preferred term as mostly the institutions would be using the voting power of their policy holders and depositors rather than their shareholders funds.
- Every board is to include specially qualified directors. One director would have to be a small shareholder and would be elected [never appointed] by those shareholders holding less than 1% of the issued capital. One director would be an employee representative elected [never appointed] by the non-executive ranks of the company's employees. One director would represent the company's clients and would be elected by the small shareholders after the vacancy was advertised. Should the number of directors [including the specially qualified directors] exceed nine, then further qualified directors are to be added so that they never total less than one third of the board.
- That the Government's preference for "independent" directors be reconsidered. The policy, in my view, has not delivered the goods. Those directors that have founded the company or have a large investment in it will have a more pressing desire to have the company survive and grow and to keep the conditions for senior staff proportional to their contributions to profit.
- All resolutions made at an AGM or EGM to be binding. What actually is the point in having all of the owners vote on a question and then ignore their decision?

SECOND PERSPECTIVE—THE NARROW VIEW

This perspective acknowledges that the culture shock arising from the first perspective and the political will to make such sweeping changes may be a little too ambitious in the short term. Perspective two therefore focuses only on the single issue of board and executive remuneration. I would understand that it is a "given" that such rewards are grotesquely out of control and that we must discontinue the recent obnoxious custom of rewarding failure.

I am personally very envious of CEOs, senior executives and board members who are able to negotiate very favorable conditions, tenure not related to performance and huge bonuses for simply doing their jobs. In my working life as a senior army officer and as a local government chief engineer, my salary and conditions were always prescribed [not negotiable] and I never once received a bonus as none was available. Did I work any less hard or any less skillfully? My rewards for a job well done were continued employment, a good and marketable reputation should I choose to look elsewhere, annual increments subject to satisfactory performance and promotions ahead of seniority. It is my experience and observation that a professional person does not need a bonus to do his best. All that bonuses achieve is creative accounting so as to trigger and to maximize the bonus payment criteria.

There used to be a myth that we had to pay top dollar to attract top people when competing against overseas firms. There was another myth about paying peanuts to attract monkeys. I hope that both myths have been so discredited that I and my children and my children's children will never again have to listen to such rubbish.

The major plank of my recommendations is that there should be a scale of CEO and director appointments. There could be ten or twenty ranks within each scale. The maximum and minimum remuneration for each rank within the two scales would be determined by some independent tribunal or could be an award under Commonwealth industrial law. The maxima and minima for each rank would be based on appropriate factors which quantify the responsibilities and managerial complexities of the positions. The guidelines or award would allow incremental annual advancement subject to

performance reviews; and as the company grows [or shrinks] the rank for the directors and CEO would change. Another means of enforcing the scales would be by shaming those who don't comply. However, recent evidence suggests that greed is beating shame every time. The fear of punishment may be the only option.

There is a perception of pecuniary interest when a board sets the remuneration of a CEO. "If we pay our CEO a very large salary," they think to themselves, "then we directors, who are his bosses, will need to pay ourselves commensurately." Basically board and CEO are joined together in an unwritten pact to help themselves to shareholder funds. Likewise, if a CEO pays his senior executives very high salaries then logically, in order to maintain relativities with his subordinates, he must ask the board for appropriate remuneration.

The regime that I am recommending is:

- That two scales [one for board members, one for CEOs] be introduced by legislation, industrial award or by voluntary guidelines. Each scale to prescribe a number of rankings which are based upon the levels of responsibility and managerial complexity attached to each rank. Each rank to have maximum and minimum remuneration prescribed.
- That directors and CEOs may advance by annual increments up to the prescribed maximum for that ranking.
- They may also advance to the next ranking, or drop to a lower ranking, as the business grows or contracts.
- A CEO may not be appointed at conditions more generous than those of his predecessor.
- There are to be no bonuses other than a bonus, approved by shareholders at the AGM, which is paid to every employee in proportion to their base wages.
- All decisions made at an AGM or EGM are binding.

In conclusion may I say that I have been a small shareholder continuously for 51 years, covering most listed Australian companies. I have never been so disgusted with the performance and naked greed of directors and senior executives as in the past five years. In my retirement I am chairman of a Queensland unlisted public company which, I have to modestly admit, runs very smoothly and profitably to the complete satisfaction of all shareholders, staff and customers. Needless to say, the directors receive no fees and the manager is paid a modest salary. Perhaps we could offer a consultancy service to some of the big companies.....for a huge fee, of course.

In the British Army prior to and during WW1, the officers were all upper class, wealthy snobs with little education and no practical experience. Millions of British soldiers died as a result, before the system was changed. It seems to me that we have allowed a similar class to establish itself and to perpetuate itself as the only people to manage businesses. Leadership has given way to the age of the "bean counter". It is past time to take a look at how people become company directors and CEOs, their career paths, qualifications and experience.

I wish the commissioners well in this enquiry. You are taking on some powerful vested interests whose self-centered cunning knows no bounds. Be strong !

Yours faithfully,

Kenneth E Park