Submission to Productivity Commission on Discussion Draft report on Executive Remuneration

By Adrian Gattenhof

I generally support the draft recommendations, particularly those under “Shareholder engagement” intended to strengthen shareholder power to influence boards on pay. However, I think they fall well short of the measures that should be advanced to address the concerns outlined in the Terms of reference. Specifically, they fail to address with sufficient directness the “excessive remuneration practices” mentioned under “Background”. While the report mentions the many calls for capping mechanisms, it fails to take advantage of ToR 4 and consider how these may positively affect executive and corporate performance and support desirable social goals. And it fails to consider the gross inequity and social damage consequent upon the chronic, disproportionate pay and inadequate accountability of executives.

My focus is the size of executive pay relative to the general community’s and the moral and social impacts of greed and excess, particularly where the disconnection between pay and performance is blatant. My submission focuses on the moral and social equity aspects of executive pay, and presents my recommendations.

Greed and envy are corrupting poisons. They are as destructive in corporations as they are in individuals, families and society at large.

My Recommendation

I recommend that executive pay be capped at a multiple of ten times the lowest paid full-time employee in an organisation, or of AWE whichever is the lesser.

I support the ACTU’s proposals as detailed on Pp. 3 - 5 of their submission under the heading of “Regulatory failure” but with these modifications: the cap should be calculated on the lesser of the lowest full-time wage in an organisation or AWE. The purpose being to prevent distortions due to some very high-paying industries – e.g. mining - and with the aim of better aligning executive employment with skills, experience and interests rather than pay levels.

I think the Commission has failed to recognise the persuasive merit in the ACTU’s observation that: “Regulation requiring transparency has helped publicise excesses, but boards continue to award these benefits without shame and large institutional shareholders continue to vote in favour of them. They do this because of an institutional bias in favour of pursuing short-term returns but also because of self-interest (in that directors and fund managers wish to ensure a high “market wage” for the types of jobs they possess themselves).

That would have been written before the unconscionable Geoff Dixon payout became public. The Dixon case illustrates the ACTU point perfectly and illustrates why anything short of black-letter regulation will fail to rein in the excesses. SMH financial journalist Ian Verrender made the same point about boards and their tie-in with institutional shareholders in his article headed “Huff and puff all you want, old Blowhard is unsackable” in the SMH on 24 October 2009.

The Commission has failed to give sufficient weight to these insights and recommendation 15 will achieve nothing beyond more disillusionment for retail shareholders and the wider community.

Boards strenuously resist the admission of anyone who is not a clone or protégée of old Blowhard. Some four or five years ago an excellent, non boys'-club candidate stood for the ANZ board. A woman with around 20 years of branch experience and customer service, and horror of horrors, an FSU member. The boys'-club closed ranks and acidly opposed her, acidly opposed the chance of someone not of their caste, acidly opposed someone who might bring a fresh, invigorating perspective to the board. Even though she would have had just one vote!! They probably feared what she might discover and maybe blow the whistle. To these ossified Brahmans of Business everyone else is untouchable. Little wonder Australia's corporate culture is generally so unimaginative and resistant to progress.

My additional recommendation – One shareholder, one vote

If the Commission is serious about reform through recommendation 15, then I anticipate strong support for my recommendation which could be spliced onto it;

The company voting system should be reformed to align it with the political, where the franchise is based on citizenship not wealth. Accordingly, the corporate voting system should be changed from one share one vote, to one shareholder one vote. To qualify to vote a shareholder would have to hold a bona fide investment in the company for a minimum time, say, $5,000 held for more than one year.

Now that would bring about reform.

Supporting arguments and observations

1) Prosperity – a communal effort

As the report makes clear, corporate executives and CEOs in particular are the highest paid employees in the land by many multiples of AWE. I believe most Australians have a strong notion of a "fair day's pay for a fair day's work". I believe this is a central, agreed understanding in the unwritten social contract, a core value, that distinguishes civilised societies from the warlord barbarities of a country such as Afghanistan, where the social contract barely holds. When the powerful and privileged exploit their position and plunder unearned, and especially undeserved wealth from the system, they violate the social contract. When they are seen to stroll away unchallenged, outrage and disgust seep through society. If it happens often enough, these poisons harden into cynicism; a loss of faith in the institutions which exist to uphold the social contract. This creates an environment where our best natural impulses, including honesty and altruism, are more likely to mutate into the cancer of ruthless self interest and a culture of getting away with whatever we can and sod everyone else.

Juggernauts, devotional vehicles of Hinduism, are pulled along by the efforts of the many. Corporations, the devotional vehicles of capitalism, are likewise pulled along by the cooperative efforts of the many. CEOs and other executives fill important roles, but the elevation of the CEO to almost Messianic status devalues and undermines the contributions of everyone else in the company. When fairness is done and seen to be done, it fosters the enthusiastic cooperation of everyone in the organisation. And it is often the ordinary employees of a company who are its best ambassadors. My recent experience with a courteous and diligent Telstra technician did more to rebuild Telstra's standing than any action of David Thody. Meanwhile, the many failed and false corporate Messiahs are never put to the financial crucifixion they deserve. And as the Draft also says, there is little or no correlation between executive pay and corporate performance. Astonishing – but not surprising. The only strong link identified is between corporate size and pay.

The senior executives of large companies have generally played no role in building them. They walk in as paid employees. They should not be able to walk out as looters. The taxpayers of Australia built the value in Telstra. Sol Trojillo and his mates only succeeded in substantially demolishing it, while looting it of some $30m. Thanks suckers. Unearned, undeserved; a violation of the social contract. And every Australian knows it. Yet there is no effective mechanism – and no recommendation in the Draft - to claw it back or prevent a recurrence once memories fade.

The concentration of greater and greater wealth into fewer and fewer hands is one of the greatest social ills. It is a core responsibility of government in a civil society to set rules to prevent this. The social contract should trump the corporate contract every time.

American economist Michael Hudson said (RN, LNL 12 Oct 09) that over the last 25 years the richest 1 percent have gone from owning around 40 percent of the country's wealth to 66 percent. The owners of corporate America now own the American government. American democracy is a shell, the reality is almost feudal capitalism**.** Corporate greed is pushing Australia in the same direction.

2) Who should be paid what?

A refreshing contrast with the CEOs is John O'Sullivan, a salaried scientist with Australia's wonderful blokes' (and blokesses') shed, the CSIRO, a publicly owned and operated enterprise. On a wage that wouldn't get Trojillo out of bed, he invented WiFi. Yet the CEOs of companies which exploit that technology will make more out of it in one year than John O'Sullivan will be paid in a lifetime. Likewise our great medical researchers such as Ian Fraser, Fiona Stanley and recent Nobel prize winner Elizabeth Blackburn. People such as these make far greater contributions to our prosperity and well-being than a lucky dip packed with CEOs .These are our best and brightest, here is real merit.

The CEO of Pacific Brands (aka Socks `n Jocks) is paid three times the PM's $340,000. Does anyone really think running a company that makes socks, jocks and T-shirts and sticks them on the shelves of K-mart, Target and Big W involves three times the skills, talent, complexity or effort as performing the PM's job and deserves or requires three times the reward? And doing so under constant Opposition attack and media scrutiny? Corporate executive pay levels violate our fundamental understanding of "a fair day's pay for a fair day's work". By what perversion of values have we allowed greed to so distort what should be merit-based pay scales, that the head of a very humdrum company is paid three times the PM and probably seven times a productive scientist?

The simple fact is corporate executives are paid in vast and increasing disproportion to their actual contribution to corporate and community prosperity and the sociopathic greed and envy driving it can only be addressed successfully by strong black-letter regulation as recommended by the ACTU – and many citizens.

3) Pay caps would probably improve executive, board and corporate performance!

All civilized societies recognise the need to put a floor under poverty. Time now to take the next evolutionary step and put a ceiling on wealth – at least for employees. Genuine entrepreneurs are in another category.

Absolute caps may well improve the performance of all in the corporate sector – because they would drain away the twin poisons of greed and envy from their working lives and allow the development of better quality human relationships within the organisation. It would encourage the genuinely talented executives to take jobs based on skills, interests and passion rather than the baited carrot of the pay packet. We might then get a return of real, long-term commitment, now so lost.

The ratcheting effect examined in the Draft (P89ff) is a manifestation of envy.

4) Incentive pay and targets

These are often evils, particularly in mature industries in saturated markets. Incentives encourage the easy option of sackings and outsourcing and an externalising of corporate costs onto the community (taxpayers). And the results; more social and financial stress borne by the least able, lost skills and the depression of scrap-heaping. I support the ACTU observations on this and the remedies.

5) The Culture of CEOism

The CEO (and a close circle of mates) gets all the credit for corporate success when things go well, as if hardly anyone else contributed. When things go bad the CEO (and mates) get the benefit of all the excuses. This breeds a sense of overweening entitlement disconnected from performance. They are paid for occupying the position and acting the part of “big man”.

6) Fly-on-the-Wall CEO cam

Ordinary employees these days are often subject to very close scrutiny of what they actually do while at work. But close the door to the CEO suite and who know what he’s up to. Is he working for the company or networking and nebulising for the next big leg up? So let’s have the CEO on CCTV streaming live to shareholders. Shouldn’t the company’s most expensive employee be subject to the tightest scrutiny?

I am surprised the Draft did not examine what CEOs and senior executives actually do for their money. Or that CEOs didn’t regale the Commission with details of their visions, actions, bold, innovative decisions that built wealth, or lay the tangible evidence of their high value on the table.

7) The wealth gradient

Countries with shallower gradients between lowest and highest paid and between poorest and richest are better societies than those with very steep gradients.

8) It’s the economy, stupid

I would amend Bill Clinton’s reputed adage to read: It’s the economy in service of the whole community, stupid.