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**Regnan Submission to the Productivity Commission on the  
Regulation of Director and Executive Remuneration in Australia –  
30<sup>th</sup> November 2009**

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## 1. Introduction

- Regnan is a specialist governance adviser that since 2001<sup>1</sup> has undertaken research and engagement on ESG<sup>2</sup> issues, including executive remuneration, on behalf of institutional investors. Eight leading institutional investors own Regnan, and at the time of this submission thirteen institutional investors retained Regnan. Its mandate is to proactively identify potential governance risks and engage investee companies in relation to these risks.
- Regnan has already lodged a public submission in relation to the Commission's draft findings. Due to timing difficulties, the proposal described below regarding shareholder approval of a Board Report has not been received endorsement from our owners and clients. Accordingly, this submission reflects the views of Regnan and does not necessarily represent its client organisations.

### Board Capability Recommendations

Regnan believes a significant contributor to the reported excessive remuneration and the global financial crisis was a lack of board and shareholder oversight.

- Regnan notes that board capabilities are a key factor in determining the quality of the remuneration framework set by a company, and believes executive remuneration is an issue subordinate to that of the capability<sup>3</sup> of the Board.
- Regnan would like the Commission to consider introducing a non-binding vote on a report prepared by the board (for the purposes of this submission called the "Board Report") explaining the board's nomination processes, board renewal plans, appraisal processes, required skill set, board education, board induction processes and policies which allow directors access to expert advice.
- The desired outcome of such a proposal is increased shareholder oversight of board composition. We believe that a vote on would also lead to increased engagement and dialogue between listed entities and their key institutional shareholders regarding, inter alia, board membership, competency and succession planning. The significant increase in dialogue and engagement between companies and their institutional investors was a key positive outcome of the non-binding vote on remuneration reports.

<sup>1</sup> Then as the BT Governance Advisory Service.

<sup>2</sup> Environmental, social and corporate governance.

<sup>3</sup> The Productivity Commission identified board diversity as an issue which may contribute to the current community concerns regarding remuneration. Regnan views "competency" rather than "diversity" as the issue as shareholders need competent boards. A board which exhibits diversity may not necessarily be competent.

- Regnan believes that, as with the non-binding remuneration report, investors (particularly institutional investors) would be prepared to vote against such a report if they had concerns regarding the competency of the Board.
- Analysis of proxy voting statistics of widely held companies (ie where no director-related entity controls 20% or more of issued capital) shows that shareholders are more likely to vote against a remuneration report than any other proposal put to shareholders. Anecdotal evidence suggests that, it is the non-binding nature of the proposal that encourages the expression of their concerns.
- Aside from the remuneration report, a vote to (re)elect individual directors is the only mechanism contemplated as a means of expressing dissatisfaction with the Board. Many institutional investors see a vote against a particular director as inappropriate absent dissatisfaction with both the involvement of that particular individual on the Board, and conviction that removal of that director needs to take immediate effect.
- Furthermore, additional, suitably qualified independent directors can improve board competency. The existing mechanism of a vote for or against existing directors does not allow investors to express the preference of the appointment of additional suitably qualified directors.
- In smaller companies where the board size is at the legal minimum of three, a vote against a director is not an option for shareholders. However, a vote against their Board Report could send a strong message to the board.
- We believe that if such a proposal were to be included on the proxy form of all listed entities then a “one strike” rule would apply in a similar manner as the proposed “one strike” rule for remuneration reports. That is, the board would be required to report to shareholders in the subsequent “Board Report” how shareholder concerns were addressed, and, if they have not been addressed, the reasons why.

We thank the commission for all their work that on remuneration. We hope that the Commission will consider the above proposal.