

THE 2009 AGM: RUN FOR COVER OR STAND AND BE COUNTED?

In the current hiatus between the FY09 results and the upcoming AGM season a strong wind of retail and institutional shareholder agitation has begun to blow...

Three principal areas of grievance are filling media columns and dominating web chatter this year:

- Perceived **lack of fairness in capital raisings** during the past year, particularly the heavy reliance on raising capital through the highly dilutionary (and heavily discounted) non renounceable rights issues, private placements and /or capped SPPs
- **Excessive remuneration** of current and past directors and senior executives, especially the payment of bonuses based on so-called 'underlying profit', which excludes the worst damage of the financial crisis and
- **Board composition**, which is still largely drawn from a very shallow pool of age, gender and experience

Gripes about these issues are sure to be loud as shareholders gather in the next few weeks to pass judgement on their Board's performance. Chairmen may find themselves in the uncomfortable position of being challenged to defend and justify actions seen by many investors to have breached a fundamental duty of Directors to protect the rights of shareholders and ensure they are treated fairly.

Corporate Governance

Each of the three identified areas of shareholder concern has a direct connection with aspects of corporate governance and disclosure and most investors and analysts will this year be paying more

attention than usual to the Corporate Governance Statement ("CGS") included in the annual report.

The CGS is a company's position statement as to its adherence, or otherwise, to the ASX Corporate Governance Council's Principles and Recommendations ("ASX Principles"). Australian listed companies are indeed fortunate to have this set of 'road rules' to guide them along the highway of governance rectitude.

Many of the issues currently exercising shareholders could have been avoided had some Boards paid closer attention to the principles so carefully articulated in the ASX governance handbook .It is too late at the AGM for Boards to find retrospective excuses for actions and behaviour deemed by some angry shareholders to have failed to meet appropriate standards of good corporate governance. So if there is robust questioning from the floor then Chairmen may to some extent have to grin and bear it. But neither should Chairmen hold back when they believe that criticisms are unfair or exaggerated.

The toughest issue this year will undoubtedly be **capital raising**. Specifically directors' perceived willingness to bypass shareholders and sanction a dilution of their equity through discretionary placements, non renounceable rights issues and capped SPPs. This goes to the heart of ASX Principle 6, "*recognising, demonstrating observation of, and respecting the rights of shareholders*".

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Often this may easily be defended by the need for speed and efficiency. For some companies a placement was the only available option amongst many that were canvassed during a period of tight credit. Reminding shareholders of the dire state of debt and equity markets between October 2008 and March 2009 and how that impacted the pricing of new issues will be sufficient in those instances where the level of corporate distress was extreme.

It may be more difficult for those companies that raised capital when the market was rallying and institutions and retail investors were keen to invest their stockpiles of cash. It is estimated that institutional investors have benefited by more than \$5bn from retail dilution alone over the past year.

Providing some outline of the board's process in structuring future equity issues so as to ensure loyal shareholders have their interests protected may well offset the sense of abandonment and betrayal felt by many shareholders – both institutional and retail.

Equally, after an annus horribilis, **remuneration** will be particularly scrutinised – especially bonus payments and option schemes. ASX Principle 8 states that boards should focus on *“remunerating in a way which attracts appropriately skilled individuals at board and executive level and reflects the performance expectations of shareholders”*. The introduction of a non-binding vote on remuneration several years ago provided the mechanism by which shareholders can keep their board accountable for that task and they do so each year without fail.

The challenge faced by Chairmen this year will be to bridge the gap between the size of the headline grabbing bonuses and termination payments and the destruction in shareholder value typically being reported. At the very least companies will need to prepare clear statements as to how the board has actively discharged its duties. This includes a plain English explanation of the process by which Directors' and senior executives' remuneration has been determined - both in the financial year past and present, what the bonus structure is, and how performance collectively and individually is measured against reward.

The issue of **Board composition** may be a more delicate matter. Every year shareholders are presented with the stark reality of how small and homogenous the cohort of directors representing them on Australian boards

continues to be. The Chairman of a top 100 company typically presides over a Board that consists of Caucasian males in their 50's or 60's. This observation is confirmed by the fact that over the past 20 years the pathetically small percentage of women on ASX200 boards (now 8.3%) has actually declined, not increased.

Australia leads the world in the breadth of equity investment from across the whole community and shareholders increasingly expect that companies will look carefully at the diversity of experience, background and skills of its Board members. For those companies that take seriously ASX Principle 2, *“ensuring an appropriate balance of skills, experience and independence of board members”*, the AGM is an opportunity for the Chairman to explain how they satisfy the test or what process they are implementing to ensure it will be met in the future.

While it is perhaps a truism that there is, all other things being equal, a direct relationship between the level of focus a Board places on improving its governance practices and the long-term success of that Company's business strategies it is a fact of life that Company Boards ignore at their peril.

This is because proactive corporate governance is, at its most fundamental level, really about effective **risk management and clear communication**. Companies that manage risk better than others achieve long-term competitive advantage and steadily improve their reputation, an intangible prize that is so hard to attain and so easy to lose.

Overall, the ASX Principles encapsulate the standards necessary for a solid, efficient and sustainable business. They provide a genuine attempt to codify the principles of good housekeeping and, if appropriately implemented, will add value to the bottom line.

Being prepared at this year's AGM to demonstrate a company's governance processes and why they are appropriate for its individual circumstances, is likely to address many shareholder's concerns.

Listening to shareholder questions and grievances, and recognising where there might be different ways to address issues going forward, is the next step in improving and refining corporate governance and operational processes.