# Stephen Mayne's submission to the Productivity Commission inquiry into executive pay

Jeff Kennett used to say: "if you can't say it in a page it's not worth saying."

Therefore, here follows the shortest submission from your tallest submitter, but apologies it has blown out to two pages.

As a professional shareholder advocate and the owner of the world's biggest small share portfolio – 640 stocks worth less than $70,000 – I've been sent a lot of remuneration reports. And having asked questions at more than 300 AGMs over the years, I've probably heard more AGM pay debates than any other Australian.

I'm a big fan of the non-binding vote that Costello introduced. The system is working well as companies better explain pay policies and shareholders in the likes of Telstra, Boral, Transurban and Wesfarmers have voted down remuneration reports. Even Macquarie Group changed its practices after a 21.5% protest in 2007.

However, there's still much for the Rudd Government to address. First up, the Government ought to be congratulated for already moving on two of the most important areas of reform: shareholder approval for termination payments and the tax treatment of equity issued to executives. The termination payouts reform proposal is spot on and the proposed changes on equity pay should be supported, despite the disappointing campaign whipped up by *The Australian Financial Review.*

There are 8 more important changes required for executive pay in Australia and they are as follows:

**# 1. Bringing down the roof globally**

Lobby the Obama administration to curb the outrageous system of executive pay in the US, which has caused blowouts and distortions all over the world. The most notable example in Australia was NAB's hiring of Ahmed Fahour from Citigroup in 2004. The 37-year-old was paid $13.3 million in compensation for the benefits he was leaving on the table at Citi, prompting former NAB CEO Nobby Clarke to observe at the 2005 AGM that Ahmed was paid more in his first 35 days than Nobby received in 35 years at the bank. See NAB's hiring announcement here: http://www.asx.com.au/asxpdf/20040811/pdf/3mfdyln88631m.pdf

**# 2. Compulsory, direct, disclosed and unconflicted voting**

Make it compulsory for the major retail and industry super funds to vote their shares in ASX300 companies. This voting should be disclosed as US mutual funds are required to do on their websites. Replace the anachronistic manual proxy voting system with a fully electronic and auditable direct voting system. Don't allow executives to vote their own shares on remuneration reports, as Paul Little does at Toll and Australia's highest paid executive, Frank Lowy, did at Westfield in 2009.

**# 3. Disclosure the full CEO contract**

Require full disclosure of a CEO contract, rather than just a summary of the key terms. This is similar to the debate we had about the Babcock and Macquarie management agreements with their listed funds last year after the ASX granted waivers to the listing rules allowing these funds to only disclose summaries of the agreements. Externally managed US funds are required to disclose the full management contract and Babcock and Macquarie relented and released the full management agreements last year. And so it should be with CEO contracts, down to everything such as the optional extras on the Mercedes and all fine dining bills. A bit of sunlight would end some of the greedy excesses, as the British political class have just discovered.

**# 4. Disclosure of cumulative CEO benefits**

Require the remuneration report to include a summary of all benefits paid to the CEO since they joined the company, regardless of how far back that goes. This should include a full history of the CEO's equity ownership record, including lapsed options or performance rights. Too often an incentive proposal is put up for approval and shareholders are not informed of earlier shares issues or share sales when they make this decision. Similarly, the valuations on various equity grants in old annual reports are often proved wildly inaccurate by market movements, so an overall summary of the complete CEO remuneration experience in each annual report which would be much more useful.

**# 5. Shareholder approval of all equity issues**

Restore the pre-existing requirement that all equity issues to senior managers requires specific shareholder approval. ASX listing rule 10.14 has created a loophole that many companies have jumped through. A classic case was Greg Gailey, now President of the Business Council of Australia, at Zinifex in 2007 when he received a new equity incentive grant despite already being more than $15 million ahead on earlier issues. This wasn't put to shareholders, which is why the remuneration report that year attracted a large protest vote of more than 40%. See results here: http://www.asx.com.au/asxpdf/20061127/pdf/3zsssyf37l9wb.pdf

**# 6. End the CEO election exemption**

Rather than giving CEOs an exemption from the three year director election cycle, put them up for election every year so shareholders can directly reflect on their performance and pay. Sol Trujillo's position on the Telstra board was never once put to shareholders for approval and Rupert Murdoch went decades without being elected, even though he was the executive chairman of News Corp getting paid more than $10 million a year. It is ridiculous that an unelected CEO could be paid $100 million in cash without shareholder approval. With annual board confirmation required, this would introduce direct CEO accountability to shareholders.

**# 7. Increase the relative pay of non-executive directors**

Australia's non-executive directors get a pretty raw deal when compared with their CEOs. The vast majority of boards are collectively paid far less than their CEO. Here are two notable examples:

**Westfield:** executive chairman Frank Lowy paid $16.2 million in 2008 when 11 non-executive directors shared in only $2.286 million.

**Macquarie Group:** out-going CEO Allan Moss paid $24.8 million in year to March 31, 2008, when the 10 non-executive directors only paid $2.65 million collectively.

NED pay has been restrained largely because the overall fee cap must be approved by shareholders. This should remain in place. One way of containing CEO pay might be to say the cash component cannot exceed three times the total fee cap for all the non-executive directors. This might lead to an increase in NED pay which wouldn't be a bad thing because at the moment we have too few people sitting on too many boards. A CEO who was earning $5 million a year, would have to join at least 4 boards to earn just $1 million a year as a professional director. A well-qualified director shouldn't have to work flat out to make $1 million a year.

**# 8. Better disclose fund manager pay and close the Alan Jones loophole**

Require fund managers to disclose their own pay packets by closing the loophole that only sees those technically classified as "executives" revealed in the annual reports of public companies. Require all major super funds to disclose their fully audited accounts and pay practices, as occurs with public companies.

The fund manager loophole is the same quirk in the system that sees shock jock Alan Jones paid a reported $5 million a year by Macquarie Radio whilst he doesn't appear in the five highest paid executives in the annual report. If the 2CH programming director Ian Holland earning $123,315 is worth listing, surely The Parrot's $5 million should rate a mention. See the remuneration tables on page 23 of the latest Macquarie Radio annual report here: http://imagesignal.comsec.com.au/asxdata/20081028/pdf/00895935.pdf

I would be delighted to appear before the inquiry to expand on these and other points.

Stephen Mayne