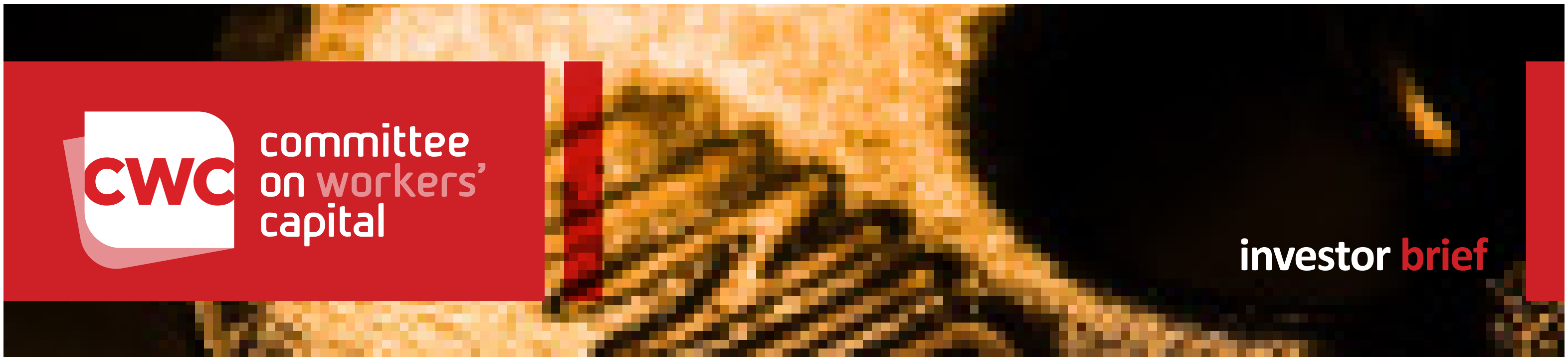


contents

The Global CEO Paywatch table provides the salaries of the top 10 paid CEO's in Australia, Canada and the US and the result of Say-on-pay votes demonstrating increasing discontent by investors

Global CEO Paywatch: Trends in Executive Compensation

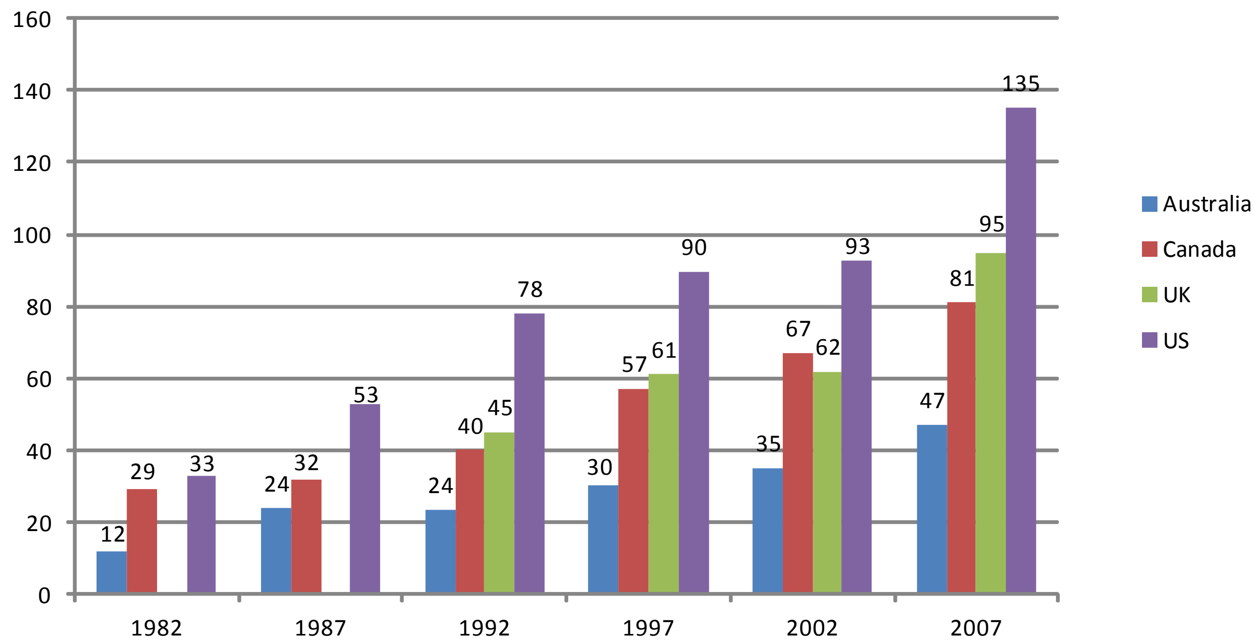
OVERVIEW

In recent years, investors, academics and non-governmental organisations along with the general public have become increasingly concerned about executive compensation practices deemed to be excessive. Indeed, executive compensation has increased at a rapid pace since the 1980's. This has occurred against a backdrop of increasing inequalities in income distribution in OECD countries. Policymakers, along with investors across the globe, have reacted to varying degrees. In some countries, policymakers have adopted laws requiring companies to hold Say-on-Pay votes, publish CEO-to-worker pay ratios or limit bonuses. Pension funds are increasingly using their ownership rights to voice discontent when executive compensation packages are considered excessive.

Trends in executive compensation and income inequalities

In recent decades, executive pay has risen dramatically across industries and across the globe. For example, in 1982, in the United States, the CEO-to-worker pay ratio was 42:1, a ratio which rose to 354:1 in 2012[i]. Concurrently, inequality in the distribution of incomes increased in almost all OECD countries between the mid 1980's and now[ii]. Below, the table demonstrates the evolution of the average income earned by the top 0.1% earners (representative of executive incomes without capital gains[iii]) relative to the income of the bottom 90% earners (reflective of average incomes) in selected OECD countries[iv]: Climate change is the result of the increase in greenhouse gas concentrations in the atmosphere generated by human activities. Climate change is leading to an increase in the frequency and intensity of extreme weather events, as well as long-term transformation in weather patterns. If emissions are left uncontrolled or only marginally reduced, climate-related risks, including catastrophic events, will increase further, exposing millions of people and the economy at large.

Average income of top 0.1% earners relative to the average income of bottom 90% earners (1982-2007)



Source: http://topincomes.g-mond.parisschoolofeconomics.eu/

Why has executive compensation increased so much?

Many arguments have been advanced to explain the increase in executive pay. Among the most prominent are the following:

- Global market for “star” executives: Over the last decades, globalisation (e.g.: improvements in information technology, increased commercial and financial integration) has transformed the market for star executives from a national into a global one. Employers want the best person in the world and compete with compensation in other jurisdictions to attract “star” executives[v];
- The widespread adoption of performance-based compensation packages: Since the late 1980’s, academics and shareholders pushed for increased performance based pay incentives, often in the form of stock options. These packages were supposed to increase performance sensitivity. Because part of their pay was now “at risk”, the level of compensation was increased to compensate for “risk”[vi];
- Changes in the nature of the CEO job: increased outside hires, increased likelihood of being fired and an increased emphasis on general rather than firm-specific skills has increased opportunities for CEO mobility and led to an increase in compensation to attract best talents [vii][viii][ix];
- Interlocked directorates: A director may serve on the board of multiple corporations or an executive of one firm may sit on the board of another firm and vice-versa. This interconnectedness between boards of directors and executives across large corporations may result in complacent behaviour when it comes to setting executive compensation. Compensation committees wishing to remain collegial with the executives may thus set excessive compensation packages that are not tied to performance[x].

The reaction to excessive executive compensation

The rise in executive compensation has received increasing attention since the 1990’s for two main reasons: First, several highly publicised cases of excessive compensation packages for executives have been linked to well-known scandals in the US (e.g.: Enron) and in the UK (e.g.: Prudential and Vodafone). Second, the global financial crisis drew public attention to the issue of compensation practices in the financial sector. These events occurred against a backdrop of growing income inequality in OECD countries[xi].

Investors and policymakers have reacted to excessive compensation practices. In 2002, the UK was the first country to pass legislation mandating a non-binding shareholder vote on executive compensation. The aim of the Say-on-Pay vote was to improve "accountability, transparency and performance linkage of executive pay"[xii]. Similar measures were taken in the United States and Australia in 2010 and 2011 respectively. In other jurisdictions where Say-on-Pay is not yet mandatory, like Canada, investors have put increased pressure on companies to hold such votes. As part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, a measure requires companies to report on CEO-to-worker pay ratios; as of October 2013, the Securities and Exchange Commission was proposing to implement this rule. At the same time, the European Union's European Banking Authority has released draft rules blocking bonuses of more than double fixed pay.

Impact of Say-on-Pay votes on executive compensation

Say-on-Pay votes have had several impacts on CEO compensation. In the UK, where Say-on-Pay votes have been held at public companies' annual general meetings since 2002, a study found that firms have responded to rejection votes by scaling back CEO pay practices that rewarded failure (e.g.: generous severance contracts) and increasing the sensitivity of pay to poor firm performance[xiii]. In the US, where mandatory votes were signed into law in 2010, evidence is starting to emerge regarding the impact of the votes on CEO compensation. A study has found that boards of directors have reacted to Say-on-Pay rejection by reducing compensation, thereby suggesting that such votes are an effective mechanism to address problems of excessive compensation packages[xiv]. In Australia, increased investor scrutiny since the financial crisis combined with the 'two strikes' rule in Say-on-Pay votes has resulted in decreased average CEO fixed pay in the Top 100 companies in 2012 year-over-year[xv]. Evidence also suggests that certain institutional investors, such as public sector pension funds, are more likely to be associated with Say-on-Pay rejection votes[xvi].

Next steps for pension trustees

Studies demonstrate that an increase in shareholder voice is indeed contributing to curbing excessive pay practices. As a result of growing awareness of the risks of excessive executive compensation, pension trustees and their funds are increasingly taking the following actions:

- Closely monitoring the link between pay and performance at companies held in their portfolios to ensure the good stewardship of the pension savings of plan beneficiaries;
- Demanding that their fund managers report on their proxy voting records and provide a rationale for supporting or opposing each Say-on-Pay vote; and
- Publicly urging securities regulators to require companies to hold Say-on-Pay votes - either binding or advisory – and to disclose the ratio of CEO to average worker pay.

For an extensive list of the top paid CEO's in these countries, please see the following web resources:

- **Australia:** "CEO Pay in the Top 100 Companies: 2012", The Australian Council of Superannuation Investors
- **Canada**: "Overcompensating: A Fact Sheet on Executive Pay in Canada – January 2013", Canadian Centre for Policy Alternatives
- **United States:** "100 Highest-Paid CEOs", AFL-CIO

Global CEO Paywatch Table

The table below provides information on the top 10 paid CEO's in Australia, Canada and the United States for corporations where Say-on-Pay votes were held (from 2012 to 2013 depending on data availability). This table shows that 60% of Say-on-Pay votes for the top 10 paid US CEOs at the most recent Annual General Meeting had less than 75% support. In Canada, 40% of the equivalent votes received less than 75% support. In Australia, all votes received more than 75% support in 2012 after a decrease in year-on-year salaries at the Top 100 companies.

Country	Company	Executive	Year of salary	Compensation (USD)[1]	Result of Say on Pay vote[2]
Australia	Westfield	Peter Lowy / Steven Lowy	2012	19,655,507	97%
	Australia and New Zealand Bank	Mike Smith	2012	9,020,710	96%
	Westpac Banking Corp.	Gail Kelly	2012	8,943,777	91%
	BHP Billiton	Marius Kloppers	2012	8,876,504	96%
	James Hardie Industries	Louis Gries	2012	8,428,307	91%
	Rio Tinto	Tom Albanese	2012	8,196,653	95%
	National Australia Bank	Cameron Clyne	2012	8,186,414	78%
	Origin Energy	Grant King	2012	7,783,851	92%
	Suncorp Group	Patrick Snowball	2012	7,706,468	97%
	Wesfarmers	Richard Goyder	2012	7,468,742	89%
Canada	Canadian Pacific Railway	E. Hunter Harrison	2012	47,643,897	71%
	Thomson Reuters Corp	James C. Smith	2012	18,228,413	84%
	Talisman Energy	John A. Manzoni	2012	18,098,432	75%
	Magna International inc.	Donald J. Walker	2012	16,334,329	75%
	Royal Bank of Canada	Gordon Nixon	2012	13,310,803	94%
	Catamaran Corp.	Mark Thierer	2012	12,497,057	94%
	Suncor Energy Inc.	Steven W. Williams	2012	11,704,838	93%
	Barrick Gold Corp.	Jamie C. Sokalsky	2012	11,012,838	15%
	Agrium Inc.	Michael M. Wilson	2012	10,820,757	82%
	Bank of Nova Scotia	Richard E. Waugh	2012	10,760,789	94%
USA	Oracle Corp	Lawrence J. Ellison	2012	96,160,696	41%
	Activision Blizzard Inc	Robert A. Kotick	2012	64,942,306	74%
	Cheniere Energy Inc	Charif Souki	2012	57,518,332	57%
	Credit Acceptance Corp	Brett A. Roberts	2012	54,282,500	85%
	McKesson Corp	John H. Hammergren	2013	51,744,999	53%
	HCA Holdings	Richard M. Bracken	2012	46,359,246	98%
	Jefferies Group LLC	Richard B. Handler	2012	45,182,239	99%
	Level 3 Communications Inc.	James Q. Crowe	2012	40,708,970	53%
	Exxon Mobil Corp.	R.W. Tillerson	2012	40,266,501	70%
	Nuance Communications Inc	Paul A. Ricci	2012	37,077,679	41%

[1] Canadian and Australian converted to US dollars exchange rate on September 16th 2013

[2] Result of Say on Pay Votes come from ASX filings by companies in Australia, SEDAR filings in Canada and EDGAR filings in the United States

Endnotes

i] http://www.aflcio.org/Corporate-Watch/CEO-Pay-and-You/, accessed 16 September 2013.

[ii]OECD (2011). “Divided We Stand: Why Inequality Keeps Rising”, OECD Publishing. p.23

[iii]Executives, managers and financial professions make up for 59% of the top 0.1% income group.

[iv]There is no reliable way to measure the evolution of CEO-to-worker pay over time; the table above is a used as a proxy to demonstrate relative change in executive-to-worker compensation

[v] OECD (2011). “Divided We Stand: Why Inequality Keeps Rising”, OECD Publishing.

[vi]Ibid

[vii]Garicano, Luis, and Esteban Rossi-Hansberg (2006), “Organization and Inequality in a Knowledge Economy,” Quarterly Journal of Economics, 121, p.1383–1435.

[viii]Giannetti, Mariassunta (2006). “Serial CEOs’ Incentives and the Shape of Managerial Contracts,” mimeo, Stockholm School of Economics

[ix]Frydman, Carola (2005). “Rising through the Ranks. The Evolution of the Market for Corporate Executives, 1936–2003,” mimeo, Harvard University.

[x] Bebchuk, L & Fried, J. (2004). “Pay without performance: The unfulfilled promise of executive compensation”, Harvard University Press: Cambridge.

[xi]http://www.nber.org/digest/dec08/w13982.html, accessed 16 May 2013

[xii]Baird, J. and Stowasser, P. (2002) Executive compensation disclosure requirements: the German, UK, and US approaches, PracticalLaw.com, PLC Document 4-101-7960, September 23.

[xiii]Ferri. F, Maber. D. (2013). “Say on Pay votes and CEO compensation: Evidence from the UK”, Review of Finance, 17, p.527-563.

[xiv]Kimbro, M & Xu, D. (2013). “Shareholders have a say on executive compensation: evidence from Say on Pay in the United States”, Working Paper Series.

[xv] http://www.workerscapital.org/images/uploads/ACSI-CEO Pay in Top 200 Companies 2012 EMBARGOED Sep13.pdf, accessed 20 Sept 2013

[xvi] Kimbro, M & Xu, D. (2013). “Shareholders have a say on executive compensation: evidence from Say on Pay in the United States”, Working Paper Series.

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