

Shareholder Consideration of the Annual Remuneration Report of a Listed Company

A Guide for Consideration of the Issues

1. Executive Summary

- The new *Corporations Act* requirements for a remuneration report and a non-binding shareholder vote (part of the CLERP 9 amendments) come into force for the reporting year on or after 1 July 2004
- Boards need to (re)consider remuneration policies and structure now, as these will be subject to the new reporting requirements
- The format of the remuneration report will require careful consideration to ensure it meets legislative requirements, has appropriate transparency, promotes shareholder understanding and is defensible
- The approach of the board at the annual general meeting (AGM) to the non-binding shareholder resolution concerning the remuneration report should be planned in advance. This will include consideration of the following issues:
 - The AGM agenda and the form of resolution
 - Whether amendments to the resolution will be accepted
 - Proxies
 - Conflicts of interest
 - Pre-AGM shareholder questions and discussions
 - Show of hands versus a poll at the AGM
 - The board's response should the resolution not be approved
- If the resolution is not approved, the board may:
 1. Accept or partially accept the vote, which may mean a review of the remuneration policies, structure and packages; or
 2. Not accept the vote and explain why it believes the remuneration policies and packages are appropriate
- Whether or not the resolution is approved, director and senior executive remuneration will require a heightened "issues management" approach by boards.

2. Background and Scope of This Paper

Amendments to the *Corporations Act* in June 2004 introduced, among other things, expanded director and executive remuneration disclosure requirements and a requirement for listed companies to submit a “remuneration report” to shareholders for a non-binding vote.

While legislative, accounting standards, and stock exchange requirements on director and executive remuneration disclosure existed prior to June 2004, this new series of provisions was introduced in a bid to ensure “shareholders are provided with sufficient information about corporate performance to allow them to make informed decisions about the board’s performance in setting remuneration for directors and executives”.¹

It remains the responsibility of directors to recommend aggregate director remuneration to shareholders, to determine levels of individual director remuneration and to determine executive remuneration policy and structuring, but the new requirements dictate active shareholder consideration of these issues at the annual general meeting (AGM). The amendments also introduce a new concept, that of a vote by company shareholders that is not binding on a company.

Some forethought by boards in the annual report and AGM planning process for 2004/05 is required in relation to these changes. This paper considers issues stemming from the new provisions and how boards and the chairman might deal with this in the lead up to the AGM, at the AGM, and/or subsequently.

This paper is not intended to prescribe solutions – it is intended to raise relevant issues for consideration so that directors may consider them in the context of their company. The issue of shareholder approval of remuneration reports will be kept under review by the AICD. As practice in this area develops, future papers on this subject may be produced with guides, case studies and examples to assist directors and chairmen.

¹ Paragraph 4.359 of the Explanatory Memorandum accompanying the draft legislation.

3. Summary of the new Corporations Act provisions

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (CLERP 9) introduced amendments to the *Corporations Act* for listed companies. As far as these changes are relevant to this paper, these changes impact:

- The contents of the annual directors' report to shareholders (by introducing a "remuneration report" component)
- The notice of meeting for the AGM
- Proceedings at (and potentially actions subsequent to) the AGM.

These changes apply to financial years commencing on or after 1 July 2004 and apply to any company listed on a prescribed financial market – including the Australian Stock Exchange. Consequently the changes will apply to the 2005 directors' report and 2005 AGM². However, boards need to consider the impact now in order to plan - including (re)consideration of remuneration policies during the 2004/05 financial year.

The requirements as to the content of the remuneration report overrule any contrary provisions in a listed company's constitution.

In summary the new requirements are as follows:

- The annual directors' report to shareholders of a listed company must include a separate "remuneration report" section outlining:
 - Board policy on remuneration of directors, company secretaries and "senior managers" (and other "group executives" in the case of a consolidated entity)
 - The relationship between board remuneration policy and company performance. This is to include discussion of company earnings and consequences of performance on shareholder wealth for the relevant financial year and four previous years (including discussion of dividends, share price changes and return of capital)
 - If a remuneration element is dependent on performance
 - a summary of the performance condition (and why chosen),

² Companies with a reporting period other than a financial year may have a different timetable to consider.

- methods used in assessing satisfaction (and why chosen), and
 - if the performance condition involves comparison with external factors, a summary of those factors
 - The prescribed details of remuneration of each director and top 5 executives (and, if different, “group executives” in the case of a consolidated entity) – including
 - the proportions of remuneration consisting of performance-based remuneration and options, and
 - certain details regarding options, including valuation
 - If director or executive remuneration includes an element of securities and that element is not performance-based, an explanation of why
 - For persons employed under a contract – details of duration, termination notice period and termination payments (s300A)
- Standard business of a listed company’s AGM now includes consideration of a resolution that the remuneration report be adopted (s250R(2))
 - The notice of AGM for a listed company must inform shareholders that the resolution on the remuneration report will be put to the meeting (s249L(2))
 - The information in the AGM notice of meeting must be clear and concise (s249L(3))
 - At a listed company’s AGM, the chairman must allow reasonable opportunity for shareholders to ask questions about or make comments on the remuneration report (s250SA)
 - The shareholder vote is advisory only and does not bind directors or the company (s250R(3))
 - The legislation also alters the requirements in respect of retirement benefit limits for directors and executives – s200F.³

(Source: *Corporations Act*)

The shareholder vote only needs to be passed as an ordinary resolution.

³ The full text of the legislation should be referred to, as only a brief outline is permitted in the scope of this paper.

4. Other relevant requirements

The new provisions summarised above do not alter the continuing *Corporations Act* and/or ASX Listing Rule (“Listing Rule”) requirements for:

- Shareholder approval of “related party” transactions between directors and companies⁴ and of financial assistance to buy shares in the company⁵
- Continuous and periodic disclosure, including notification of the holding of the AGM and shareholder resolution outcomes, changes of a director’s interests, periodic reporting and annual reports (and their content)
- Shareholder approval of aggregate director remuneration⁶ and termination benefits⁷
- Shareholder approval for issues of securities and options⁸ and
- Employee incentive schemes.⁹

Regard should also be given to:

- The ASX Corporate Governance Council’s *Principles of Good Corporate Governance and Best Practice Recommendations* (“ASX Principles”)¹⁰
- Accounting standards which currently apply to disclosure of remuneration in financial accounts,¹¹ and
- The company’s constitution. While the new legislation overrules any contrary provisions in a company’s constitution to the extent that they apply, regard should be given to the various provisions of the constitution, particularly in relation to the AGM process.

Detailed consideration of these and other relevant requirements is beyond the scope of this paper.

⁴ Chapter 2E of the *Corporations Act*. Note that s211 contains an exception for reasonable remuneration.

⁵ Chapter 2J of the *Corporations Act*.

⁶ Listing Rule 10.17. The company constitution is also likely to contain relevant provisions.

⁷ Note Listing Rule 10.19 and the *Corporations Act* s200A et seq.

⁸ Including Listing Rule 10.11

⁹ Listing Rule 10.14

¹⁰ Particularly Principle 9 (Remunerate fairly and responsibly) and associated recommendations

¹¹ Australian Accounting Standards Board’s *AASB 1046: Director and Executive Disclosures by Disclosing Entities* of January 2004 is particularly relevant to listed companies. The standard applies to annual reporting periods ending on or after 30 June 2004. The *AASB 1046* requirements for remuneration disclosure appear not entirely consistent with the CLERP 9 amendments to the *Corporations Act* either with respect to persons whose remuneration requires disclosure or the contents of disclosure.

5. Overseas experience

The UK has had a regime in place since 2002 (for “quoted companies”) in respect of the requirement for a remuneration report and a non-binding shareholder vote¹². Since the regime’s introduction there has been some history of shareholder concern over, and failure to approve, remuneration reports. This has included several top 250 FTSE companies.¹³

It has been stated that in the U.S., more than 40% of all governance proposal resolutions submitted by shareholders for inclusion in AGM agendas held in 2003 asked companies to change the way they compensate executives.¹⁴

Based on this experience, shareholder activism on remuneration is not a theoretical concern and boards must give some early attention to the issue in Australia.

¹² See *The Directors’ Remuneration Report Regulations 2002* pursuant to the UK *Companies Act*

¹³ In May 2003, 50.72% of GlaxoSmithKline shareholders rejected its remuneration report due to concern over a potential £22m termination payout to the CEO. A revised report was passed a year later (with 82.4% support), following consultation with institutional investors by the chairman.

No other FTSE 100 companies have suffered similar fate. J. Sainsbury PLC would have become only the second FTSE 100 company to have its remuneration report rejected if it were not for the votes of the Sainsbury family. Shareholders were concerned at a US\$4.3m bonus being paid to the CEO despite the company’s diminishing market share and profit.

In 2004, two FTSE 250 companies - Aegis, and Eurotunnel - have had their remuneration reports rejected by shareholders on the basis of ‘excessive’ CEO remuneration packages. In addition, three FTSE SmallCap companies (one advertising, one pharmaceutical and one IT) had their remuneration reports rejected.

¹⁴ See B Martin and R Sankey: *Shareholder democracy: an analysis of current trends*, PLC Global Counsel Corporate Governance and Directors’ Duties Handbook 2004, 2nd edition, Practical Law Company, p 21. Also, some recent decisions in the U.S. courts have some relevance for remuneration of executive directors and chairmen. Issues of fiduciary duty, dealing in good faith, arms-length negotiation of remuneration, and the need for robust remuneration determination processes have been raised.

6. Issues to consider

The issues to be considered may be divided into two categories – issues which need consideration well prior to the AGM and issues for the AGM itself. These are dealt with in the following two sections.

6.1 Issues prior to the AGM

In planning the response to the new *Corporations Act* requirements there are a series of issues to consider during 2004/05 well prior to consideration of the directors' report, remuneration report and the AGM. These are considered below.

6.1.1 Review of board remuneration, and executive remuneration policy and structure

The new shareholder non-binding vote opens the way for stakeholders to revisit remuneration decisions by the board, so board processes and decision-making, particularly those in setting remuneration policy and remuneration, need to be robust and transparent.

Consideration should be given to reviewing current remuneration policy¹⁵, structure and settings for both directors and executive management to ensure clarity and completeness (especially where there are performance-based or variable components) and alignment, where necessary, with corporate strategy, business plans and the remuneration market. In particular, given the thrust of the new legislation, the link between remuneration policy and corporate performance needs review. It will be harder to explain remuneration policy and structure to stakeholders if it is not clearly articulated by the board and management. This may involve the need for (re)engaging external expert advice:

- To benchmark director remuneration
- To benchmark and/or re-design the executive remuneration structure.

Current letters of appointment for directors and employment contracts for executives may then need to be reviewed to ensure they reflect and/or comply with current remuneration policy and structures.

Other board processes, including minutes and board papers, should be reviewed again to ensure that it can be shown, if necessary, that directors have been diligent and have considered and addressed appropriate issues.

¹⁵ "Remuneration" is widely defined and includes termination and performance-based payments.

6.1.2 Review the impact of the new legislation

In order to meet the new disclosure requirements and deadlines there is a need to consider:

- Which additional personnel are covered by the new disclosure requirements – particularly those employed within the consolidated group but not within the listed entity itself
- What additional aspects of remuneration need to be included in the disclosure – particularly performance-based components
- Whether:
 - the current board/committee and corporate calendars, and
 - the schedule for board evaluations and executive performance reviews (and resulting bonuses)

are aligned so that the remuneration policy can be (re)considered, and if necessary (re)set, and remuneration finalised, in an orderly way when compared to the disclosure deadlines related to the remuneration report.

6.1.3 Shareholder understanding of remuneration report

The proposed resolution on the remuneration report should be presented to shareholders in a clear and concise way in terms of the notice of meeting, the resolution itself and the accompanying explanatory material.¹⁶

Thought should be given to:

- The presentation of the remuneration report material for ease of understanding by shareholders, and
- Whether further supplementary explanation is desirable in the explanatory material accompanying the notice of AGM,

so that remuneration structuring, individual director and executive remuneration, and the reasons for remuneration structuring can be fully understood by shareholders and if necessary discussed at the AGM in an informed way.

¹⁶ A suggested formulation of the remuneration resolution in the notice of meeting or accompanying material is “The Remuneration Report required by section 300A of the Corporations Act, as contained in the Directors’ Report for ABC Company Ltd for the year ended [insert], is approved”.

In particular, boards should consider a clear explanation of the reasons why they recommend adoption of the remuneration report to shareholders. This explanation may cover issues such as:

- The board process of consideration and approval of remuneration policy and levels and types of remuneration, including:
 - Whether external advice was sought – it is probably good practice to get such advice, although the overall situation of each company will be different¹⁷
 - Whether the whole board or only the remuneration committee considered the matters in detail
 - Whether comparative industry or company remuneration data were considered
- Alternative remuneration policy/structures considered by the board
- The reasons for adoption of remuneration policy and rejection of alternatives.

Shareholder failure to approve the remuneration report is not necessarily without consequences, notwithstanding that the vote is non-binding. Boards may also consider outlining possible consequences of a shareholder failure to approve the remuneration report, which could include:

- Possible director resignation(s) if the failure is perceived by them to be a vote of no confidence (although care is required so this is not put as a threat to shareholders)
- difficulty attracting experienced, competent directors and /or executives in the future.

Should a board choose not to follow the shareholder vote, there will be no legal effect on remuneration terms through that action alone, although shareholder and other stakeholder reactions will have to be dealt with. If a board adopts a position to either accept or reject the shareholder vote, the board should consider whether and to what extent it will communicate this position in the explanatory material. In the interest of transparency, it would seem that any firm board position on the matter should be fully communicated.

The order of agenda items at the AGM and in the notice of meeting should be considered so that enough time is left for debate and consideration of the remuneration report. Apart from *Corporations Act* and ASX Listing Rules requirements as to notices of meetings, companies should have regard to the

¹⁷ Consider whether external advice can be classified as fully 'independent' if remuneration consultants are paid other than a flat fee eg. a fee related to levels of director and/or executive remuneration. Also consider whether the advice is to be made available to shareholders or otherwise disclosed in some form; if so, the advisor should be specifically asked to consent to this.

guidance in the *ASX Principles* (particularly Principle 9 and associated recommendations) and the *Guidelines for notices of meeting* contained in Attachment A to the *ASX Principles*.

The *ASX Principles* also contain recommendations on disclosure of company policies including website disclosure. Thought should also be given to such disclosure in addition to the (annual) remuneration report circulation to shareholders.

While the remuneration report requires discussion and analysis of a number of issues, presentation of the material on director and executive remuneration components and amounts may be amenable to a graph, table or tabulation-style presentation, as this is often an easy way to communicate information in a succinct manner.

The new legislation clearly intends that the vote should be taken separately from other items of business on the AGM notice of meeting, notwithstanding that the remuneration report is part of the directors' report.¹⁸ Therefore the proposed resolution on the remuneration report should not be grouped with any other proposed resolution (including adoption of the directors' report).

6.1.4 Pre-AGM shareholder questions and discussions

Thought should be given to:

- whether shareholders are invited (in the notice of meeting or explanatory material or otherwise) to submit written questions on the remuneration report to the board in advance of the AGM, and
- how the board will respond, and what deadlines apply to receipt if this course is followed.¹⁹

Giving shareholders this ability will facilitate informed response by the board at the AGM and potentially better debate of any issues.²⁰

Companies with large shareholders (including institutional shareholders) should consider whether there are any remuneration report issues that can be discussed with those shareholders in advance of the AGM so that respective positions are understood. In doing so, boards need to remain cognisant of continuous disclosure obligations and ensure no shareholder or set of shareholders is given market sensitive information that would require general disclosure.

¹⁸ s250R(2) of the *Corporations Act*.

¹⁹ s249P of the *Corporations Act* requires companies to circulate members statements that meet the Act's criteria. This would include any material the required number of members wishes to have circulated in relation the proposed resolution on the remuneration report.

²⁰ The Chairman should ensure that major issues raised by a significant number of shareholders in written questions received at least two business days prior to the AGM are answered at the meeting - refer to paragraph 20 of the AICD's and ASA's *The Conduct of Annual General Meetings – Code of Best Practice*.

6.1.5 Proxies

As with other resolutions to be put to shareholders at an AGM, the proxy form sent to shareholders should contain provision for shareholder voting on the question of the remuneration report and should comply with *Corporations Act*, Listing Rule and constitutional requirements.²¹

The board needs to consider whether and to what extent any proxy solicitation is to take place on the issue of the remuneration report. Generally, a board is entitled to solicit proxies.²²

Consideration should also be given to disclosing in the explanatory material sent with the notice of meeting, directors' intentions as to how they will vote any undirected proxies lodged in their favour.²³

6.1.6 Conflicts of interest

Both the *Corporations Act* and the Listing Rules contain complex provisions regarding voting in situations of conflict²⁴ and a full examination of these is not possible in this paper. However, as the remuneration report obviously pertains to director and executive remuneration and will (presumably) be recommended by directors to shareholders for adoption, thought should be given to whether directors (and relevant executives who hold shares) should vote and whether voting exclusion statements are required. Any conflicts should be clearly set out. If directors intend to vote on the remuneration report – presumably in favour – their intentions should be set out in the explanatory material sent with the notice of meeting.

6.1.7 Director liability

While it is apparent that the government, in introducing the new non-binding vote requirement, did not see legal consequences for not following the shareholder vote²⁵, questions arise as to whether this is entirely true in all cases. For example, if a company becomes insolvent subsequent to an AGM at which directors ignore the negative vote, and the insolvency was partially due to remuneration increases to directors and /or executives, liability may accrue to directors. Circumstances will differ in each case, and if a director has a concern then legal advice should be sought.

²¹ See *Corporations Act* s249Y et seq, Listing Rule 14.2. The form should contain options for voting – 'for' and 'against' (refer Listing Rule 14.2.1) and 'abstain' (refer to the *Guidelines for notices of meeting* contained in Attachment A to the *ASX Principles*).

²² See for example Lang: *Horsley's Meetings - Procedure, Law and Practice*, 4th edition p195.

²³ Note that a statement of the chairman's voting intentions on undirected proxies is required by Listing Rule 14.2.3 of the Listing Rules require a voting exclusion statement to be included in the notice of meeting, and the proxy form specifies that the chairman is appointed the proxy in the absence of a shareholder nomination of the proxy.

²⁴ For example note *Corporations Act* ss191 and 192, and Listing Rules 14.2 and 14.11. Regard should also be given to the constitution.

²⁵ Refer to paragraph 5.436 of the Explanatory Memorandum accompanying the draft legislation and to the explanation in the Bills Digest No 166 2003-04.

6.1.8 The board response to negative shareholder vote

Shareholders may not support the proposed resolution on the remuneration report either wholly or in part. However, uniquely, as the shareholder vote is non-binding the board will have a choice to accept, partially accept or not accept the shareholders' negative vote. Boards need to review two issues in advance of an AGM:

- how they will respond to any shareholder failure to support the resolution, and
- the timing of their response.

Response choices

Boards can realistically adopt one of the following responses:

- accept (or partially accept) the shareholder failure to support, or
- not accept the shareholder failure to support and explain their reasons why.

Different consequences will follow depending on the board's reaction and the board should consider its position in advance, especially if the remuneration report is likely to be controversial.

If the board is to accept or partially accept shareholder failure to support the remuneration report, board consideration will need to be given to:

- Any impact on letters of appointment for directors and employment contracts with executives including:
 - the issues of whether board acceptance may expose the organisation to breach of contract under letters of appointment and/or contracts of employment with executive staff and
 - whether such contracts should be made subject to that vote – not a particularly realistic option at least in the case of executives as they may not be inclined to accept this as a contract condition
- Remuneration policy and structure re-setting subsequent to the AGM
- The need for further external expert remuneration advice.

A board may decide not to accept the shareholder vote in which case an explanation to shareholders is warranted. It can be argued that directors are elected to represent shareholders in the overall governance of the company and that directors are in a better position to review and approve director and executive remuneration; if shareholders disagree with directors, their ultimate remedy is not to re-elect directors.

Timing of the board response

Prior to the AGM, boards should consider the timing of their response to a shareholder vote to not support (or only partially support) the remuneration report – in particular, whether the response is:

- At the AGM as part of the proceedings on the day or subsequently as an adjournment, or
- Taken under consideration by the board and dealt with subsequent to the AGM (in which case the issue of communication of the board's response to shareholders needs to be considered).

If rejection of the shareholder negative vote is to be dealt with at the AGM, then explanatory material covering the boards' response needs to be prepared in advance so that the chairman is prepared. More difficulty may be experienced with this approach, as there may be less certainty as to the particular issues of concern to shareholders that may be raised at the AGM. Also, this approach does not cater for any amendments to the proposed remuneration resolution which are accepted and approved at the AGM.

If rejection is to be dealt with subsequent to the AGM, then thought needs to be given to whether the AGM is to be adjourned and reconvened (raising issues as to cost, suitable timing and venue and any requirements for a new notice of meeting) or the rejection is noted by the board as an issue that the board will respond to after the AGM. The latter course of action would appear to be the better choice in most situations as the board can respond in a measured and reasoned way, assimilating any views expressed at the AGM but without the need to reconvene the AGM.

6.2 The AGM itself

The board needs a plan as to how to deal with issues arising at the AGM including applicable meeting procedure, any amendments that may be proposed to the resolution, whether a poll is to be called, and (if the board is to respond at the AGM) the board response to any failure to approve the resolution on the remuneration report. These issues are briefly reviewed below.

6.2.1 Meeting procedures

Ultimately, the chairman has control of the proper conduct of an AGM. Normal shareholder meeting procedures should be applied to shareholder consideration of the remuneration report bearing in mind the new specific *Corporations Act* requirement that the chairman must allow reasonable opportunity for shareholders to ask questions in relation to the remuneration report.

Advance consideration by the board, and especially the chairman, of the conduct of the AGM proceedings on the remuneration report is recommended especially in relation to:

- handling shareholder comments and questions and debate generally
- timing issues.²⁶

Procedures for answering shareholder questions should be agreed so that it is clear whether the chairman will respond or will direct these to the Remuneration Committee chairman, the chief executive or another senior executive. It would seem appropriate for the chairman or committee chairman to answer questions relevant to board and chief executive remuneration and also executive remuneration policy set by the board; the chairman could direct detailed questions on executive remuneration (other than the chief executive's) to the chief executive.

Consideration can also be given to preparing for questions from the floor by preparing, in advance, a likely list of questions and responses, so that the chairman and directors can be as prepared as possible to respond in an informed way and add to the quality of AGM discussion on the remuneration report.

The AICD supports the position that as a general rule journalists should be given access to the AGM.²⁷ If the press is admitted to the AGM the board needs to be

²⁶ Generally accepted meeting procedures include:

- Time limits should not normally be set on questions or debate, except with support of the meeting
- Questions and debate should be germane
- Without the support of the meeting debate should not be curtailed if shareholders still wish to speak, but the chairman has the right to curtail discussion if questions or comments are irrelevant, repetitive or cause unnecessary delay.

²⁷ See paragraph 10 of the AICD's and ASA's *The Conduct of annual General Meetings – Code of Best Practice*.

aware of the public relations aspects of how and when it responds to the shareholder vote on the remuneration report.

6.2.2 Amendments to the proposed remuneration report resolution

A detailed examination of whether and to what extent shareholders can move amendments to the proposed remuneration report resolution is beyond the scope of this paper, but consideration of the company constitution and accepted meeting procedures is required.²⁸

The board should consider the extent to which amendments to the proposed resolution on the remuneration report (for example, an amending motion may propose a partial acceptance of the remuneration report) will be accepted either in advance of the AGM or at the AGM. Obviously, if an amendment is accepted at the AGM, shareholders not in attendance will not have an opportunity to consider it. On the other hand, care must be taken by the chairman in rejecting a valid proposed amendment without putting it to a vote. In summary any proposed amendment:

- must fall within the scope of the original proposed resolution in the notice of meeting
- must not materially alter, negate, contradict or be inconsistent with the original proposed resolution, and
- should desirably be submitted in writing (for clarity).

6.2.3 Show of hands versus poll

As with other AGM resolutions, voting on the remuneration resolution must be conducted in accordance with requirements of:

- The *Corporations Act*
- ASX Listing Rules
- The company constitution.

Subject to provisions in a company's constitution permitting the chairman to call a poll, the board should consider its position on whether the vote on the remuneration report is to be carried on a show of hands or whether a poll is to be called by the chairman, and if so when – immediately, later in the meeting or subsequent to the AGM. This may especially be important where a vote on the floor may result in a “no” vote but a poll is likely to result in a “yes” vote (or the reverse) as the chairman has a duty to ascertain the sense of the meeting and should probably call a poll in this case. Also important in this respect is the question of when the Chairman discloses the overall summary of proxy voting to

²⁸ For further reading, see Lang: *Horsley's Meetings - Procedure, Law and Practice*, 4th edition Chapter 10.

the AGM. To do it before shareholder debate on the resolution may stifle that debate; to do it after the debate and before the resolution is put to the AGM may be perceived as wasting time or influencing attendees on how they vote. It is a matter for the Chairman's judgement which strategy should be used in this situation. One option might be for the Chairman to seek guidance from the meeting on this point.

As to the exercise of proxies:

- If the proxy form specifies the way the holder should vote and the proxy is the chairman, the proxy must vote on a poll and must vote in the way designated²⁹
- When directors are appointed proxies, the better view seems to be that they should exercise their proxy votes³⁰
- Where the chairman and/or directors hold uncommitted proxies any discretion in exercising the proxies should be exercised in good faith and in the best interests of the company. If the uncommitted proxies are to be used to overturn the vote of shareholders present at the AGM, an explanation should be given by the chairman.³¹

In the rare event that the chairman has to exercise any casting vote at the AGM, advance thought should be given as to whether this will be used in favour or against, or at all, in respect of the remuneration report resolution.³²

6.3 Stakeholder communication

If the board does not accept the shareholder vote board consideration will need to be given to the issues of stakeholder communication and reputation management.

Regardless of whether the board responds to the shareholder vote at or after the AGM, the board needs to give thought to:

- the method of communication of its position and the results of the AGM,
- the audience - including shareholders

²⁹ s250A of the *Corporations Act*.

³⁰ See Lang: *Horsley's Meetings - Procedure, Law and Practice*, 4th edition p.195.

³¹ See paragraph 27 of the AICD's and ASA's *The Conduct of Annual General Meetings – Code of Best Practice*.

³² As the Board is (presumably) recommending the remuneration report, the casting vote could be exercised in favour – if this is the case, consideration should be given to disclosing this in the explanatory material sent with the notice of meeting. However the issue of conflict of interest also needs to be considered as the remuneration report contains material regarding director remuneration. The preferable course may be to refrain from exercising the casting vote. "When a Chair exercises a casting vote, it is regarded as preferable, generally speaking, to give it against the motion..... However, there may be circumstances where the Chair may decide that the best interests of the body are likely to be served by giving a casting vote in favour of, for instance, a well-investigated and carefully planned proposal of the board of directors or management committee, about the merits of which the members are equally divided in their voting" Lang: *Horsley's Meetings - Procedure, Law and Practice*, 4th edition p.175.

- whether a summary of shareholder questions asked and the company's response(s) will be provided³³.

Transparency remains the key. If the board's response to the shareholder vote is to be given at the AGM then obviously shareholders in attendance will be appraised of the board position. But given that not all shareholders can attend an AGM, the company needs, in addition to any requirements to notify results of shareholder resolutions to the ASX, to consider transparency and the issue how and when it will disclose the vote on the remuneration report and the board's reaction to it to both shareholders not in attendance at the AGM and to other stakeholders.

If the board decides not respond at the AGM to a shareholder failure to support the remuneration report and defers consideration, then again in the interests of transparency the board needs to consider both a full level of explanation and the methods of communication and the audience (including shareholders).

Options to consider in communication are all or some of the following:

- company website
- shareholder mailout
- institutional shareholder briefings
- analyst briefings
- media release
- press conference
- internal staff publications or communication materials.

Depending on the options selected, material should be prepared in advance, in the case the board's position on the shareholder vote is decided pre-AGM, or after the board's position is known. This should fully explain the board's position. Continuous disclosure requirements need to be considered in relation to the timing of the board response(s).

³³ A practice encouraged and commended by the AICD – refer to paragraph 22 of the AICD's and ASA's *The Conduct of Annual General Meetings – Code of Best Practice*.

7. Conclusion

There are a number of issues to consider in relation to the new *Corporations Act* requirement for shareholder consideration of the remuneration report. These issues include remuneration policy, legislative, Listing Rule, meeting procedure, and shareholder and other stakeholder communication considerations.

Director and senior executive remuneration will require a heightened “issues management” approach by the board. Early preparation and consideration of the issues by boards will ensure that the board’s position on director and executive remuneration is clearly thought out, established and enunciated to shareholders in a reasoned, transparent and timely way. While shareholders have the choice to ultimately decline to support the remuneration resolution, advance preparation will avoid as much as possible, any misunderstanding of board positions on the issue of director and executive remuneration.

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