



AUSTRALIAN INDUSTRY
GROUP

Ai Group Submission
on the Productivity Commission's
Discussion Draft Report

Executive Remuneration in Australia

November 2009

About Ai Group

The Australian Industry Group (Ai Group) is a leading industry association in Australia. Ai Group member businesses employ around 750,000 staff in an expanding range of industry sectors including: manufacturing; engineering; construction; automotive; food; transport; information technology; telecommunications; call centres; labour hire; printing; defence; mining equipment and supplies; airlines; and other related service industries.

Submission

Ai Group welcomes the opportunity to comment on the Productivity Commission's Discussion Draft Report on Executive Remuneration in Australia.

Ai Group supports the threshold conclusion in the Discussion Draft that prescriptive pay constraints on executive remuneration such as caps are not warranted.

Ai Group also agrees that the appropriate direction of reform should focus on strengthening corporate governance to improve remuneration setting practices and better engage with shareholders.

Ai Group generally supports the Draft Recommendations and the Draft Finding set out in the Draft Report. We have specific comments in two areas.

Two Strikes Proposal

We do not support the proposed "two strikes" policy and certainly not as it is presently formulated.

We take the view that if the broad thrust of the Draft Recommendations is acted upon, there would be little need to put in place the two strikes proposal.

The proposal has two elements

- The first element proposes that where 25% or more votes are cast against a remuneration report, the board's next remuneration report should explain how shareholders' concerns were addressed, or why they were not addressed.
- The second element relates to the subsequent remuneration report in which such shareholder concerns were addressed. If this remuneration report received a 'no' vote above a prescribed threshold, all elected board members would be required to submit for re-election either at the next AGM or at an EGM.

It seems inappropriate that the threat of a full spill of positions could hang over a Board whose remuneration report received support from as many as 75% of shareholders.

This threat is made all the more difficult because of the considerable uncertainty that would surround the identification of “shareholder concerns”. It is quite possible that a range of, perhaps contradictory, concerns could have been expressed and there could well be a legitimate range of interpretations placed on the expression of those concerns. A board may well find the task of addressing shareholder concerns was very difficult to define.

In avoiding the second element of the proposal, there is a strong likelihood that, following a dissenting vote on its remuneration report, a board and the management team would devote considerable time and effort to possibly ill-defined remuneration issues both perceived and real and to demonstrating efforts in this area. Particularly because the task would be difficult to define, there is a strong likelihood that such time and effort would be disproportionate to the objective importance of the issues and this would inevitably “crowd out” other areas of management and governance from receiving the consideration they deserve.

While a patch-up solution to these difficulties would be for the prescribed minimum threshold for the second element of the proposal to be set at 50%, this is not likely to address the fundamental problems because boards would be likely to strive to avoid a dissenting vote of at least 25% at the second stage both for reputational reasons and to avoid going through another year under the threat of the full spill of positions.

Ai Group favours a softer touch approach to regulation in this area. Indeed, as indicated above, we suggest that by putting in place the bulk of the other recommendations proposed, there would be little need to adopt the two strikes proposal.

Should this argument not be accepted, we suggest that a 50% threshold should apply at both stages of the two strike proposal.

Recommendations 2 and 3

Ai Group supports Draft Recommendation 3 proposing that the ASX Corporate Governance Council's current suggestion on the composition of remuneration committees should be elevated to a 'comply or explain' recommendation, specifying that remuneration committees:

- have at least three members;
- be comprised of a majority of independent directors, and
- be chaired by an independent director.

If Draft Recommendation 3 is adopted, we do not think that Draft Recommendation 2 which would mandate that executives of ASX 300 companies could not sit on Remuneration Committees should be adopted.

Ai Group is of the view that Draft Recommendation 3 would address the substantial concerns and that the extra benefits (if any) of also adopting Draft Recommendation 2 are unlikely to be justified. These costs are acknowledged in the fact that the Draft Report fell short of proposing that Recommendation 2 should apply to all companies.