

**DISCLOSURE OF EXECUTIVE REMUNERATION AS A CORPORATE GOVERNANCE
CONTROL MEASURE IN SOUTH AFRICAN LISTED COMPANIES**

by

NEIL ULRICH

**Submitted in accordance with the requirements
for the degree of**

DOCTOR OF BUSINESS LEADERSHIP

at the

UNIVERSITY OF SOUTH AFRICA

SUPERVISOR: PROF J A DE VILLIERS

OCTOBER 2010

Declaration

Student number: 3198-470-3

I declare that **DISCLOSURE OF EXECUTIVE REMUNERATION AS A CORPORATE GOVERNANCE CONTROL MEASURE IN SOUTH AFRICAN LISTED COMPANIES** is my own work, and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

SIGNATURE

(Mr N Ulrich)

DATE

Acknowledgements

First of all I want to thank God for giving me the strength, determination, patience and guidance to complete this research.

I also wish to express my sincerest gratitude to the following people, without whose support and assistance I would not have been able to complete this research, and grow both as a person and a scholar:

- Professor Andre de Villiers, my promoter, for his guidance, support and patience throughout the research process.
- My family, Michelle, Charl and Kian, who sacrificed so much in terms of quality time they could not always spend with me, for their understanding and unwavering support.
- The academic staff of the UNISA Graduate School of Business Leadership, for their much valued guidance and support. Their ideas, constructive criticism and advice was invaluable in shaping this study.
- The staff at the UNISA Graduate School of Business Leadership library, for their keen interest and fantastic support in locating much of the reference material I consulted during the research.
- All the study participants who either agreed to be interviewed or formed part of a focus group, for their willingness to do so.
- My colleagues and friends in the South African Reward Association, who were always more than willing to share ideas and to engage in discussions on remuneration principles and practice in South Africa.

“Never again clutter your days or nights with so many menial and unimportant things that you have no time to accept a real challenge when it comes along. This applies to play as well as work. A day merely survived is no cause for celebration. You are not here to fritter away your precious hours when you have the ability to accomplish so much by making a slight change in your routine. No more busy work. No more hiding from success. Leave time, leave space, to grow. Now. Now! Not tomorrow!”

- O Q Mandino

Dedication

To the memory of my father, George Ulrich, who supported and encouraged me so much during my studies, fought so hard against ailing health to celebrate graduation with me, but sadly passed on a mere 85 days before my graduation.

Table of Contents

EXECUTIVE SUMMARY	12
1. INTRODUCTION	17
1.1 Problem statement	20
1.2 Research objectives	21
1.3 Contribution of the research to existing body of knowledge	23
1.4 Limitations of the research.....	27
1.5 Definitions of key terms.....	29
1.5.1 Corporate governance	29
1.5.2 Disclosure.....	30
1.5.3 Executive remuneration	30
1.5.4 Remuneration.....	31
1.5.5 Stakeholder.....	32
1.5.6 Total remuneration.....	32
1.6 Assumptions.....	33
1.7 Chapter Plan.....	34
2. LITERATURE REVIEW.....	36
3. DEVELOPMENT OF THE MODERN CORPORATION.....	41
4. CORPORATE GOVERNANCE.....	48
4.1 Background and development of corporate governance in modern business	51
4.2 Forms of corporate governance measures.....	60
4.2.1 Internal measures	64
4.2.2 External measures	69
4.2.3 Shareholder activism.....	71
4.3 Corporate governance regulations	73
4.3.1 Legislative regulation.....	74
4.3.2 Guidelines contained in voluntary codes	75
4.4 Problems associated with corporate governance.....	82
4.5 Corporate governance trends.....	84
4.6 Concluding remarks.....	90
5. EXECUTIVE REMUNERATION.....	96
5.1 Origins and nature of executive remuneration	98
5.2 Composition of executive remuneration packages.....	100
5.3 Executive remuneration theories	105
5.3.1 Agency theory.....	107
5.3.2 Social comparison theory	110
5.3.3 Stakeholder theory	110
5.3.4 Managerial power theory	111
5.3.5 Tournament theory.....	111
5.4 Problems associated with executive remuneration.....	112
5.4.1 Excessive executive remuneration.....	113
5.4.2 Conflicts of interest.....	115
5.4.3 Setting of executive pay	118
5.4.4 The role of boards.....	124

5.5	Modern trends in executive remuneration	125
5.6	Conclusion	130
6	DISCLOSURE OF EXECUTIVE REMUNERATION	133
6.1	The reasons for disclosure.....	135
6.2	The nature and extent of disclosure.....	142
6.3	Disclosure trends	152
6.4	Conclusion	159
7	THE ROLE OF DISCLOSURE OF EXECUTIVE REMUNERATION IN A CORPORATE GOVERNANCE FRAMEWORK	163
7.1	Executive remuneration and corporate governance	166
7.1.1	The alignment of conflicting interests	167
7.1.2	Internal and external corporate governance mechanisms	174
7.2	Disclosure and corporate governance.....	178
7.3	Conclusion	182
8	CONCLUSIONS FROM LITERATURE REVIEW.....	184
9.	RESEARCH PROPOSITIONS.....	188
9.1	First Proposition	189
9.2	Second Proposition.....	190
9.3	Third Proposition.....	191
9.4	Fourth Proposition	192
10.	METHODOLOGY	193
10.1	Research methodology and design	196
10.1.1	Research philosophy	197
10.1.2	Research approach	198
10.1.3	Research strategy	200
10.1.4	Research process.....	202
10.2	Sample selection.....	204
10.3	Data collection and preparation methods.....	209
10.4	Justification for using these methods.....	212
10.5	Research instruments	217
10.6	Method for testing propositions	222
10.7	Nature and form of results	223
11.	ANALYSIS AND RESEARCH RESULTS	224
11.1	Phase 1: Disclosure requirements.....	225
11.1.1	Legislation	227
11.1.2	King Codes on Corporate Governance	229
11.1.3	JSE Listing Requirements	237
11.1.4	Conclusions	242
11.2	Phase 2: Sample selection and quantitative analysis	250
11.2.1	Sample selection	251
11.2.2	Quantitative analysis of disclosures in Annual Reports.....	255
11.2.3	Conclusions from quantitative analysis	280
11.3	Phase 3: Qualitative analysis.....	285

11.3.1	Research process.....	286
11.3.2	Analysis of qualitative data	290
11.3.3	Conclusions	347
12.	CONCLUSIONS AND RECOMMENDATIONS	354
12.1	Research problem	354
12.2	Research objectives	355
12.3	Research propositions	357
12.4	Research analysis and results	358
12.4.1	Literature review.....	359
12.4.2	Executive remuneration disclosure requirements	363
12.4.3	Quantitative analysis	365
12.4.4	Qualitative analysis	370
12.5	Findings on research propositions	381
12.6	Recommendations	384
12.7	Future research	387
	REFERENCES.....	389
	ANNEXURES.....	403

List of Figures

1.	The development of the modern corporation _____	44
2.	Corporate governance control measures _____	61
3.	Systems view of corporate governance _____	63
4.	WorldatWork Total Rewards Model _____	100
5.	Executive remuneration package _____	101
6.	The causal relationships in an executive balanced scorecard _____	123
7.	Disclosure model _____	150
8.	Geopolitics of executive remuneration _____	169
9.	Value add through inclusive and effective corporate governance measures _____	194
10.	The research process onion _____	196
11.	Research process _____	203
12.	Sampling techniques _____	204
13.	Executive remuneration disclosure locations per industry _____	258
14.	Executive remuneration disclosure locations per research category _____	259
15.	Annual Report disclosure analysis per category _____	268
16.	Annual Report disclosure analysis per industry _____	268
17.	Areas of compensation disclosure being revised due to SEC requirements _____	342

List of Tables

1.	Balanced Scorecard measures _____	103
2.	Arguments for and against voluntary disclosure _____	136
3.	European disclosure trends _____	154
4.	Drivers of executive remuneration disclosure reform in Europe _____	157
5.	Differences between deductive and inductive processes _____	199
6.	Research strategies _____	201
7.	Probability sampling techniques _____	206
8.	Non-probability sampling techniques _____	206
9.	Threats to reliability and validity _____	214
10.	From rules-based to principles-based corporate governance _____	236
11.	Annual Report disclosure results _____	252
12.	Final sample composition for qualitative analysis _____	254
13.	Location of multiple disclosures _____	261
14.	Location of aggregated remuneration tables _____	262
15.	Differences in disclosure characteristics _____	263
16.	Typical content per disclosure location _____	266
17.	2007 Annual Report disclosure distribution _____	267
18.	Industry Disclosure cross-tabulation _____	273
19.	Chi-square test results _____	274
20.	Symmetric measures _____	275
21.	What causes corporate governance failures _____	309
22.	Impact of ineffective corporate governance on executive remuneration _____	318
23.	Disclosure characteristics across research categories _____	330
24.	Factors influencing companies' disclosure choices _____	337
25.	The role of Boards and Board Committees in disclosures _____	346

List of Annexures

A.	Stakeholder framework_____	404
B.	Inclusive / Systems view of corporate governance_____	405
C.	Corporate governance reports of different countries_____	406
D.	GRI Guidelines_____	407
E.	Executive remuneration theories_____	408
F.	Voluntary disclosure checklist_____	409
G.	Current disclosure practices across Europe_____	410
H.	Comparative governance measures in EU countries_____	411
I.	Preliminary research sample_____	412
J.	Annual Report Disclosure Compliance Index_____	413
K.	Interview schedule_____	414
L.	Sample interview schedule_____	415
M.	King II guidelines on components of executive remuneration_____	416
N.	Draft Annual Report disclosure tables_____	420
O.	Guidelines for the disclosure and determination of remuneration for non-executive and executive directors_____	421
P.	Phase 2 results_____	426
Q.	Locations of executive remuneration disclosures_____	431
R.	Annual Report Disclosure analysis (Numbers of companies)_____	432
S.	Critical values of the Chi-Square distribution_____	438
T.	UK Directors' remuneration report under the Companies Act, 1985_____	439

Key terms used

Annual Report

Board of Directors

Corporate governance

Disclosure

Executive remuneration

Listing requirements

Remuneration Committee

Shareholder interests

Stakeholder

Total remuneration

TERMINOLOGY	
Term	Description / Definition
Base pay	The guaranteed basic pay or salary received every month by employees in exchange for time / services / knowledge / competence, excluding incentives.
Benefits	Programmes employers use to supplement cash remuneration, including health, income protection, different types of leave, savings and retirement programmes.
Bonus	The incentive amount employees earn as a result of performance. Also referred to as performance bonus.
Guaranteed remuneration	The concept according to which base pay, allowances and employer-related costs of benefits are added to arrive at an amount referred to as guaranteed remuneration or also referred to as guaranteed package. Remuneration is also referred to as compensation in mostly American literature.
Incentives	Payments typically resulting from performance over a period of up to 12 months and made payable after the results have been compared to pre-determined targets.
Long term incentives	Incentives of which the measurement / exercise period is typically longer than one year, typically share option, restricted shares, share appreciation rights, phantom shares.
Performance bonus	The incentive amount employees earn as a result of performance. Also referred to as a bonus.
Recognition	Acknowledgement of employee actions, performance and behaviour that meets intrinsic psychological and emotional needs and can be done formally, informally, in cash or non-cash (e.g. trophies, certificates).
Share Option	A right granted to an option holder, but not an obligation, to sell or acquire an underlying share at a specific price at a future date.
Shares	Shares granted to eligible employees typically at no cost to the recipient.
Total cost to company	Total remuneration plus the cost of long term incentives.
Total remuneration	Guaranteed remuneration plus the cost of short term incentives and associated benefits. Also referred to as total package.
Total rewards	Everything that employees receive from their employers (financial and non-financial rewards, intrinsic and extrinsic, direct and indirect) as a result of their employment with an organisation, including goods and services that are offered as payment in kind.
Total reward framework	The combination of all possible rewards offered to employees to attract, retain and motivate them included in a framework for employees from which to choose in order to develop their own reward profile.
Transactional rewards	Tangible rewards arising from transactions between employers and employees, including pay and benefits.
Transparency	Employees are informed of the reasons for pay and reward policy decisions.
Variable pay / remuneration	Remuneration that is not guaranteed, also referred to as incentives, either short- or long-term.

EXECUTIVE SUMMARY

Corporate governance and executive remuneration are not new phenomena, but have erupted to the forefront of corporate, academic and public attention as a result of a series of well publicized corporate collapses and scandals over the last decade, which have raised both a curiosity of executive remuneration levels, and an awareness of the potential impact of conflicts of interest between owners and executives in modern corporations. Although literature on corporate governance and executive remuneration in general is plentiful, there is a lack of comment on the relationships between certain specific components of these two broad constructs. These specific components, such as disclosure, executive remuneration and governance needed to be analysed individually before they could be combined into a whole that explains both their interrelationships with each other and the larger corporate governance sub-system, and ultimately in the corporation, as an organisational system.

In view of greater globalisation of the world economy, and the market for executive talent, the consequent reforms in the fields of corporate governance and executive remuneration, as well as the changing competitive dynamics of modern corporations, it was necessary to examine whether traditional theory and regulatory frameworks have kept pace with corporate development. A review of both classic and current literature show vastly different approaches to both executive remuneration and corporate governance mechanisms practiced around the world. There is however a noticeable trend towards convergence of

these different sub-systems. The most prominent differences in respect of these sub-systems relate to the extent to which disclosures are made. Some of these issues relate to full or limited disclosure, internal or external corporate governance measures to regulate executive remuneration, and differences in respect of a narrow shareholder focus or broad stakeholder focus of different interests in an organisation.

This doctoral thesis analysed disclosure of executive remuneration, as a sub-component in the executive remuneration / corporate governance debate, individually and in relation to other sub-components of the larger corporate governance system. This was done in an attempt to develop a best practice for the alignment of conflicting interests that characterise the modern corporation, and as a possible contribution to an inclusive and effective corporate governance system in organisations.

The study contributes to an understanding of the underlying reasons for disclosure of executive remuneration, and its part in a corporate governance system in which disclosure interrelates with several other control measures. A distinction is made between backward-looking disclosure for the purpose of monitoring of executive actions, and forward-looking disclosure which publishes relevant information to assist informed investor decisions. In addition the study analyses different approaches in disclosure practices around the world, and the reasons for such differences. Disclosures by virtue of legislative or regulatory requirements are compared to voluntary disclosures, in terms of the underlying

reasons for corporate strategy in relation to disclosure preferences and practices.

The main assumption which guided the study was that corporate governance control measures have become ineffective in addressing problems that arose out of the development of the modern corporation. Although some of these problems can be ascribed to the separation of ownership from control, modern theory questions the accuracy of the assumptions that have underpinned the popular agency theory since the 1930's. Broader stakeholder interests, globalised practices and needs, and increased protection against powerful and self-serving managers, have caused a need for change in traditional corporate governance control measures. This study analysed how one of these control measures, namely disclosure of executive remuneration, could contribute to improving an inclusive corporate governance system in order to make it more effective.

Although this research was essentially qualitative, it also included a measure of quantitative analysis from the executive remuneration disclosure practices of companies listed on the Johannesburg Stock Exchange (JSE) in South Africa. Besides analysing the content of executive remuneration disclosures in the 2007 Annual Reports of these companies, qualitative interviews and a focus group were done with a representative sample from those companies. This sample had been stratified to enable cross-industry and cross-sectoral comparisons.

Following a systems thinking research philosophy, this research was mainly inductive and explanatory. Data was collected by means of literature analysis, interviews, a focus group, and content analysis of executive remuneration disclosures in Annual Reports. In order to do so, the requirements for disclosure of executive remuneration in South Africa were collated from the South African Companies Act, the King I and II Reports on Corporate Governance, and the JSE listing requirements. JSE listed companies were ranked into categories which reflected their levels of compliance (less/same/more than the minimum disclosure requirements) with the collated disclosure requirements, on the basis of their executive remuneration disclosures as contained in their 2007 Annual Reports. Finally, qualitative interviews were conducted with representatives from a stratified sample of those companies, to find a deeper meaning and context of such disclosure practices, in an attempt to test the propositions developed in this study.

Factors were identified which distinguished between companies that disclose less than, equal to, or more than the collated minimum disclosure requirements. Despite identifying a general trend across all sectors to make executive remuneration disclosures which merely comply with the minimum disclosure requirements, cross-industry and cross-sectoral analysis was done to identify disclosure trends within and across different industries and sectors.

This research has shown that ineffective internal and external corporate governance control measures contribute to corporate governance failures, and

that both the high levels of executive remuneration and the conflicted process for determination of executive remuneration packages are symptomatic of the failure of corporate governance control measures. In addition, the research has shown that effective disclosure of executive remuneration levels and processes, and the underlying reasons and performance measures that inform it, as an external corporate governance control measure, could contribute to more effective corporate governance in an organisation, but that disclosure should not be relied upon in isolation. The intricate relationships between all internal and external corporate governance control measures should be finely balanced to achieve a desired improvement in a corporate governance framework.

A myriad of factors that inform the disclosure choices of organisations have been identified. These do not only emanate from sources external to the organisation (such as the regulatory environment), but also from internal sources (such as capacity or cost-benefit comparisons). Ultimately it was found that companies have to balance comprehensiveness of disclosures, which could be both costly and increase complexity, with simplicity and the extent to which the disclosed information is both useful and understandable, but that an effective such balance could lead to effective corporate governance in an organisation.

1. INTRODUCTION

"I see in the near future a crisis approaching... corporations have been enthroned, and an era of corruption in high places will follow until all wealth is aggregated in a few hands."

- Abraham Lincoln

It is commonly believed that corporate governance is a measure to regulate and control one of the key characteristics of the modern corporation, namely the separation of ownership from control, which is especially acute in organisations with a dispersed ownership structure. Although corporate governance is not a new phenomenon, its pre-eminence in business and society today has been escalated to the forefront of academic attention, particularly in the light of many well-publicized recent corporate collapses and scandals, such as Enron, WorldCom, One.Tel, and in South Africa, Leisure Net and African Bank.

Executive remuneration has featured very prominently as a focus point in the corporate governance debate following such corporate scandals, in view of some considerable concern over the high levels of executive remuneration, and in particular, the perceived lack of a relationship between executive performance and executive reward. This interest has been ascribed to both a

public fascination with the “how much” question, as well as a greater awareness of the potential impact of conflicts of interest between owners and agents in modern corporations (International Corporate Governance Network, 2002). After suggesting that the literature is full of stories of excessive executive pay where prominent companies failed, Pepper (2005), records that the top 200 executives at Enron earned an annual total compensation of US\$ 1.4 billion in 2000, which translates to an annual average of US\$ 7 million per executive for the year. Statistics of this nature are plentiful, but what is generally lacking is comment on the rationale for these levels of pay, and especially whether these can be justified in relation to the performance of executives.

Corporate governance is however a wide and complex construct that comprises of many different components, but that ultimately simply amounts to a reinforcement of sound management principles. The spate of corporate failures since the 1990’s have shown that corporate governance is not without shortcomings. In order to consider an inclusive and effective corporate governance framework, it is necessary to analyse the individual components thereof, and their interrelationships with each other.

Senge (2006) suggests that a system cannot be healthier than the sub-systems on which it depends. He adds that the inability of leaders to see the systems in and patterns of interdependency within and surrounding organisations threaten our future. He concludes that there is no right model for a complex system, but that the criterion that ought to be used is usefulness rather than accuracy, and

that this requires an insight of how systems work and fit together to solve a problem. This study therefore explored both a deeper understanding of the rationale for and benefits of disclosure of executive remuneration, as one of the sub-systems of an inclusive corporate governance system in an organisation, and its interrelation with other sub-systems therein.

Despite significant literature in relation to corporate governance and business management, the field has been evolving with such intensity and speed, that traditional theory in this regard needs to be critically evaluated to determine whether it is still relevant in the modern environment. Drucker (1987) suggests that there is still a great deal to be learnt from traditional management theory, but that the major challenges facing modern business are new ones that require consideration well beyond the traditional field of management theory. Nonetheless, he still considers traditional theory as a valuable foundation in a field where management success has not changed the work of management, but essentially its means. For this reason, it was important to first consider the traditional theories and principles that underpin corporate governance, executive remuneration, and disclosure. This would not only be essential to ultimately better understand these constructs, but also to evaluate the extent to which these theories and principles are still applicable to the new challenges faced in modern corporations, or in need of change.

1.1 Problem statement

The recent increased focus on corporate governance and executive remuneration in the business environment highlighted the fallacy that traditional corporate governance control measures are able to adequately cope with the increasing conflicts of interest between shareholders, as assumed owners of the modern corporation, and increasingly powerful executives who run these corporations. These well recorded conflicts of interest are however only symptoms of a much more fundamental principle of the modern corporation, namely the potential conflicts of interest between different stakeholders. Traditionally these stakeholders include both shareholding investors, who are assumed to enjoy ownership rights in the corporation, and a wider category of stakeholders who have interests in the long term sustainability and growth of the corporation. The nature of ownership of the modern organisation is therefore put in contention.

The main problem which informed this study is therefore that it seems that corporate governance as a construct has not kept pace with the development of the modern corporation, and to such an extent that the corporate governance control measures that operate within the larger corporate governance system have become ineffective in many ways. The ineffectiveness of these corporate governance control measures in turn causes symptoms that impact on the core rationale of the modern corporation. One of these symptoms is excessive executive remuneration. Another symptom is the inefficient executive

remuneration pay-setting process. These symptoms of ineffective corporate governance control measures materialise in both internal (board composition and effectiveness) and external (disclosure and regulation) aspects. Each of these has an individual and collective impact on the total corporate governance system in a firm.

In addressing the main problem, the following issues have to also be considered:

- whether it is possible to increase the effectiveness of corporate governance control measures generally by improving individual sub-systems within the corporate governance framework;
- how individual sub-systems interrelate with each other in an inclusive corporate governance framework;
- what the role of disclosure of executive remuneration is in an inclusive and effective corporate governance framework; and
- how a better understanding of the strategic role of disclosure of executive remuneration can improve corporate governance in a corporation.

1.2 Research objectives

Effective disclosure of actual executive remuneration packages, the linkage thereof with specific objectives and philosophies, and the process and factors for determination of executive remuneration packages, have a potentially significant contribution towards an effective and inclusive corporate governance

framework, but cannot solve all its problems in isolation. The most appropriate mix between internal and external control measures must be found and implemented to ensure an effective overall corporate governance system. Disclosure as a mechanism to monitor, control and inform executive remuneration is an increasing phenomenon worldwide. It is however used in different ways and to a different extent in each separate company. Despite current debate over the possible congruence of corporate governance systems across the world, significant differences remain unexplained.

The main objective of this study is therefore to determine and understand how an effective system of disclosure of executive remuneration, which is both informative (or forward looking) and allows for executive monitoring (or backward looking), could contribute towards an inclusive and effective corporate governance system, having also regard to environmental and societal differences influencing corporate structures across the world.

In order to achieve this objective it would be necessary to consider, amongst others, the following issues:

- whose interests ought to be served by a corporate governance system;
- what the relationship is between executive remuneration and corporate governance;
- what the optimal regulatory framework is for executive remuneration and corporate governance;
- what constitutes disclosure best practice in a globalised market; and

- how disclosure of executive remuneration could contribute to good corporate governance control measures in modern corporations.

1.3 Contribution of the research to existing body of knowledge

Although corporate governance has evolved into a much researched field that is information-rich, Bury and Le Blanc (2007) convincingly aver that the scope of the field is so vast and fast developing, that there is always scope for further studies on specific aspects within the broad concept of corporate governance. Kakabadze, Kakabadze and Kouzmin (2004) affirm that despite the fact that executive remuneration, as a sub component of the corporate governance construct, is one of the most intensely researched areas, it is probably one of the least understood. They suggest that current debate and research in this area have focused mainly on the excessiveness of executive remuneration, specific remuneration structures, and the link between executive remuneration and performance, but that little has been done to explain the relationship between executive remuneration and its impact on a broad category of stakeholders, based not only on financial impact, but on broader corporate social responsibility impact. It is for this reason that this research sought to explain the rationale, dimensions and potential impact of disclosure of executive remuneration on a more effective and inclusive total corporate governance

system in an organisation, in which different stakeholder needs, whether for informative or monitoring information or a combination thereof, could be satisfied better.

The literature review below has exposed a general gap in empirical research and comment on the interrelationship between specific corporate governance practices and executive remuneration. Crotty and Bonorchis (2006) comment on the paucity of South African information on the subject of executive remuneration, where there is almost no academic, journalist or research papers on the subject. The literature review conducted for this study has shown that this is in stark contrast with the abundance of such information sources in the USA and UK, where executive remuneration has been under the spotlight for at least the past ten years. These sources are more fully dealt with in the literature review below. The lack of commentary in South Africa also impacts negatively on vigorous public debate and activism, and this study will contribute to informed such debate. It would therefore be required, in studying such relationships, to focus firstly on individual components, before attempting to integrate those into a comprehensible whole.

One of the most current and controversial governance aspects in the debate around executive remuneration relates to the disclosure of executive remuneration policy and levels, which debate has not yet yielded a clear direction between two opposite directions, namely convergence and divergence. This study attempts to inform this debate by critically analyzing the

relationship between disclosure of executive remuneration and good corporate governance in organisations.

A Price Waterhouse Coopers Executive Directors Best Practice Report (2009) reiterates the currency of the executive remuneration debate in the current global economic crisis as follows: *“Scrutiny over executive pay is now greater than ever before as a result of the economic downturn combined with public anger over the role that remuneration is perceived to have played in the collapse of financial markets. It is quite clear that change is required. The levels of trust between shareholders and Remuneration Committees are lower than ideal. Committees feel that shareholders have insufficient understanding of the commercial realities of motivating an executive team. Shareholders on the other hand feel that too many Committees adopt a stance as management advocates negotiating on management’s behalf”*.

In a changing environment therefore, where there is increased scrutiny, stakeholder activism, and reduced levels of trust on executive remuneration, it is critical that all stakeholders have both a thorough understanding and a clear perception of the nature and potential impact of disclosure of executive remuneration, and other corporate governance control measures, before informed engagements could be made. This study will empower and facilitate engagements and decisions of this nature, by not only explaining the individual sub-systems but also their interrelationships with each other.

The selected theme is therefore researchable for the followings reasons:

- There is a lack of empirical evidence of the link between specific aspects of corporate governance, such as disclosure, and executive remuneration;
- There is a need for clarity, understanding and simplicity in the currently complex field of executive remuneration;
- Traditional theory and practices have to be critically evaluated in view of modern developments and reform in both corporate governance and executive remuneration;
- The impact of increased globalisation and a worldwide marketplace on executive remuneration is not yet clear enough to inform comprehensive global corporate governance and remuneration strategies; and
- There is an increased public interest in the fields of both corporate governance and executive remuneration, which are still in a process of rapid evolution, and which often leave more questions than answers.

This study aims to add to the existing body of knowledge on the relationship between disclosure of executive remuneration and corporate governance by:

- Examining the underlying reasons for payment of executive remuneration from a corporate governance perspective;
- Analysing the role of disclosure of executive remuneration as a tool to align and reduce conflicts of interest;

- Examining the role of disclosure of executive remuneration policy and levels in relation to the traditional executive remuneration and corporate governance problems,
- Conducting a comparative analysis of executive remuneration disclosure practises in an increasingly global market; and
- Considering different approaches to corporate governance regulation.

1.4 *Limitations of the research*

Due to the very wide scope of this topic it was essential to limit the scope of the research. These limitations need to be noted at the offset.

- The first limitation is that the research does not deal with every measure found in a total corporate governance system. The study is intended to focus on disclosure of executive remuneration, as one of a number of different corporate governance control measures, to determine its role in an inclusive and effective corporate governance framework. In order to understand the larger system of corporate governance, it is important to first understand each of the sub-systems within the larger system, and how these sub-systems interrelate with each other.
- The population and sampling frame used for this research was limited to South African companies listed on the Johannesburg Stock Exchange (JSE). This however does not mean that the same principles would not

necessarily apply to other companies. The sample will however be selected to be fully representative of those listed companies to which current South African corporate governance regulatory measures apply. The research results and applicability however may have some global significance in view of convergence of the global economy and some business practices.

- Healy and Palepu (2000) convincingly note that any research in relation to disclosure is limited by the very difficult nature of measuring the full extent and impact of disclosure, as well as the significance and reasons for both the disclosure itself and the timing of such disclosure.
- Although every attempt was made to conduct this research and to present its findings as objectively as possible, it is unavoidable for the researcher to have a measure of subjectivity. Booysen (1999) suggests correctly that all research results depend on the researcher in ways in which he or she may not even be conscious of. Norum (2000: 319) takes this view further in suggesting that “*Researchers are biased. We are biased by our experiences, our education, our knowledge, and our own personal dogmas. As researchers, we inevitably commit acts of intervention*”. It is therefore inevitable that the researcher’s own background, experiences and acquired views would influence both the research and analytical processes in this study. The researcher was conscious of this potential limitation, and continuously sought to guard

against unjustifiable subjectivities. On the other hand though, these subjectivities bring about unique interpretations, where the researcher may behold or contemplate things differently from other authors, or in a different context that is more contextually aligned with the research problem identified for this study.

1.5 Definitions of key terms

The following terms are used frequently in this report, and should be defined at the offset.

1.5.1 Corporate governance

There are probably almost as many attempts to define corporate governance as there are literature sources dealing with the construct. Although the most widely used definition was formulated in the Cadbury Report (1992) as “the system by which companies are directed and controlled”, this study prefers to use the more comprehensive and descriptive definition proposed by Abor and Adjasi (2007). These authors view corporate governance as the process and structure used to direct and manage the business affairs of a company towards enhancing business prosperity and corporate accountability, with the ultimate aim of creating long term shareholder wealth whilst at the same time taking into consideration the interests of all other stakeholders (Abor and Adjasi, 2007). In

particular, the focus on the aim or result of an effective corporate governance process in their definition is compelling in the use thereof for this study.

1.5.2 Disclosure

The term disclosure refers to the publication of useful information regarding different governance aspects of the firm, which aims to reduce and eliminate information asymmetry between internal and external stakeholders of the firm. Although different means may be used for disclosures, the principle of sharing information with stakeholders in the most appropriate manner for their particular needs is critical in developing an effective disclosure model.

1.5.3 Executive remuneration

The term “executive remuneration” is often misunderstood by commentators and executives alike. One of the possible reasons for this misunderstanding could be due to the use of alternatives such as compensation, pay or reward. Although there is a growing tendency towards using the term “total rewards” in remuneration practice, to refer to both financial and non-financial allocations to employees in return for their services, the term “executive remuneration” will be used in this report with reference to the total guaranteed, short and long term financial rewards paid to company executives. Although a practice has

materialised to consider only the remuneration paid to formally appointed Executive Directors of a company as “executive remuneration”, the term should fundamentally apply to all employees with executive powers and duties.

1.5.4 Remuneration

Generally commentators agree that executive remuneration packages would consist of a combination of basic salary, benefits, short term, and long term incentives (Allcock and Pass, 2006; Hill, 2006). One would expect the basic component of the remuneration package to enable an executive to maintain a standard of living that is commensurate with the status and esteem of the position held, and for the competent performance of all required tasks associated with the job. Short term and long term incentives are ordinarily linked to a mix of performance measures (Epstein and Roy, 2005). Whether this is in practice more than a theoretical aspiration remains to be seen. The lack of disclosures of underlying performance conditions for executive remuneration packages highlighted in the analysis of disclosures in Annual Reports below reinforces this point strongly. Short term incentives are normally paid in the form of *ex post facto* cash bonuses for meeting prior agreed performance objectives within a twelve month period, whereas long term incentives are in the form of share or share option allocations to incentivise certain behaviour and actions over the long run.

1.5.5 Stakeholder

The term “stakeholder” refers to all those who benefit from the corporation and its activities within its business environment, including current and future generations (Wheeler and Sillanpaa, 1997). Annexure A sets out the possible different stakeholder groups of an organisation. The broad group of stakeholders identified therein immediately questions the overwhelming emphasis placed in most organisations on the interests of shareholders and executives, whereas the sustainability of the organisation often relies on a balanced consideration of the interests of all stakeholders in the organisation.

1.5.6 Total remuneration

Total remuneration refers to the annual flow of resources that shareholders could have kept for themselves had they not used it to compensate executives (Aggarwal and Samwick, 1999). This includes the full monetary value of all pay components, benefits and incentives. Increasingly however, organisations are realising the need to formulate employee value propositions which not only discloses the financial rewards employees will receive in return for their services to the organisation, but also other non-financial rewards. These include valued reward elements such as developmental training, career opportunities, work-life balance, recognition, and a positive workplace.

1.6 Assumptions

The purpose of this research is to determine how disclosure of executive remuneration fits into and contributes towards an inclusive and effective corporate governance framework, and to seek ways in which disclosure could improve on ineffective corporate governance control measures. The research is therefore both explorative and descriptive.

It is explorative in the sense that a literature survey was conducted into the theory of concepts such as corporate governance, executive remuneration and disclosure, and in particular into the different variables on the formation of an inclusive and effective corporate governance system. Propositions were developed in respect of the different collective and individual factors in a corporate governance framework. It is descriptive in the sense that it describes the difference between corporate governance sub-systems and the focus put on them in different jurisdictions. The research is also potentially predictive in the sense that it exposes directions of how different sub-systems could work together to create an effective corporate governance system in different environmental scenarios. This research depended largely on the interactions with and responses by current business executives and board members. It is a necessary assumption of this research that interviewees were completely honest and open in their responses and that all sources used were completely credible.

The research topic lent itself to mixed methodology in which both qualitative and quantitative analysis would be performed at different junctures. Qualitative research on abstract concepts such as governance and disclosure tend to describe better the ways in which these systems are responsive to particular circumstances or events. Qualitative research is also more likely to emphasize the significance of the situation on the effectiveness of a governance system. Qualitative research is therefore more sensitive to the implications of particular environmental circumstances on the larger system.

Nevertheless there are certain aspects that could be tested by means of a quantitative methodology. In particular, specific disclosure items could be tested and analysed with familiar quantitative methods of analysis. This then formed the basis for sample selection and further qualitative analysis. The study therefore made use of a combination of initial quantitative and later qualitative methodologies to test the propositions described below.

1.7 Chapter Plan

Chapter 1 of the dissertation contains the introduction to the study. It deals with the statement of the research problems, objectives, limitations, definitions and assumptions. It also highlights the contribution of this study to the existing body of knowledge, and the benefits to be achieved through this study.

Chapters 2 to 8 deal with a review of existing literature. Special areas of discussion include executive remuneration, disclosure, and corporate governance, and more specifically the interrelationship of those concepts.

In Chapter 9 research propositions are identified, developed, motivated and discussed.

Chapter 10 deals with the research design for this study, and includes the methodology, data collection and preparation, data analysis techniques, population, sampling frame and sample.

Chapter 11 contains the data analysis and research findings, and the testing of propositions.

In Chapter 12 conclusions and recommendations are made in terms of this study, and the need and areas for further studies is identified.

2. LITERATURE REVIEW

“Theory is where you know everything; practice is where everything works but nobody knows why; here we combine theory and practice: nothing works and nobody knows why.”

- Grint (1997)

Cooper and Schindler (2003) suggest that the first step in exploratory research should be the search of secondary literature generated by other authors for their own purposes, and that such a search should include learning from the relevant methodologies applied by other authors, and from the relevant content of their research results. Secondary data sources provided valuable background and directive information for this research and for the eventual analysis of the data obtained from personal and group interviews. The literature review not only assisted in creating an understanding of the different constructs of corporate governance, executive remuneration and disclosure, but also in understanding the reasons for and extent to which corporate governance control measures have often become inefficient in the modern corporation.

Executive remuneration has become a highly emotive and one of the most contentious aspects of contemporary corporate governance. It is a complex issue that involves infinitely more than merely the levels at which executives are being remunerated. The complexity thereof is especially acute when trying to

correlate the notions of attraction, motivation and retention of scarce executive talent in an increasingly global economy, with principles of good corporate governance.

There is general agreement amongst commentators that executive remuneration, as a key component of corporate governance reform, has been at the forefront of international debate over the last three decades (Mongalo (2007), Hill (2006), and Ferrarini and Moloney (2005)). Szondy (2003) adds that excessive executive remuneration, which has been a general tendency since the 1990's, is fuelling massive investor anger towards executive greed that destroys instead of adds value to organisations and the interests of shareholders. He describes this phenomenon as an unparalleled crisis. These arguments are however based on the popular perception that executive remuneration levels are excessive compared to the salaries paid to ordinary workers, and often without properly considering whether it may be completely in line with their performance. The focus of the executive remuneration debate of late has unfortunately deviated from a principled argument to a sensationalist approach driven by the "how much" fascination of commentators.

Hill (2006) suggests that adequate disclosure of executive remuneration policies and levels was widely recognised as the linchpin in effective regulation of executive remuneration and good corporate governance. Where there is however a clear lack of consensus and commitment, is in relation to the nature and extent of such disclosure, and in the role that disclosure plays in the overall

governance system in the organisation. In support of this contention, Ferrarini and Moloney (2005) argue that the often sharp conflicts of interest between executives and shareholders, and the consequent non-alignment of executive remuneration with performance, highlights the need for increased disclosure and investor activism. This is an insightful observation in that it already predicts the potential of disclosure as a corporate governance control measure to address symptoms of governance failures such as conflicts of interest and the absence of a link between performance and reward. This study tested this observation, amongst others, but also considered how such disclosure interrelates with other corporate governance control measures to create an integrated and effective overall corporate governance system in an organisation.

Handy (2002) justifiably suggests that, in view of the recent corporate collapses and scandals, it might be necessary to reconsider the traditional assumptions relating to the purpose and ownership of a business, to which the answer is no longer clear after modern business developments and reform. Traditional business ownership interests have been replaced by investment interests, which bring into question the assumptions around the protection of owners' interests under popular agency theory, as will be explained in 2.1.1. below. Modern investors, to whom Handy refers as gamblers, often have short-term financial interests which are not necessarily aligned to the long term social responsibility and sustainability of the company. These investors are often only there for the money, and this may not justify the traditional high emphasis being

placed on the protection of their interests above those of other stakeholders, as identified in Annexure A, who may have a more pertinent interest on the long term sustainability of the organisation.

Van Wyk (2009) suggests that the collapse of banks and other financial institutions towards the middle of 2008 showed that corporate failures could not be guarded against effectively, even where boards have complied well with relevant governance codes and legislation. He adds that one of the possible explanations for this is an undue focus on short term profitability rather than long term sustainability. A different explanation is however that current compliance requirements are inadequate to deal with complex business practices, which are often developed by executives to circumvent formal compliance requirements. This is especially relevant where compliance is approached as an item-by-item tick-box exercise rather than holistically, as this research has shown to be common practice in South Africa.

Modern development of the corporation has therefore created a need for further study to address new issues that have shifted the once revolutionary concept of a modern corporation into a new paradigm. Miller and Vaughan (2001) are of the opinion that the study of management history can create a historic perspective that could shape present and future vision and thought, which could in turn assist in the analysis of current issues. Donham (1922) adds that, although no amount of theory could substitute for practical energy, enthusiasm, initiative, creative ability and technical knowledge, it could create a critical

understanding of the underlying principles and forces that impact on business, irrespective of the different environmental forces that may affect individual business or industries differently. For that reason, the literature review sought to provide wide perspectives on the relevant sub-components of the research topic, to contribute to a more holistic understanding not only of those different sub-components, but also in how they potentially interact with each other in an inclusive overall system of corporate governance.

Despite the paucity of literature dealing directly with the role of disclosure of executive remuneration in a good corporate governance framework, there is plentiful literature relating to the different sub-components of this theme, namely executive remuneration, disclosure, and corporate governance, to enable the researcher to analyse the interrelatedness of these concepts.

Becht, *et al.* (2005) argue that, although the extensive literature on executive remuneration and on corporate governance constitutes a useful framework, the direct link between the two concepts is still open to more formal analysis. A clear understanding of the theoretical and historical basis of these concepts, supplemented by a scientific research methodology, will therefore go a long way to explain this relationship.

3. DEVELOPMENT OF THE MODERN CORPORATION

“There is no security on this earth, there is only opportunity.”
- General Douglas MacArthur

Research shows that corporations existed in Europe since the early 17th century, but that these corporations were limited to entities that served the public good (Grand, 2003). In time, business corporations emerged as international traders who traded assets for company stock. The western ideals of capitalism and free enterprise provided the perfect platform for corporate growth, to the extent that almost 80% of workers in the USA were employed in corporations by 1980. In 2007 the world’s largest companies controlled about 33% of the world’s total assets.

This chapter examines how corporations have developed from the primitive public good entities of the 17th century to complex modern organisations serving the interests of many different stakeholders. In particular, it examines how the modern corporation has developed into two rival structures, based on either concentrated or dispersed shareholder structures. This, together with an increased stakeholder base interest in corporations, has led to challenges for stakeholders to protect their interests in these corporations. It is therefore necessary to understand this development, as well as the different interests stakeholders may have in each of these structures, to evaluate the corporate governance needs in each thereof.

Berle and Means (1932) reshaped thinking on the nature of the modern corporation, by identifying the separation of ownership from control as the central characteristic of the modern corporation. They argued that this separation caused agency costs in the process of aligning and controlling conflicting interests between owners and managers. Despite the popularity of their model, which views shareholders as the principals and managers as agents of the corporation, some theorists have recently questioned the accuracy thereof.

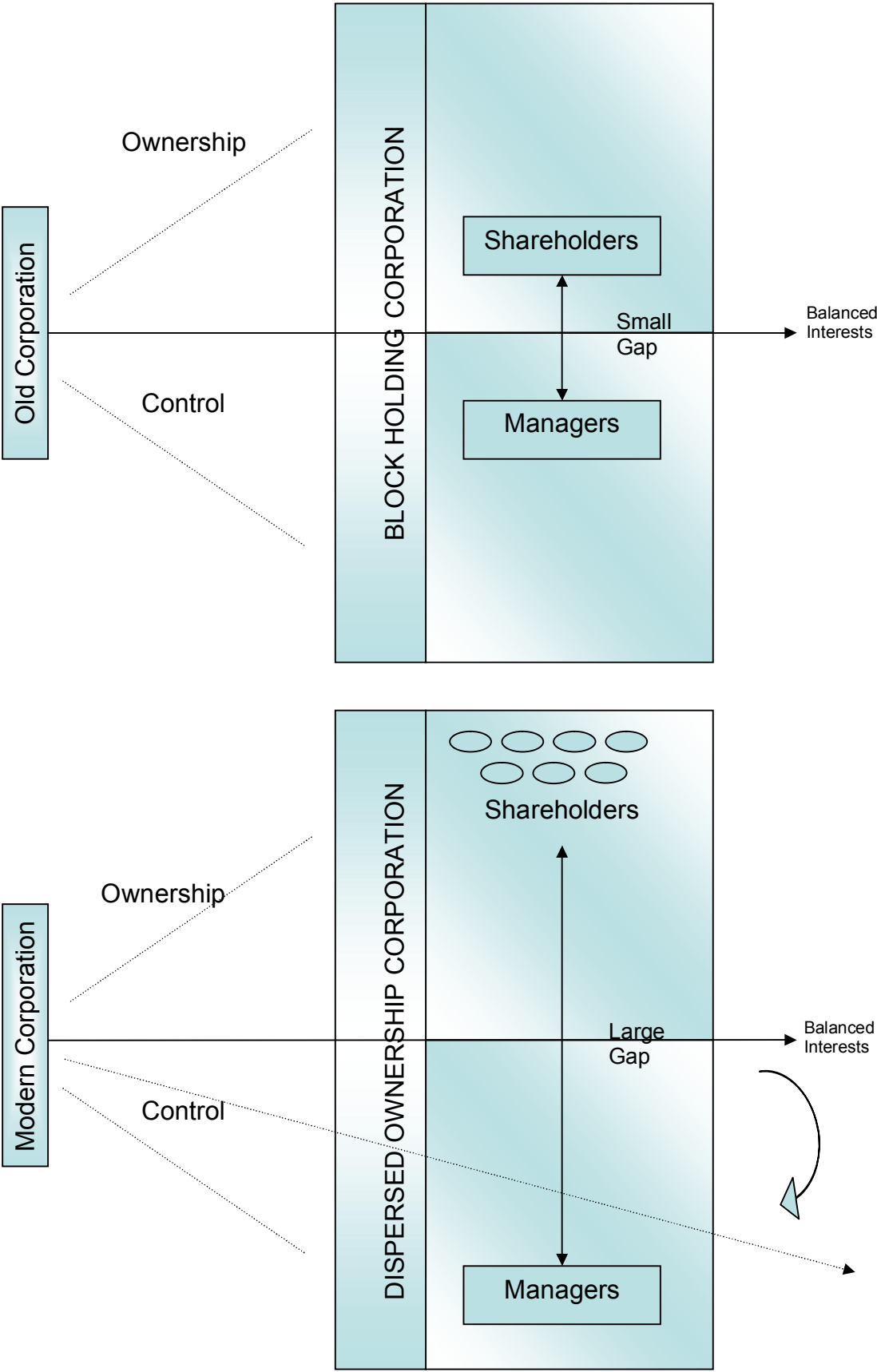
Recent changes in corporate governance and organisational structures have brought into question the very nature of the firm, its purpose and accountability (Bradley, *et al.* 1999). Commentators have increasingly viewed the modern corporation as a complex web of contracts between different stakeholders (Coffee, 1986). Mahoney (1995: 1051) describes a corporate firm as a “web of agency relationships”. Fama and Jensen (1983) see this nexus of unwritten contracts as among owners of factors of production (capital, human resources) and customers. Fama (1980) regards the modern corporation as a system of contracts covering the way inputs are joined to create outputs, and the way receipts from outputs are shared. He adds that ownership of capital should not be confused with or equated to ownership of the corporation, in which each different factor is owned by somebody. This makes exclusive ownership irrelevant.

What seems clear therefore is that corporations have become far more complex over time, and that there is an increased need for corporate governance measures to ensure balance amongst conflicting interests, effective relationship management, adherence to accepted ethical standards, and assurances for the sustainability of the organisation.

While Berle and Means (1932) assumed that all large public corporations would be characterised by a separation of ownership from control, the contemporary empirical evidence is decidedly to the contrary. Instead of a convergence to a single capital structure, the 20th century saw a polarisation of two rival systems of corporate ownership, namely concentrated block holding and dispersed ownership. Figure 1 below demonstrates the differences in the development of dispersed ownership structured corporations and block holding corporations. The central feature of the development is a growing gap between shareholders and managers. In a dispersed ownership structured corporation, the fragmented ownership structure enables managers to become more powerful, and for the balance of interests line to shift towards the managerial side of the corporation.

The question is whether such a dichotomy is sustainable in an increasingly competitive and globalised world. As early as 1776 Adam Smith (in *The Wealth of Nations*) warned of problems with absent ownership in corporations, but Jensen and Meckling (1976) conclude that the phenomenal growth of the modern corporation seems to indicate that investors have generally not been disappointed with their returns, despite increased costs.

Figure 1: The development of the modern corporation



The conflicts of interest in the modern corporation came to the fore in organisations with dispersed ownership structures. Managers in such corporations commonly have considerable discretion in running the affairs of the corporation for their own gain (Salamon and Smith, 1979). This includes, amongst others, manipulation of information, not accounting for their performance, and having strong negotiating power. It therefore provides for potentially significant differences between owner controlled businesses and manager controlled businesses. Rahman (2002) suggests that modern corporations seek to mitigate the adverse effects of this conflict through internal and external corporate governance control measures.

The challenge in an inclusive and effective overall corporate governance system however is for corporations to find the most optimal balance between aspects such as internal and external corporate governance measures, costs and benefits of imposing these measures, and transparency versus protection of privacy.

Coffee (1986) questions whether there is still a need to protect shareholder interests through corporate governance mechanisms in the modern corporation. He argues that shareholders are often protected against risk through their diversified stock portfolios, and that there is a larger stakeholder interest which is not necessarily the same as shareholder interests. The question ought rather to be whether shareholder interests should receive preferential treatment over the interests of other stakeholder groups, whose interests are often closer

related to the long term sustainability of the organisation than that of institutional investor type shareholders.

One of the common characteristics in the modern dispersed ownership corporation is the difference in risk exposure between shareholders with diversified portfolios and managers who have all their risk (mainly human capital) in a single company. The long-standing tendency to identify with shareholder interests on all aspects of corporate governance therefore appears more reflective than thoughtful in the modern corporations.

Dispersed ownership corporate structures, which are still common in Anglo-American societies, are however not as common globally as was assumed by Berle and Means in the 1930's. Many Continental and Asian countries exhibit corporate structures characterised by concentrated shareholding, which are often achieved through large institutional shareholders (e.g. Germany) or networks of cross-ownership (e.g. Japanese Keiretsu). Bradley, *et al.* (1999) suggest that there must be a strong efficiency element in block holding systems that had made it possible for these systems to withstand congruence to a single and universal structure.

Perhaps it is the measure of direct control over managers that is exercised by hands-on owners in these corporations, which reduces information asymmetry between owners and managers, and therefore impacts on the extent of corporate governance control required.

From the above it is clear that traditional corporations have developed in different ways according to environmental, political and social factors. The most fundamental development though relates to the relationship between owners, managers and other stakeholders in the corporation. In order to fully understand these complex relationships it is important not to focus on individual aspects or interests, but to optimize the whole system through an understanding and improvement of the working relationships within the system. A constructive cross reference between the two structures may be meaningful in the raging debate on the possible convergence of corporate governance systems to a globally consistent system.

4. CORPORATE GOVERNANCE

If management is about running a business, governance is about seeing that it is run properly. - Tricker (1984)

Although corporate governance is defined differently across the business and academic world, it ultimately involves the mechanisms by which a business is organised, directed and controlled in a limited liability corporate form, and the mechanisms by which corporate managers are held accountable for corporate conduct and performance. Corporate governance therefore refers to the process and structure used to direct and manage the business affairs of a company towards enhancing business prosperity and corporate accountability, with the ultimate aim of creating long term shareholder wealth, whilst at the same time taking into consideration the interests of all other stakeholders (Abor and Adjasi, 2007). The term “governance” is derived from the Latin *gubernare*, which means to steer or direct an entity. When a person is appointed to steer or direct a corporation, he has a fiduciary duty to the corporation and its owners. The King I and II reports on corporate governance in South Africa identify the basic principles of faith, care, skill and diligence as the guiding corporate governance principles for such a fiduciary duty. Grant (2003) suggests that corporate governance is a broad theory concerned with the alignment of shareholder, manager and stakeholder interests. Corporate governance is therefore essentially about managing relationships and balancing different stakeholder interests.

The global impact of well documented recent corporate collapses and scandals in major corporations across the world, as well as unparalleled executive remuneration increases, have led to the development of many corporate governance initiatives to restore public confidence in corporations (Spanos, 2005; Robins, 2006). The greater public awareness of corporate governance failures created by these scandals has proven to be a significant catalyst for corporate governance reform. The question however remains whether the focus of this reform is on the cause of these problems, or on the symptoms thereof. In order to answer this question, it is necessary to understand the individual and collective impact that different corporate governance control measures, as sub-systems in a larger corporate governance system, have on both the causes and symptoms of corporate failures.

There is an overwhelming acceptance amongst commentators that a lack of corporate governance deters investors. An investor opinion survey by McKinsey and Company in 2002 reveals that investors are prepared to pay a premium for investment in companies with good corporate governance practices. While corporate governance measures are generally already in place in developed countries, it is being increasingly embraced in developing countries because of its ability to impact positively on sustainable growth through investors' goodwill and confidence (Abor and Adjasi, 2007). Despite this however, the prevalence of corporate failures and scandals across the world have shown that the mere existence of good corporate governance codes and practices have not been a guarantee for effective governance. It is therefore necessary to examine the underlying reasons for these failures, in order to address the cause thereof, rather than its symptoms.

One of the complicating factors in analysing literature in respect of corporate governance, executive remuneration and the modern corporation is the different meanings and nuances ascribed to common terms (Turnbull, 1997). Karpoff (2001) adds that this contributes to the inconclusive current research results in these fields. Another complicating factor is that most of the current research relates to English speaking countries, which is not always relevant when differences in culture, business characteristics and socio-political structures are considered. Turnbull (1997) adds that the different models applied to corporate governance perspectives make the construct complex to understand holistically. He identifies these models as:

- The “finance model”, which sees the central problem in corporate governance as the construction of rules and incentives to align behaviour of managers with interests of shareholders.
- The “stewardship model”, which sees managers as stewards of the corporation who diligently work to attain high level of corporate profit and shareholder returns.
- The “stakeholder model”, which sees the firm as a system of stakeholders operating within a larger system, with the purpose of creating wealth for all stakeholders.
- The “political model”, which recognizes that the allocation of corporate power is a function of legal and political frameworks that exist.

No single model on its own is however sufficient to understand and fully explain governance structures. A holistic approach is required. This chapter examines the background and development of corporate governance in modern business, and distinguishes between different corporate governance needs in

organisations with blockholding shareholders and dispersed ownership structures. It also analyses different forms of corporate governance control measures, and how these interrelate in an inclusive overall corporate governance system in an organisation. The chapter also distinguishes between legislated regulation and voluntary codes, as the two distinct forms of corporate governance regulation across the world. It then concludes with an analysis of the most common problems experienced with corporate governance in different environments, and the trends in the development of corporate governance and control measures in different corporate structures and jurisdictions. The aim of this chapter is therefore to understand corporate governance both as a construct and in terms of the development thereof, and to collate and comment on the different scholarly views thereon.

4.1 Background and development of corporate governance in modern business

INTRODUCTION

Although corporate governance is not a new phenomenon in business, focus on it has increased tremendously in recent times as a result of, amongst others, well publicized corporate failures and scandals. Bury and Le Blanc (2007), while accepting that there is no single, commonly accepted definition of corporate governance, describe corporate governance as a complex concept that requires appropriate consideration of the interests of many different stakeholders within a framework that caters for all such interests. Yeoh (2007) defines corporate governance as a set of relationships between a company's board, its

shareholders and other stakeholders, through which the structures for setting and achieving objectives and monitoring of performance are determined.

Corporate governance is therefore not only about board structure and the alignment of conflicted interests, but also about the perceived benefits for the company in attracting and retaining capital. It assumes a mechanism for balancing interests of shareholders with the interests of all other stakeholders, including executives, in the organisation, but also for balancing short term wealth maximization with long term sustainability of the organisation (Conyon and Leech, 1994).

Ney (2007) identifies the following key components of a corporate governance structure:

- protection of shareholder rights to influence corporate strategies;
- the role of non-executive directors to strengthen boards;
- curbing the power of failing executives;
- establishment of internationally accepted accounting standards; and
- greater disclosure of executive remuneration.

The International Corporate Governance Network (2003), (ICGN), which was founded in 1995 to facilitate international dialogue on the development of global corporate governance practices, published a statement of corporate governance criteria that constituted the essential investor consideration of the governance profile of a company. These criteria include:

- an overriding objective to maximize long term returns to shareholders;

- the disclosure of accurate, adequate and timely information to ensure informed investor decisions;
- equal shareholder voting rights;
- fiduciary responsibility and accountability of boards to shareholders;
- alignment of executive remuneration to the interest of shareholders;
- shareholder approval for strategic changes to core business;
- full disclosure of remuneration policy and individualised executive remuneration packages;
- optimization of long term company performance;
- adherence to both the letter and spirit of applicable law; and
- development, application and compliance with voluntary corporate governance codes.

These criteria make it clear that the purpose and justification of modern business is not, as many shareholders might believe, to make money, but rather to generate money as a means to do something more or better. Handy (2002) suggests that whereas in theory, owners understood this purpose, investors simply don't care about it. This underscores an inherent problem with agency theory, namely whether modern shareholders/investors could truly be regarded as the owners of a corporation. If investors are not regarded as owners, it would be more appropriate to require executive actions to be aligned to the long term sustainability of the organisation *per se*, than to dubious shareholder interests. This would certainly eliminate many of the modern difficulties associated with conflicts of interests between executives and shareholders. Dividends could accordingly be paid to both those who invest their capital into the business as well as those who invest their skills.

Epstein and Roy (2005) state that investor surveys have shown that corporate governance has become an important factor for investors. This accords with the results from the McKinsey survey (2002) which found that investors were prepared to pay premiums for well governed companies. Tsamenyi, *et al.* (2007) add that increased globalisation, as well as the impact of major corporate collapses of late, is driving a surging interest in corporate governance in developing countries as well, where good corporate governance practises are viewed as incentives for foreign direct investment.

Rapid globalisation has also brought about some ethical challenges. Whereas there is general acceptance that executives have both a fiduciary duty to act in the best interests of the company and a duty to care, or to exercise the care, diligence and skill that a reasonably prudent person would do in the circumstances, modern developments in corporate governance require those duties against the interest of a wider group of stakeholders than the traditional shareholder group (Bury and LeBlanc, 2007). Traditional shareholder theory, which is still very common in the USA and UK, focuses on value maximization for shareholders, whereas modern stakeholder theory, which is found in, amongst others, Japan and Germany, focuses on wealth maximization for all affected stakeholders of the company. Bhasa (2004) suggests that corporate governance problems only arise when stakeholder rights are violated. This view is however practically problematic, since what is considered a stakeholder right in one country is not necessarily so in another, because of different legal and political structures, and cultures.

AGENCY THEORY

Agency theory, which was mainly developed by virtue of the work of Berle and Means in the 1930's, is based on the assumption that all firms experience a separation between ownership and control which results in agency problems and costs. Roe (2002) however makes the point that it is not the separation between ownership and control that causes the agency problem, but rather the atomisation of ownership that is caused by dispersed ownership structures. He adds that the problem is less acute with large shareholder block controls. La Porta (1999) however, after questioning the empirical validity of the Berle and Means hypothesis, showed that such a separation does not always exist, and that clear differences in this regard exist between ownership structures characterised by dispersed owners versus block holding owners. These two rival structures have been depicted in Figure 1 above. The author explains that traditional dispersed ownership companies, such as are common in the USA and UK, ordinarily focus on external governance systems such as disclosure, while block holding companies, as could be found in Japan and continental Europe, focus on internal governance measures, such as board composition and effectiveness, as they have stronger incentives to monitor executives closely. It is therefore clear that differences in corporate structures impact differently on the nature of corporate governance control measures utilised in those organisations.

The agency problem is an essential element of the contractual view of the firm. The essence of the agency problem is the separation between management and investors (control and ownership). Managers obtain significant

discretionary control over the funds of the corporation, which presents opportunities for self-interested behaviour. One possible solution is to incentivise managers to align their actions to investors' interests. Such incentives however not only generate its own agency costs, but in itself allows for self-interested behaviour by executives. The question could therefore be asked why investors still part with their money when both theory and evidence suggest that managers may serve their own interests above those of shareholders. The answer possibly is to be found in a 2002 McKinsey survey report, which found that investors prefer to invest in companies exhibiting good corporate governance control measures, and that they are prepared to pay a premium for it (Shleifer and Vishny, 1997).

The shortcomings of agency theory led to the development of a broader stakeholder theory in the 1950's (Bhasa, 2004). In terms of this theory, the benefits of the corporation should be extended to all stakeholders affected by it, in a socially responsible manner. Shareholders are viewed as only one category of stakeholders in the corporation. Greiner (1998) explains that many executives hang on to organisational structures and theory, as the source of their power, long after it has served its purpose. This possibly explains the maintained prominence of agency theory in modern business despite its apparent shortcomings. Huczynski (1992), in his study of the development of popular management ideas over the last century and the recurring themes that have been found in the majority of these ideas, presents a possible explanation for the survival of agency theory despite its clear shortcomings, namely its appeal to strongly interested parties. It is accordingly in the interest of investors to be considered as shareholding owners of a corporation, and to enjoy the

superiority of their interest under the agency model, than to diminish those interests under a new stakeholder model. Long term organisational growth requires flexibility, innovation and the development of new structures and theories in accordance with the ever changing business environment. Whereas the agency problem exists between executives and shareholders in dispersed ownership structures, it exists to an extent between majority and minority shareholders in block holding ownership structures (La Porta, 1999; Spanos, 2005).

Despite the prominence of agency theory in corporate governance, Cyert and Hedrick (1972) propose that, even if the primary objective of an organisation is profit maximisation, stakeholder theory is still applicable in that the environment within which a company operates has the potential to significantly impact on the firm due to its social interactions. A company's behaviour is therefore deduced from assumptions describing the environment. The authors suggest that there is still a lack of agreement over whether companies should follow a profit maximization or social responsibility strategy. This translates to uncertainty to which executive behaviour should be incentivised as part of an executive remuneration policy. Abor and Adjasi (2007) ask a fundamental question in this debate, namely what shareholder interest is, and distinguishes between short term profit maximization and long term growth and sustainability. They suggest that the stakeholder approach extends the traditional shareholder approach to a long term corporate social responsibility level.

The ideal therefore of the stakeholder view of an organisation is to mitigate the potential for greed, exploitation and short term profit taking, through emphasis on sustainability, co-operation and long term growth of the business.

INCREASED GLOBALISATION

Despite these different points of view, Spanos (2005) argues that increased globalisation has caused tremendous pressures to converge and harmonize national corporate governance frameworks, while maintaining some degree of flexibility to allow for unique local conditions and culture. Practically such convergence may be difficult to achieve in view of the many different legislative and corporate governance codes in effect in different countries. In the UK for example, there are eleven corporate governance codes, as well as two additional international and a further two pan-European codes with which UK companies are required to comply. These codes are issued by a number of different institutions, which causes some open interpretation on its universal application and status.

The increased levels of corporate governance reforms which have swept the world after prominent corporate collapses, such as Enron, through legislation, governance codes and listing requirements, have contributed significantly to this convergence. Caroati and Rad (2000) identified two corporate governance systems in the world's strongest markets, namely market based (UK, USA) and group based (Japan, Europe). The market based system focuses strongly on shareholder interests and competitive markets, while government involvement

is at a low level. In contrast, the group based system focuses less on shareholders, and allows for the government to direct the economy through different policies. They also identified two possible ways in which corporate governance systems could converge, namely convergence of corporate rules and convergence of business practices. They conclude that, in order to converge:

- There should be marginal improvement in board effectiveness in a market based system; and
- There should be radical changes in both the regulatory environment and ownership structure in a group based system.

Corporate governance focus and reforms of late, have led to increased activism by institutional investors, which have, amongst others led to rejections of executive remuneration proposals in, amongst others, Australia. Despite this increased investor activism, Drucker (1987) is of the opinion that managers' interests have developed into proprietary rights against the organisation, which is comparable to owners' positions in traditional business enterprises. These rights however need to be structured in terms of objective performance standards and independent performance appraisals. The development of executive interests into proprietary rights is still nebulous and in a state of constant change, which has allowed executives to take advantage of personal wealth-creating opportunities.

4.2 *Forms of corporate governance measures*

Corporate governance control measures are put in place to counter the incompleteness of contracts between owners and managers. These control measures can be internal or external in nature (Rahman, 2002).

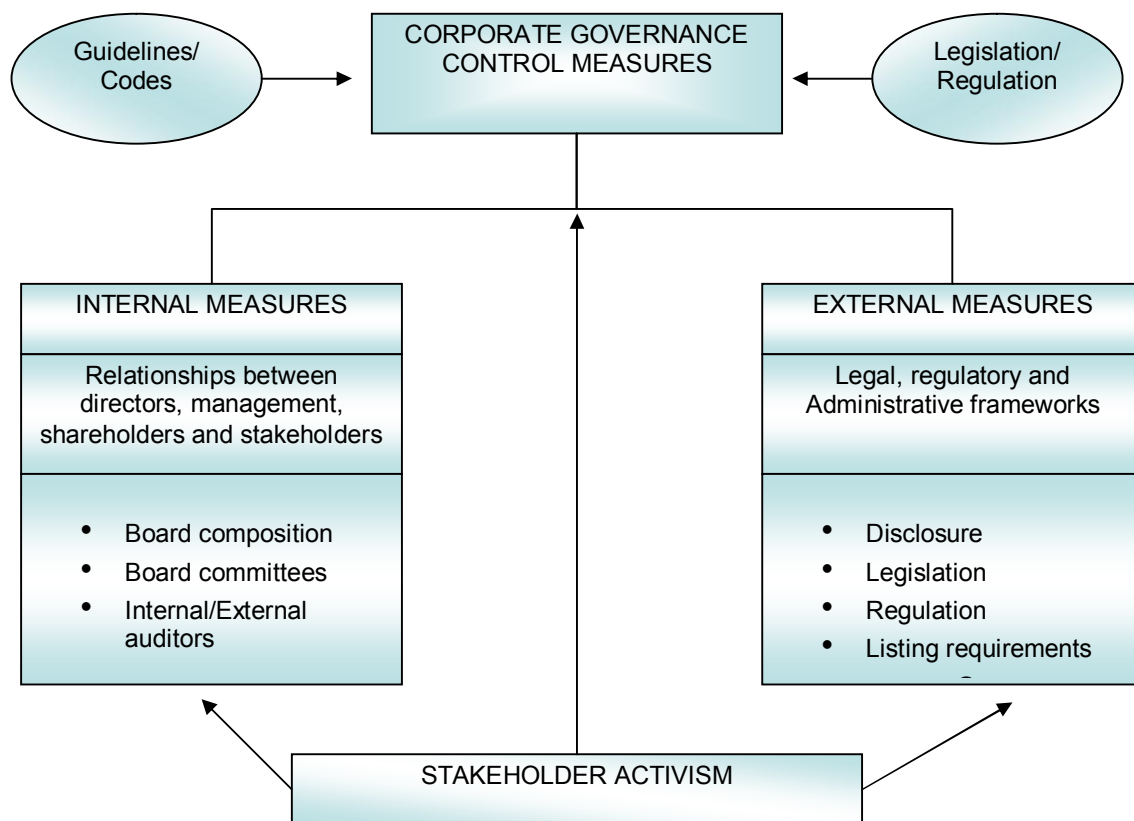
Some of the biggest global challenges to a convergent system of corporate governance best practise, are the differences in legal, political and cultural systems in different countries (Bhasa, 2004). Black and Coffee (1994) question, in view of possible signs of such a conversion, whether systems would converge closer to a system based on internal or external measures. Shim (2006) suggests that the primary corporate governance mechanisms to be found in different countries could be classified into two separate components, namely internal measures (the relationship between directors, management, shareholders and stakeholders), and external measures (legal, regulatory and administrative frameworks). Bhasa (2004) makes a similar distinction under the terms insider and outsider mechanisms.

Chambers (2005) suggests that, irrespective of the form of corporate governance measures implemented, compliance and agency costs are increased for the organisation. What seems clear therefore is that different situations may call for a different combination of corporate governance control measures. Aspects such as the regulatory, economic and social environment, as well as the nature of the corporate structure, will influence the optimal mix of governance control measures. It is for companies to develop the most effective combination of control measures in their own respective situations and frameworks, but to remain true to the underlying principle of protecting the

interests of their stakeholders through an effective corporate governance framework, and the control measures therein. The selection or design of control measures may be different for different companies, but the ultimate aim thereof ought to be the same.

Figure 2 below sets out how corporate governance control measures are shaped by legislation, regulation, codes and guidelines to materialise in internal and external measures, which are in turn impacted upon by activism.

Figure 2: Corporate governance control measures



(Adapted from Shim, 2006)

Gadfly and Smacker (2010:336) describe a system as “*any structure or process consisting of two or more interactive elements, created for the purpose of realising specific objectives*”. They add that it is important to understand the following characteristics of a system for the system to function effectively:

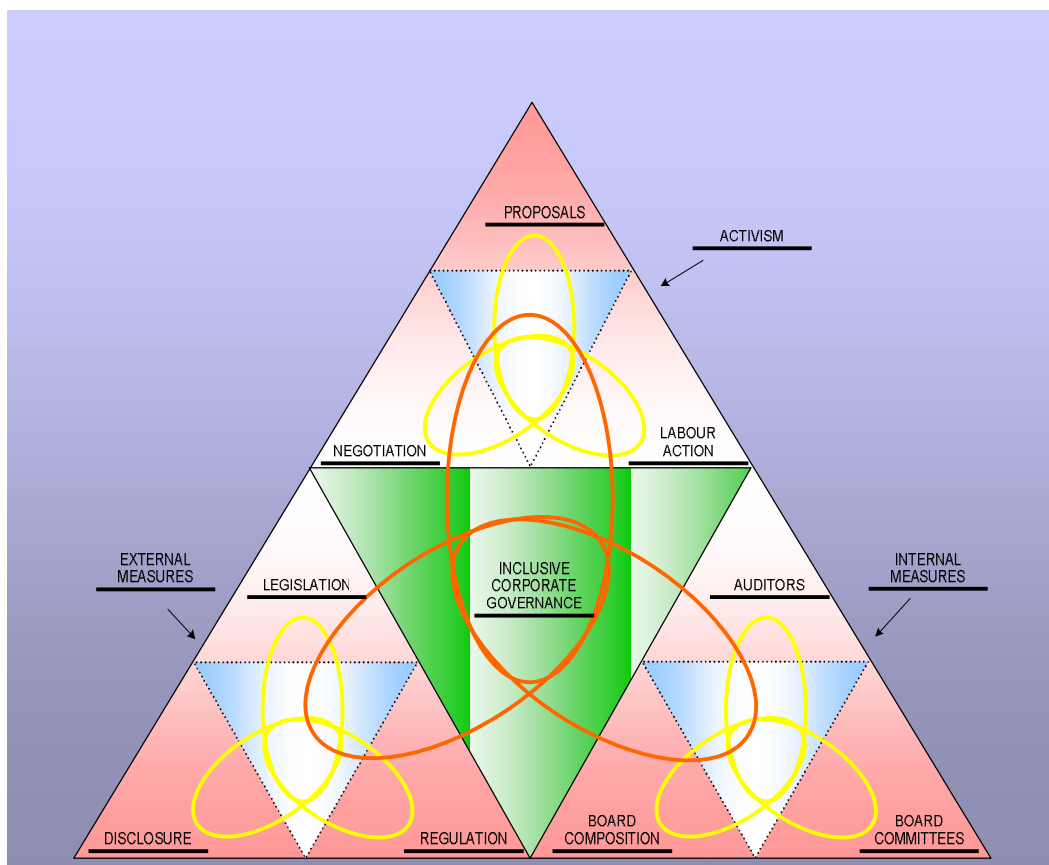
- The performance of the system is not equal to the sum of the performances of its sub-systems, but rather the total product of the interactions of all of the sub-systems;
- An effective system requires facilitation of the interactions of its sub-systems, rather than controlling each individual sub-system;
- A process view of changes in the system is required, rather than a snapshot view thereof;
- A system consists of sub-systems and sub-sub-systems depending on the complexity thereof; and
- In open systems, the desired end state may be achieved in a number of different ways.

These characteristics of basic systems can be applied to corporate governance, as they are open systems. Figure 3 below sets out an inclusive or systems view of corporate governance, which shows how corporate governance control measures interact with each other to form a total corporate governance framework and system within an organisation.

The systemic problem identified as a basis for this study was that corporate governance control measures have become ineffective due to the development of the modern corporation. This requires a consideration of the interrelatedness

of different sub-systems rather than the total corporate governance system as a whole. Capra (1990) summarises aptly that the complex systemic problems of our time cannot be understood in isolation, but require an awareness of the interrelatedness and interdependence of all phenomena that form part of the system. In addition to understanding the interrelatedness of different components of the system, it is however also necessary to understand the underlying causes of the problem. Wheatley (2010) therefore suggests that our very survival depends on us becoming better systems thinkers.

Figure 3: Systems view of corporate governance



An inclusive corporate governance system as developed in Figure 3 above not only consists of interrelationships between internal measures, external measures and activism, but also of interrelationships of sub-sub-systems within

each of those control sub-systems. Under the external measures these sub-systems include legislation, regulation and disclosure. The internal measures include board composition, board committees and auditors. Activism includes negotiation, proposals and labour action. As a result of the frequency in which Figure 3 is utilized, it has been reproduced as Annexure B.

It was necessary for this research to gain different insights and interpretations of the sub-systems within the overall governance system depicted in Figure 3 above, in order to understand the whole governance system better. Wheatley (2010) suggests that the more interpretations on these sub-systems are gathered and considered, the easier it becomes to gain a sense of the whole system. The interpretations from both the literature review phase of the research, as well as from the interviews, assist in this regard.

4.2.1 Internal measures

Internal measures of corporate governance refer to the relationships between directors, management, shareholders and stakeholders in an organisation. In a principal-agent environment there is always inherent potential for conflicts of interest as a result of the different economic interests of different groups. Mardjono (2005) suggests that most studies of corporate governance practices focus on the different roles of an executive director and non-executive director, board independence, the role of board committees and of internal auditors, to identify the underlying values of good corporate governance. These values include accountability, integrity, efficiency and transparency. Mardjono (2005) concluded that there is still no consensus on the role that corporate governance plays to ensure sustainable business success, but ascribes corporate

governance failures to either a lack of corporate governance frameworks and practices, or implementation thereof.

Ferrarini, *et al.* (2003) state that two mechanisms have been developed in Anglo-American corporate governance models to reduce the risk of the board's capture by self-serving executives, namely the appointment of independent directors, and the composition of remuneration committees with non-executive directors. They argue that these measures are increasingly finding a way into many European corporate governance systems, albeit not in the originally intended forms.

Chambers (2005) however questions the contribution made by non-executive directors to good corporate governance, and ultimately to the creation of value for the shareholders of an organisation. He concludes that where there is a smaller chance of a company to collapse because of the mere existence of non-executive directors in the company, then these non-executive directors add value to the organisation. Chambers (2005) refers to consistent research results produced between 1997 and 2000 by Henley Management College, which could not find a relationship between the existence of non-executive directors in an organisation and improved corporate performance, in support of the conclusion that the contribution by non-executive directors is questionable.

Chong (2004) questions the independence of non-executive directors, by referring to the preferential appointment processes followed by many boards, who appoint friends and associates to such positions. This has the potential of increasing risk and agency costs to such an extent that it would be costly for

shareholders to implement internal corporate governance measures to protect their interests. Unfortunately there are plentiful examples in practice that indicate that non-executive directors are not as independent as they are intended to be.

Although there is certainly a compelling case to be made for the existence of internal control measures in a larger corporate governance system, the effectiveness of these control measures lie in the manner in which these are implemented in accordance with the underlying principles that informed their development in the first place. An “independent non-executive director” who is not truly independent or truly non-executive causes this control measure to be ineffective. The same applies to the composition of a board, where its members are not sufficiently experienced, qualified, diversified and engaged in the execution of their duties. It is therefore often not the mechanism itself which is defective, but the application thereof. Companies therefore ought to spend time and effort on focusing these control measures strategically, rather than merely to create the existence of a governance body, which is often without the necessary teeth.

REMUNERATION COMMITTEES

The use of remuneration committees, composed of non-executive directors, are according to Hill (2006) a clear procedural improvement in the conflicted executive pay-setting process, but not the complete answer to the problems that generally occur in this process. Nonetheless, Ferrarini and Moloney (2005) report that the use of remuneration committees composed of only independent

non-executive directors are on the rise throughout EU countries. These remuneration committees determine executive remuneration policy and levels in terms of sophisticated “comply or explain” rules contained in voluntary codes to which companies are not directly bound, unless the code is copied into specific listing requirements. Given that the executive remuneration problem is more acute in companies characterised by the dispersed ownership structures, as a result of agency cost, there is a possible inference of a direct correlation between the regulatory approaches and company structure. The authors report an inconsistent trend towards convergence towards the Anglo-American model of full disclosure, which could in their view improve the currently low level of shareholder activism in the executive pay-setting processes of EU companies.

The Myburgh report on the collapse of Regal Treasury Private Bank in South Africa stated that the relevant non-executive directors may as well have played bowls for all the energy they put into the discharge of their duties. Mongalo (2007) supports the view that non-executive directors and remuneration committees have been ineffective in curbing excessive executive remuneration. He ascribes this firstly to the general practise of remuneration committees to benchmark executive remuneration in their companies directly to the levels of executive remuneration published in respect of other companies, without any clear reference to the achievement of performance objectives. Secondly, most remuneration committees rely on the advice of remuneration consultants who act for multiple companies, which brings their objectivity into question. The reputation of known consultants for being either liberal or conservative in their advice also has a potential manipulative influence on their appointment to be of service to the board. Consultants are furthermore known to market their

services in the most appealing fashion, and would do almost anything to secure appointment as service providers. Thirdly, the objectivity and independence of non-executive directors, who are often executive directors in other companies, is questionable. None of these problems would however materialise where such directors are truly independent, non-executive, and appropriately qualified to perform the required duties at that level. If they are independent, knowledgeable and assertive enough, they should not be susceptible to undue influences or bad advice.

Lowenstein (2000) makes the point strongly that captured boards cannot negotiate at arms length, which often leads to shareholders either selling their stock, refusing to invest further, or engaging in activism and private negotiations. Shleifer and Vishny (1997) add that boards do not necessarily represent shareholders' interests – even where board members are elected by the same shareholders. Byrne (2002) however suggests that it is not enough to hold only the board accountable for its actions, but those shareholders should also be responsible for monitoring the board closely and managers should act as a moral compass for the company. He uses the example of the collapse of Enron to show that there has rarely been such managerial deception, but similarly such an asleep board and shareholders.

Although most corporate governance codes encourage executive directors to hold non-executive directorships in other companies to the extent that it does not interfere with their management responsibilities, this *caveat* is often ignored. Non-executive directors are well aware that their recommendations in a company where they hold non-executive directorships may directly impact on

their positions as executive directors in other companies. In South Africa, the King II Report however requires that non-executive directors should be free from any business or other relationship which could be seen to materially interfere with the individual's capacity to act in an independent manner.

Shleifer and Vishny (1997) analyse the differences in board composition between USA and UK dispersed ownership companies on the one side, and Japanese and German block holding companies on the other, and comes to the conclusion that a combination of legal protection (common in USA and UK companies) and large investor control (common in Japanese and German companies) is essential for a good corporate governance system. Roe (1993) suggests that the differences in corporate structures between USA/UK firms and Japanese/German firms are not only attributable to economic factors, but also to social, political and cultural factors. The faceless relationships in a dispersed ownership structure, as opposed to the personified relationships in block holding structures, cause power in the firm to shift from shareholders to managers. It is in this environment where we have seen a prevalence of corporate governance failures which could be attributed to abuse of power by conflicted executives. In most of these failures however, there were state of the art corporate governance control measures, and the compliance rates were high, but the principled application thereof significantly lacking.

4.2.2 External measures

External measures relate to the legal, regulatory and administrative frameworks designed to ensure good corporate governance practices. These include

measures such as legislative requirements, listing requirements, and guidelines contained in corporate governance codes. One of the most prevalent such measures relates to the disclosure of executive remuneration.

Ferrarini, *et al.* (2003) advises that executive remuneration regulations in most EU countries focus on disclosure, as well as corporate governance structures and procedures as measures to ensure good corporate governance. This view is confirmed by Ferrarini and Moloney (2005), when they state that disclosure is central to the effectiveness of executive incentives in that it has the potential to reduce agency costs without severe interventions, which could distort competition, flexibility and economic contexts.

The most significant benefit of external measures such as disclosure is that it may lead to informed shareholder, investor, and public activism that may even cause companies to change remuneration practices when it is perceived to be unjustified or inconsistent with shareholder returns. Allens Arthur Robinson (2007) lists some of the reasons for such pressure as follows:

- a lack of transparency of remuneration costs;
- excessive directors' bonuses;
- increases in executive remuneration at a time of declining corporate performance;
- unapproved ex gratia payments to executives;
- incentive schemes allowing for immediate exercise of options;
- inconsistent performance objectives;
- stock option re-pricing, and other downside protection; and
- excessive termination payouts and "golden parachute" clauses.

A central puzzle however in understanding governance in modern corporations is why shareholders remain passive despite clear governance failures (Black and Coffee, 1994). Under the Berle-Means paradigm this passivity was considered to be an inevitable result of the scale of modern industrial enterprise and fractional ownership. A paradigm shift however seems in the making, as the Berle-Means thesis that shareholder dispersion implies weak oversight over management has long received sceptical reception from especially UK academics. There is a general observation that governance developments in the UK could be seen as a predictor of possible developments in the USA. In this, there is an important lesson for the USA, namely to reduce regulatory controls to increase shareholder activism and other measures. It seems that at least one of the reasons for the development of the King III Code of Governance in South Africa in 2009, namely to reduce the potential strictness of the draft Companies Act, set to come into operation in South Africa in 2011, shares this insight.

4.2.3 Shareholder activism

A control tenet of shareholder activism holds that it ameliorates shareholder-manager agency conflict (Karpoff, *et al.*, 1996). Karpoff (2001) adds that shareholder activism appears in two forms, namely proposals at meetings and private negotiations, but that empirical research has shown that both forms only prompt small changes that have negligible impacts on corporate earnings, impair management, decrease value and focus management more on the issues raised.

Notwithstanding the increase in shareholder activism since the 1980's and a general positive assessment thereof by commentators, empirical research indicate that such activism has little or no effect on performance, despite a common belief that it would replicate the benefits of block holding ownership, by filling the void in managerial monitoring. In contrast to the lack of success of shareholder activist proposals, private negotiations have shown to have short-term benefits. The types of board and compensation reform proposals that have come from activists have however not been found to be value-enhancing corporate governance devices (Romano, 2000; Romano 2001).

Gillian and Starks (1998) therefore ask whether shareholder activism has had any positive impact on corporate decision making and performance. They view activism as an integral part of corporate governance control measures, but concede that it is difficult to measure both the level of activism and the impact thereof. They conclude that shareholder activism is still and especially important where boards fail to protect shareholder interests.

One possible explanation for the lack of success of activism as a governance control measure may be the lack of the quality and timeousness of information upon which informed activism could take place. It stands to reason that fully informed activists would without doubt be far better equipped to protect their interests than uninformed or ill informed ones. Equal access to relevant information to stakeholder activists would elevate their impact above the current noise levels. Effective disclosure could be one of the mechanisms to facilitate better activism, and creates the potential for interaction between different corporate governance control measures in an inclusive governance system.

4.3 Corporate governance regulations

The good of the people is the chief law. - Cicero

Compliance with both statutory regulations and voluntary codes of corporate governance has become the norm for listed companies all over the world (Abor and Adjasi, 2007). The corporate governance codes and regulation practised in the USA and UK are held in high regard across the world for its thoroughness, greater transparency frameworks, and ability to secure a closer alignment of conflicts of interest between shareholders and executives (Yeoh, 2007). The USA response to corporate collapses in particular, which collapses have caused a worldwide loss of investor confidence and trust in modern corporations, was according to Robins (2006) mainly legislative in nature. The promulgation of the Sarbanes-Oxley Act of 2002 in the USA, which increased listing requirements that have to be met by public companies, is one prime example hereof, as was the statutory capping of executive remuneration levels in the USA in 2009, where companies received state assistance to survive the global financial crisis of the time.

Despite a significant increase in new legislative regulation and voluntary codes of good corporate governance worldwide, Robins (2006) is of the opinion that it would not necessarily result in better compliance. He adds that the most important challenges in this regard are the increased compliance costs associated with the new requirements, and the frailty of human nature to fully comply with regulatory codes. As long ago as the 18th century Adam Smith foresaw the possibility that businesses and business executives would do

inconceivably wrong things, where he states that “*the want of proper indignation is a most essential deficit in the manly character*” (Smith, 2000).

In the same way as a proliferation of corporate governance control measures would not automatically result in better governance, a proliferation of strict legislative and regulatory requirements would not *per se* result in better governance. There must still be an understanding of the underlying principles these prescripts or control measures seek to achieve, and an informed and focused application thereof, to be effective. What is required is not necessarily more regulation or more control measures, but rather better application of those that already exist. This does not however mean that there ought not to be regulatory reform to adapt to changing environments. The one is not a substitute for the other.

4.3.1 Legislative regulation

The Sarbanes-Oxley Act of 2002, which was enacted in the USA in response to the Enron collapse, is widely touted as the single most important piece of legislation affecting corporate governance and financial disclosure (Szondy, 2003). The Act made life more difficult for executives all over the world as its impact on the global economy spreads fast and wide. Collier (2004) adds that the Sarbanes-Oxley Act in the USA, and the UK Listing Rules (which incorporates the UK Combined Code), provide most of the detailed disclosure and executive remuneration rules to be found in the world today. The author adds that companies that operate under either of these have their performance scrutinised more than ever before.

Robins (2006) however warns against too strict or too much regulation in the field of corporate governance, which may cause companies to comply with the letter of the law rather than the spirit thereof. Such compliance would be less effective in a field where ethics and human behaviour have a significant role to play. The King II Report in South Africa makes the point very eloquently that it is not possible to legislate against ethics failures. Styan (2009) quotes professor Gill Marcus's criticism of the practice of regulating corporate governance through legislation, by suggesting that legislation often focuses on what is said by companies rather than what is actually done by them. This could be compared to the shift in focus, in amongst others the King III Code of Corporate Governance, from a "comply or explain" culture to one which could be described as "apply or explain". Abor and Adjasi (2007) reiterate the point that strict legislative regulation of corporate governance may undermine the competitive advantage of firms that exists in their creativity and innovation. Legislative regulation of corporate governance therefore has the potential to destroy the value created through corporate entrepreneurship, and may jeopardise innovation and creativity associated with taking risks. On the other hand, Robins (2006) suggests that prescriptive rules may provide important guidelines for good corporate governance, but cannot by itself raise standards of compliance or performance. The debate around governance should therefore move beyond the checklist debate, to rather address executive deception and negligence.

4.3.2 Guidelines contained in voluntary codes

Bhasa (2004) suggests that most corporate governance codes are offshoots from the 1992 Cadbury Committee Report in the UK. Annexure C hereto

highlights some to the most prominent of these codes. In South Africa, the King Committee on Corporate Governance was formed in 1992 to consider corporate governance in the context of South Africa. Its purpose was to promote the highest standards of corporate governance in South Africa. The publication of the King Report on Corporate Governance in November 1994 (King I Report) institutionalized corporate governance in South Africa. The King I Report went beyond the financial and regulatory aspects of corporate governance, by advocating an integrated approach to good governance through fundamental principles of good financial, social, ethical and environmental practice (so-called triple bottom line).

The King I Report emphasized the need to distinguish between accountability (liability to render an account) and responsibility (liability to be called to account). It further developed seven characteristics of good corporate governance, namely:

- Discipline: Commitment to adhere to behaviour that is universally recognized and accepted to be correct and proper.
- Transparency: The measure of making necessary information available publicly, candidly, accurately and timely.
- Independence: Extent of mechanisms to minimize or avoid potential conflicts of interest.
- Accountability: Effective mechanisms to allow responsible parties to render an account for their actions.

- Responsibility: Behaviour that allows for members to be called to account.
- Fairness: Taking into account all those who have an interest in the company and its future.
- Social responsibility: Non-discriminatory, non-exploitative and responsible treatment of environmental and human rights issues.

As a result of many political, legislative and business developments since 1994, the King Committee reviewed corporate governance standards and practices in South Africa, under the following four guiding principles:

- To review the King I Report for currency against local and international developments;
- To review the proposed “inclusive approach” for sustainable success of companies;
- To recognize increasing importance of non-financial issues, and triple bottom line (economic, environmental and social aspects) reporting thereon; and
- To recommend how the success of companies can be measured through the “balanced scorecard” approach for reporting.

The King Report on Corporate Governance 2002 (King II Report) was therefore published in March 2002, and advocates the principles of openness, integrity and accountability as the pillars upon which corporate governance practices should be built. Although the King II Report does not have the power of statute,

it sets out a set of guidelines to which listed companies are bound by virtue of the listing requirements on the JSE, and private companies are encouraged to adhere to. South African listed companies are expected to comply with the corporate governance guidelines set out in the King II Report, by virtue of JSE listing requirements and the Companies Act, or explain its failure to do so. A “comply or explain” regime therefore also applied in South Africa under King II. The King III Code, which became effective in South Africa in March 2010, addresses changes that occurred in the legislative and economic environments in South Africa since the publication of the King II Report. King III might well become the blueprint for corporate governance practices in South Africa over the next few years.

The most important feature of the guidelines contained in these codes, is that it is nothing more than mere guidelines. The adherence thereto or not by companies is voluntary. Failures to adhere to these codes do not carry penalties. The position is however different when the guidelines contained in codes are incorporated into formal listing requirements to which companies are strictly bound. Voluntary codes require a strong measure of self-regulation as a means to adhere to both the letter and spirit of the law (Shim, 2006). Legislatures ordinarily prescribe minimum standards of compliance (“letter of the law”), whereas voluntary codes set out best practise guidelines (“spirit of the law”). Together these two elements lead to a higher standard of corporate governance in an organisation, which is not about box ticking, but rather a mindset of conscious compliance with best practice. Judin (2007) suggests that, in view of the imminent enactment of the new Companies’ Act in South Africa (for which there is already a published draft Companies’ Law Amendment Bill),

the time was appropriate for the King II Report to be supplemented and updated, to cover for “spirit of the law” developments required in response to the “letter of the law” prescripts of the new legislation. Viewed in this way, the success of the King II Report in South Africa underscores the theory that success is a journey rather than a destination. With King III, the journey in South Africa will continue as corporate South Africa gets to grip with an as yet incomplete set of corporate governance rules. Shim (2006) aptly describes this as “substance over form”. It is however no easy task to achieve a mindset of conscious and voluntary compliance with codes in an environment characterised by different self-serving interests. Drucker (1985) is of the opinion that habits are hard to break, even if it leads to setbacks, corporate collapses and scandal. Business executives who are let down by their conflicted and self-interested habits will rather look for any other excuse but to admit to their own bad habits. Huczynski (1992) suggests that it is possible to change peoples’ behaviour by incorporating such features into a new idea that would make the acceptance thereof more appealing to the individuals. Effective leadership, proper incentives and good communication are therefore the most effective tools to guide this complex process.

Sethi and Emelianova (2006), after comparing voluntary codes with strict legislation, conclude that industry groups prefer voluntary codes that allow for more individual flexibility above strict regulations by means of legislation. The authors however point out the following problems experienced in respect of voluntary codes:

- many companies view adherence to voluntary codes as giving in to the critics of industry;

- it is inherently difficult to find common grounds in a competitive environment;
- voluntary codes are often incompatible with a company's operational and financial strategies, as well as its culture;
- adherence to voluntary codes generate short term costs that have to be recovered through related productivity improvements; and
- agency costs overwhelmingly emphasize the short term character of earnings.

Shim (2006) observes that in most countries where there are voluntary, self-regulatory codes of corporate governance, compliance with the disclosure provisions contained therein are usually made mandatory under specific listing requirements for public companies listed on a particular stock exchange. This is certainly also the case in South Africa for companies listed on the JSE.

Sethi and Emelianova (2006) add that voluntary corporate governance codes in a way require a promise and a commitment by companies to certain standards of conduct, which has the purpose of improving the underlying problems related to corporate governance practices, in the interest of all shareholders. The success however of such a system relies on its ability to create and maintain public credibility, which is difficult in an environment built upon inherent competition. In this competitive environment it is necessary for such codes to include some enforcement measures which could address free rider and adverse selection problems associated with adverse industry perception as a result of some poor performance, which in turn benefit from the level of public approval of a well governed industry. Treanor (2007) highlights an interesting

inconsistency in the applicability of voluntary corporate governance in an increasingly global economy. Currently only companies domiciled within the UK are obliged to comply with the UK Combined Code, which has been incorporated into formal listing requirements (Treanor, 2007). The author argues that the same requirement should hold in respect of foreign businesses which operate within the UK. These plausible principles could be drawn to the arguments for greater convergence of governance systems in the global economy. It is however more feasible to believe that convergence would only be material at a philosophical or principle level, rather than in terms of specific regulatory prescripts or control measure mixes.

Sethi and Emelianova (2006), after analysis of a number of industry-based codes of conduct, come to the conclusion that most such codes have failed to engender public trust in the conduct of companies. They therefore developed a set of conditions that have to be met to reduce the gap between stakeholder expectations and company performance. These include:

- some forward-looking industry leaders who could take the lead in the adoption of a code;
- the addressing of issues of wider concern than just for some companies;
- a governance structure that allows for balanced representation and independent, external input;
- institutionalised compliance with codes throughout the company;
- independent, external monitoring of compliance with the code; and
- uncensored public disclosure of compliance with the code.

Events around the world have shown that codes of corporate governance function better as guidelines for voluntary adherence because of the fact that environmental differences make it impossible to design a one-size-fits-all solution. In the end it is more important to focus on governance principles and the quality of corporate governance control measures, rather than viewing governance as a quantitative tick-box exercise.

4.4 Problems associated with corporate governance

This study departed from the assumption that corporate governance control measures are inadequate to deal with problems experienced in the modern corporation. It is however trite that major differences appear from the control measures applied across the world, which together with legal, institutional, social and cultural differences, make it difficult to compare corporate governance systems in the process of searching for the optimally efficient system (Romano, 1993). Valuable lessons can nevertheless be drawn from differences in these different systems.

Economic theory has long recognised that where there is a separation of ownership from control, a potential conflict of interests exists between owners and managers. Gugler, Meuller and Yurkoglu (2003) report that agency problems exist in any country, but that it appears weaker in developing countries than in developed countries. This agency problem is exacerbated in public corporations where dispersed owners are seldom sufficiently incentivised to monitor management's actions and to reduce agency costs. Yablon (1992) suggests that the answer to this problem should be sought within the field of

managerial science, rather than through legislative regulation, which should only become relevant when executives abuse their powers for own benefit. Moxey (2004) proposes that large shareholder concentration, take-overs, proxy voting, effective board control, incentivised alignment of interests, and clearly defined fiduciary duties could be used to address these conflicts of interest.

The Enron situation challenges some of the core beliefs and practices that underpinned corporate governance thinking. Gordon (2002) suggests that it raises at least the following issues:

- The questionable strength of the market mechanism to ensure business success;
- The undermining of monitoring boards as governance mechanisms;
- Trade-offs in the use of stock options to compensate for risk; and
- A poor fit between stock-based compensation and retirement benefits.

Chingos (2004) highlight two significant corporate governance responses to the collapse of Enron, namely legislation (such as Sarbanes-Oxley) and strict listing requirements which incorporate voluntary codes of compliance in most instances. The subsequent increased focus on corporate governance has put directors in the spotlight, and has made their jobs more risky and demanding. Senge (2006) avers that the current economic and political systems have resulted in firms being irresponsible and unsustainable, by not holding them accountable for their negative impacts on society. Global response to this problem, through corporate governance reform, has however not been uniform.

According to WorldatWork (2007) the typical modern corporate governance model has three dimensions, namely:

- Accountability: Who is accountable for what results and policies?
- Alignment: Goals and strategy must be clear, and must deliver value.
- Accuracy: Corporate governance control measures must support decision making.

Stabile (2000) proposes that if boards cannot be relied upon to negotiate vigorously on shareholders' behalf, shareholders will increasingly become more active to protect their own interests. The question is how to enable shareholders to protect their interests optimally. An integrated approach to corporate governance may provide a workable solution in this regard. This study focuses especially on the role of disclosure of executive remuneration, as one of the corporate governance control measures in such a framework, in enhancing this ideal.

4.5 Corporate governance trends

Allio (2003) refers to Einstein who believed that it would not be possible to solve the problems created by current patterns of thought without first changing those thought patterns. This belief could be applied to popular theory that the separation of ownership and control in the modern organisation leads to conflicts of interest between shareholders, who are believed to be the owners of the modern corporation, and executives. The author adds that most current

managers lack the skills and knowledge required to shift to a new paradigm that could address governance complexities in modern corporations. He is of the opinion that executives rather tend to reduce complex issues to simple ones, for which they seek simple solutions. One such simple solution could be the use of share price alone as a measure of company performance and value creation, instead of multi-dimensional factors such as those contained in the balanced scorecard. This results in managerial misunderstanding of business and the environment within which it operates.

Drucker (1985) reports that many managers instinctively opt for a “fastest with the mostest” entrepreneurial strategy, which he considers to be highly risky. The fundamental question that ought to be asked is what the dominant interest should be in a business – short term maximization of returns, or long term social structure and sustainability. Too often shareholders are no more than short term investors who are only in it to make as much money as possible in the quickest time (“fastest with the mostest”). Other stakeholders in the same business, such as for example employees and local communities, often have a direct interest in the long term sustainability of the organisation. It is therefore essential for companies to understand the different interests of their diverse stakeholders, and to ensure a fair and equitable balance between those different interests.

Traditional theory seems to suggest that all other business interests should be aligned to shareholder interests – even if they are not beneficial to the long run sustainability of the organisation. This is clearly an unintended and flawed consequence of traditional agency theory, and may be out of touch with modern reality.

According to Shim (2006) increased globalisation and the current prominence of corporate governance reform in leading countries will inevitably cause most countries and governance systems to converge to a fairly similar framework for governance practices, which allow some measure of flexibility to allow for environmental difference. There is however no consensus on whether any particular corporate governance system enjoys significant advantage over the other, to compel convergence towards it. Coffee (2001) suggests that informal convergence usually takes place before formal regulatory measures are implemented. He adds that one of the most important reasons for the great level of convergence across Europe was the central currency and trade arrangements within the European Union. Bergloff and Pajuste (2005) add that the corporate governance challenges facing Central and Eastern Europe were similar to those faced in many other emerging economies, and will eventually facilitate a greater level of convergence to a similar global corporate governance system. It seems quite feasible that such operational convergence would escalate once there is a significant convergence on a conceptual and principle level.

There has been widespread and significant global corporate governance reform of late, in the form of new corporate governance codes, regulations and legislation. Typically these reforms set out either voluntary codes or mandatory rules in a regulatory context, which are often formalised through listing requirements for public companies. The increased focus on corporate governance since the 1990's has led to influential reports such as Cadbury (1992), Greenbury (1995) and Hampel (1998), which still form the basis for many such codes across the world (Canyon and Murphy, 2000). These reports

outline, amongst others, a best practice framework for setting executive remuneration and expanded disclosure rules, but predominantly focus on board composition and effectiveness. Becht, Bolton and Ruehl (2005) suggest that the prominence of corporate governance of late could be ascribed to a worldwide wave of privatisation, pension fund reforms, increased corporate take-overs, capital market reforms and corporate crises since the 1990's. One of the most important consequences of these reforms is increased activism by shareholders and institutional investors alike, as a result of improved access to relevant information needed for decision making. The ascendancy of "triple bottom line" reporting, which emphasizes not only economic performance, but also social and environmental performance, has gone a long way to improve access to relevant information. This method of reporting has been institutionalised in South Africa as well through the King II Report and JSE Listing Requirements. More and more companies use the GRI guidelines of August 2002, which appear in Annexure D, for the publication of relevant information. Triple bottom line reporting strengthens business sustainability in a society, which is impacted upon if the business fails. It also gives effect to the four cardinal values of good governance, namely fairness, accountability, responsibility and transparency, which values also form the central tenet of the King Reports in South Africa.

Mardjono (2005) refers to two recent studies by Walker and Fox (2002) and Grant (2003) for his suggestion that there is increased convergence between the corporate governance systems in place in the USA and East Asia, towards more protection for shareholders. The studies also suggest that corporate governance systems in countries such as the USA, UK, Germany and Japan now rely on an appropriate mix of concentrated ownership and governance

regulation. Mardjono (2005) adds that several studies have shown that corporate collapses, such as Enron, are to be ascribed to poor corporate governance practices, and in particular a departure from the four underlying principles of corporate governance, namely accountability, integrity, efficiency and transparency, rather than a failure of corporate governance frameworks. In most instances good structures were in place, but not applied or followed effectively by those who were required to adhere to it.

Rezaee, *et al.* (2003) propose the following nine principles of good corporate governance:

- Knowledge of what governance requires;
- Achievement of strategic objectives;
- Equal status of board and management;
- Strategic alignment and cohesion;
- Clarity and unity in control;
- Clarity in responsibility and accountability relationships;
- Focus on ownership interests;
- Continuous improvement of board competencies; and
- An understanding of governance costs.

Ferrari and Moloney (2002) caution that, although some measure of convergence in corporate governance practice is good, such structures and practices should remain flexible enough to allow for healthy competition between competing businesses and states. They divide current reform

strategies into three different categories, namely disclosure, board structures, and shareholder activism.

Disclosure convergence is seen as an important tool in the harmonisation process for member states to converge towards fuller disclosure of executive remuneration. The composition of boards and board committees should reflect a majority of non-executive directors' in order to effectively protect the interests of weak shareholders against the self-serving interest of powerful executives. Shareholder activism is viewed as a natural consequence of access to relevant information and informed decision making.

Hill (2006) summarises that recent corporate governance reforms have been aimed at increasing the independence of boards. The view is held that where executive remuneration is fixed in accordance with a formal procedure, by relatively impartial decision-makers under a structured remuneration framework, there is less reason for concern about abuses in the setting of executive remuneration. In practice however, it is not always possible to accurately define or determine board independence in relation to executive influences. Nevertheless, if independence is one of the fundamental principles upon which a governance framework is built in an organisation, there should be sufficient control measures to assess such independence objectively by all stakeholders of the organisation.

A global investor opinion survey (McKinsey, 2002), which covered research in 31 countries in Africa, Asia, Europe, Latin America, Middle East and North America, identified the top reform priorities for companies as follows:

- More timely, broad disclosure (52%);
- More independent boards (44%);
- More effective board practices (38%); and
- Adoption of performance related compensation (28%).

The success of this reform however will not be related to the number of new requirements to be complied with, or the boxes to be ticked, but rather to the extent in which it enables more equitable and informed protection of the interests of a wider group of stakeholders in an organisation.

4.6 *Concluding remarks*

Moxey (2004) concludes that there is little evidence that good corporate governance measures will prevent future corporate failures and contribute to organisational effectiveness. This could on the one hand be related to the lack of consensus on the nature of corporate governance – some view it as merely a bureaucratic exercise, while others view it as an attempt to protect shareholder interests. On the other hand, it could express the understanding that the existence of corporate governance control measures alone are not sufficient to ensure good governance, but should be understood, integrated, and applied properly to be fully effective.

The ultimate aim of corporate governance is to create value for different stakeholders. The concept of value may however be different for different stakeholders, and it is essential for the company to understand these

differences before designing and implementing an appropriate mix of control measures in its overall corporate governance system.

Two distinct but related aspects of corporate governance are important, namely internal governance (which is concerned with direction and control) and external governance (which is concerned with accountability to shareholders). The focus on corporate governance post Enron has unfortunately almost exclusively been on external governance. A more inclusive stakeholder and governance model should be adopted to make the practical aspects of corporate governance more effective (Vinten, 2002). The model developed in Figure 3 above (Annexure B) proposes such an integrated corporate governance framework. Kim and Senge (1994) add that such a model should enable organisational learning that links cause and effect, which are often far removed in time and space, through a process of systems thinking. It also requires an understanding and acceptance that obvious interventions do not always cause obvious or expected outcomes.

The desired outcome of good corporate governance is not just good legislation or regulation, but an ethical business culture based on informed stakeholder activism (Robinson, 2006). Legislation and regulation are only parts of the solution. The other part relates to honesty and general ethical behaviour which lies outside the letter of the law. In practice, the regulatory environment, integration of different governance mechanisms, and executive ethics have been found wanting. Robins (2006) suggest that whereas laws and regulations could be updated easily to deal with regulatory deficiencies, it would not be as easy to address deficiencies that can be ascribed to human frailty. It would take considerable effort by organisations to entrench good governance in their day-

to-day activities, but it is not a bridge too far. Shim (2006) suggests that an effective framework for corporate governance should feature simple, fair and efficient laws, with minimum fragmentation or overlapping regulatory statutes. In addition, it should create flexibility to adapt to different environments, allow for competitive advantage, and be communicated and incentivised for proper and effective application in an organisation.

Holstrom and Kaplan, (2003) identify three reasons why modern shareholders monitor managers more closely than in the 1980's, namely increased institutional shareholding across the world, strict regulatory measures, and an increase in shareholder activism. Although strict legislative interventions, such as the Sarbanes-Oxley Act in the USA and the UK Combined Code, impose very strict legal and compliance duties on companies, executives nevertheless continue to find loopholes in an increasingly complex field of executive remuneration, which allows them to serve their own interest above those of shareholders and other stakeholders of a company (Chong, 2004). The real effects of legislative interventions are however questionable in view of the fact that practical change happens before legislative changes are made. There is however strong support for the contention that Sarbanes-Oxley restored some confidence in corporate USA after the dramatic collapse of Enron. Authors speculate that the effects of Sarbanes-Oxley will probably be positive for companies with poor corporate governance practices, and negative in terms of costs for those with good practices (Holstrom and Kaplan, 2003).

Ferrarini, *et al.* (2003) list several problems with corporate governance practises in relation to executive remuneration. Firstly, boards are generally either too

passive or otherwise captured by executives to be able to efficiently act as agents for shareholder. This could be ascribed to impediments to the true independence of non-executive directors in the fulfilment of their duties. Secondly, independent directors should be able to withstand overbearing influences of executives, and should be able to judge executive performance objectively in relation to company performance. Unfortunately, here too the true independence of directors is questionable. Thirdly, remuneration committees should exercise objective control over the executive pay-setting process. The influences of CEO's and other executives may however impact negatively on the effectiveness of the pay-setting process. Some commentators go so far as to suggest that presumed independent directors do not necessarily do a better job, or add more value, than executive directors.

Allio (2003) offers a possible solution towards a better understanding of the concept of corporate governance, when he proposes that it is often necessary to understand the relationship between parts of the concept, in order to fully understand the concept as a whole. In following this logic, individual aspects such as executive remuneration, disclosure, and corporate governance ought to be considered individually before they are combined as a whole. Corporations could be viewed as social community systems in which ownership would be irrelevant (Senge, 2006). Shareholders would be regarded as investors, and not as owners, as under traditional agency theory, and would constitute only one group of many different but equal stakeholder groups in the organisation.

In the end, whatever the business theory is that prevails, there needs to be an effective balance amongst voluntary guidelines contained in codes of conduct,

statutory regulations, professional judgment and flexibility, in order for a corporate governance system to be effective. The important consideration is not the governance mechanisms in itself, but rather its effectiveness in establishing certain desired behaviour in modern business. There is no perfect, one-size-fits-all corporate governance system. Dramatic, over reactive pendulum swings is not the solution.

Holstrom and Kaplan (2003) suggest that the current corporate governance problems arose under exceptional market conditions which are unlikely to be repeated. If the underlying principles upon which a corporate governance system is built however remain valid, any dramatic changes in the environment should be sustained. It may be necessary from time to time to tweak some governance control measures as a result of the changing environment, but a strong focus on the principle to which it applies will reduce or eliminate the potential for abuse of the process, as is currently often the case.

Bradley, *et al.* (1999) summarise that, stripped of all its complexities, the debate on corporate governance can be reduced to the fundamental issue of whether the modern corporation should be viewed as a “nexus of contracts” negotiated amongst self-interested individuals, or as a “legal entity” in its own right. An inclusive approach to the very complex corporate governance construct, as proposed in Annexure B is required.

Warren Buffet in 2002 suggested that CEO’s don’t need independent directors, oversight committees or auditors to solve conflicts of interest, but simply need to do what is ethically right. The inclusive approach to corporate governance not

only holds executives accountable to the company, but also to the interests and expectations of all stakeholders of the company. It also requires a direct focus on the principles that underlie corporate governance, and an alignment of executives to balance the interests of all of the stakeholders in the organisation.

With all of these changes around, it is not surprising that scholarly interest in corporate governance has flourished in recent years.

5. EXECUTIVE REMUNERATION

We're overpaying him, but he is worth it.

- Samuel Goldwyn

Perhaps no topic in business is so emotive as remuneration of executives. The term “executive remuneration” is often misunderstood by commentators and executives alike. One of the possible reasons for this misunderstanding could be due to the use of alternatives such as compensation, pay or reward. Although there is a growing tendency towards using the term “total rewards” in remuneration practice, to refer to both financial and non-financial allocations to employees in return for their services, the term “executive remuneration” has been used in this study with reference to the total short and long term financial rewards paid to company executives.

Kakabadze, *et al.*, (2004) suggest that although the area of executive remuneration is one of the most intensely researched, it is probably one of the least understood. They ascribe this to a limited research focus on only excessive executive remuneration, pay design structures, and the link between remuneration and performance, while very little has been done to explain the relationship between executive remuneration and its impact on the interests of different stakeholders, which, according to Blair and Ramsay (1992), become very prominent in the area of executive remuneration. This supports the view of Ferrarini, *et al.* (2003), who state that the executive remuneration debate has three elements, namely structure, governance and disclosure. Each of those elements however have many subsets and interrelations which need to be

properly considered before executive remuneration as a construct can be fully understood (McKnight and Tomkins, 1999).

Much of the scholarly writing on executive remuneration starts from the premise that executives are overpaid, and then attempt to offer suggestions to address the problem. There are however those who believe that the level of pay is not the problem as long as it is linked to performance, and that it is therefore merely a cost of doing business in the corporate form (Stabile, 2000). It is however interesting to note that Plato posited that no-one should earn more than five times the wages of an ordinary worker, while Drucker argued in the mid 1980's that the difference should not be larger than twenty times, and that the growing gap may threaten the credibility of business leadership. Current gaps are already greater than 400 times in South Africa.

Executive remuneration has become a hot potato across the world in view of the phenomenal global escalation of its levels, and the connection between excessive executive remuneration and corporate collapses. While there might be a popular tendency to view executive remuneration as a specialised topic, its connection to corporate collapses of late emphasized the fact that executive remuneration presents the traditional corporate governance problems in a highly concentrated form (Hill and Yablon, 2002).

The conflicts of interest between executives and shareholders, which are exacerbated by the positional power of executives over, amongst others, financial reporting, disclosure and performance, may provide executives with opportunities to advance their own interest above those of the company and its

shareholders. Fine-tuning executive remuneration packages may reduce, but will not eliminate these problems.

This chapter examines the origins and development of executive remuneration, both conceptually and practically, and how these impact on the composition of executive remuneration packages. The different theories advanced over time for determining executive remuneration packages and levels will also be evaluated, and related to the problems associated with executive remuneration. These problems include, amongst others, excessiveness of remuneration packages, conflicts of interest, and ineffective pay setting processes. The chapter also investigates some current global trends in executive remuneration practice, and how this could be related to the corporate governance process and mechanisms in a company. The aim of the chapter is to create an understanding of the concept of and rationale for executive remuneration, and to analyse the role of executive remuneration in balancing interests in an effective corporate governance system.

5.1 Origins and nature of executive remuneration

Drucker (1987) explains that modern business enterprises did not develop out of traditional organisations, but rather as a result of a paradigm shift to a new business enterprise that was not run by its owners, but by shareholders who had a claim against the organisation's profits, rather than against its fixed assets. The primary focus of these shareholders was not to run the business, but to receive a return on their investment in the organisation.

A separation between ownership and control of the organisation had to be developed by means of the creation of a new legal *persona* - the corporation, which has subsequently evolved into the most pervasive, universal organ of modern society. One of the underlying characteristics of the modern corporation is that professional management executives are required to run the corporation in such a way as to generate returns for others rather than for themselves, in exchange for fair executive remuneration. This separation of ownership from control has led to a multitude of studies, criticism and controversy.

The primary objective of the modern corporation is ordinarily to maximise shareholder value, which it does, at least in part, through its choices of managerial compensation contracts to incentivise certain managerial behaviour (Rajgopal and Shevlin, 2001). Rogers and Gago (2003) suggest that, whereas executive remuneration was based traditionally on economic performance, the modern practice is also informed by a combination of the following considerations:

- Egoism: Acting in self-interest;
- Deontology: Adherence to independent moral rules or duties;
- Relativist: Using peers to define ethical standards;
- Utilitarianism: Ensuring greatest positive consequences for the greatest number of people;
- Virtue ethics: Cultivating virtuous management traits; and
- Ethics of care: Listening to other perspectives.

High executive remuneration could therefore be justified where significant wealth is created for shareholders. Such remuneration could be based on

either inputs (skills) or outputs (performance). The challenge is to find the right combinations which would incentivise the desired behaviour best – that is between “an incentive to achieve” or “reward for having achieved” a target.

5.2 Composition of executive remuneration packages

The composition and levels of executive remuneration packages are used increasingly as a strategic tool to attract, motivate and retain key executive skills in a globally competitive labour market (Allcock and Pass, 2006). The international WorldatWork Total Rewards Association propagates the diagram in Figure 4 below to show how business and reward strategies influence the attraction, motivation and retention of satisfied and engaged employees in a reciprocal relationship with business performance and results.

Figure 4: WorldatWork Total Rewards Model

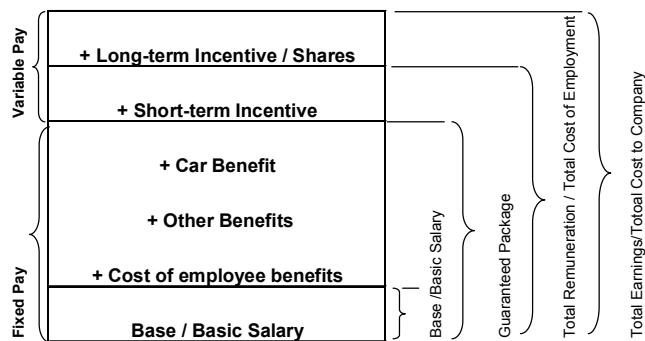


(Source: <http://www.worldatwork.com>)

Generally, executive remuneration packages would consist of a basic salary, benefits, short term, and long term incentives (Allcock and Pass, 2006; Hill, 2006). One would expect the basic component of the remuneration package to

enable an executive to maintain a standard of living that is commensurate with the status and esteem of the position held, and to pay for the competent performance of all tasks required to be performed in the job. Short term and long term incentives are ordinarily linked to a mix of performance measures (Epstein and Roy, 2005). Short term incentives are normally paid in the form of *ex post facto* cash bonuses for meeting prior agreed objectives within a twelve month period, whereas long term incentives are in the form of share or option allocations to incentivise certain behaviour and actions over a period of up to five years. Bussin (2007) describes these components of executive remuneration by means of the diagram in Figure 5 below.

Figure 5: Executive remuneration package



(Source: Bussin, 2007)

A clear distinction needs to be drawn between the following components of an executive remuneration package:

- **Salary:** The fixed cash amount of compensation that does not vary according to performance;
- **Bonus:** Compensation based on individual, group or corporate performance;

- Stock options: Option to purchase stock at an exercise price on a fixed date;
- Stock grants: Allocation of actual shares; and
- Stock appreciation rights (SAR's): Right to receive the increase in value of stock above a specified level at a specified date.

Recent studies show increased use of non-financial measures in an executive performance evaluation, because it predicts long-term sustainability better than what financial performance measures could do (Banker, *et al.*, 2000). There is however very little empirical evidence of the relationship between non-financial measures, such as those identified in Table 1 below, and financial performance. One useful motivation for the use of non-financial measures is that it reflects actions that do not appear in financial statements, and often have a longer term impact than short term financial measures. For this reason, non-financial measures could serve as heading indicators of future financial performance.

Kaplan and Norton (1996) developed the Balanced Scorecard as a way to manage business, in which financial measures are embedded in a more balanced management system that links short term operational performance with long term strategic objectives. Table 1 below sets out the standard measures that are most often included in a Balanced Scorecard. These measures could provide a balanced approach to linking executive remuneration to the satisfaction of different stakeholder needs, and could therefore play an important role in the executive remuneration/corporate governance debate. The balanced scorecard approach is however significantly underused in the executive remuneration space in South Africa, and perhaps across the world.

Table 1 : Balanced Scorecard Measures

FOCUS AREA	
Financial	ROI; EVA; Profitability; Revenue growth; Cost reduction; Productivity
Customer	Market share; Customer acquisition/retention; Customer satisfaction.
Learning and growth	Employee satisfaction; Employee retention; Employee productivity
Business processes	Efficiency; Effectiveness

(Kaplan and Norton, 1996)

The recent explosion in the use of long term incentives as part of executive remuneration packages has led to significant increases in the wage gap between executives and ordinary employees. Bebchuck and Friend (2004) record such increase in the USA, between 1991 and 2003, as rising from 140 times to 500 times the pay of an ordinary worker. Crotty and Bonorchis (2006) give a very graphical description of the excessiveness of executive pay in South Africa. According to them, South African executives are really worth their weight in gold if one assumes an average weight of 90 kilograms per executive and a cost of gold at R138 000 per kilogram (2006 cost). This amounts to R12,4 million per executive, which is not far off the 2006 average executive remuneration package in South Africa. The question however should not be whether this level of remuneration is excessive, but rather whether it is fair and linked to the achievement of realistic performance targets which create value for the stakeholders of the organisation.

Porter (2004) provides a possible explanation for these high levels of executive remuneration in that executive jobs are extremely complex because of the external demands put on them, their inability to fully control functions that determine the company's direction and success, the constant scrutiny of all

executive actions, and the need for executives to build trust and share power. He adds that the increasingly public lives and images of executives force them to make very difficult trade-off decisions, which cause attraction-focused levels of executive remuneration to unparalleled heights. Mintzberg (2004) however questions this reasoning by arguing that, if leadership is about teamwork, the benefits of excessive remuneration should not be an exclusive payment to executives, but should also be available to those ordinary employees who add value through their actions. Such a sharing of benefits would improve the trust relationship between employees and executives, which is hampered by the current exclusivity of certain rewards to executives only. The only justifiable solution is to ensure that rewards for executives and other staff are fully commensurate with the relative value they create for the business and its stakeholders. That assessment will however not come from merely ticking compliance boxes, but from an active and focused measurement of whatever performance evaluation and control measures the company has implemented to ensure this.

Economic theory predicts that executives will work smarter when incentivised properly. Abowd and Kaplan (1999) however question whether incentive contracts actually motivate executives in this way. They argue that most incentivised pay-designs are not effectively linked to improved performance. The recent failure in 2009 of ESKOM in South Africa to produce improved corporate performance despite justifiable incentives to executives to cut operating costs, is a prime example.

Bushman, *et al.* (1996) believe that a pay design that makes executive remuneration sensitive to performance on some tasks only, may lead to suboptimal effort on other tasks, to the detriment of the total business system. McTaggart, *et al.* (1994) suggest in this regard that pay-for-performance should be designed as a relative-pay-for-relative-performance system, where performance is measured against that of comparable peers. There have been many attempts in literature to test the relative performance hypothesis, namely that there are some aspects of firm performance that are outside executives' control. A scheme that displays a relative performance link can reduce risk of poor or incentive alignment (Abowd and Kaplan, 1999). Aggarwal and Samwick (1999) however, found a contrast to this view in research results that show that, despite its attractiveness, few corporations utilize relative performance evaluation. Possible explanations for this is the complexity of this kind of benchmarking, and the unavailability of comparative data in the market. Gibbons and Murray (1990) add that such a design risks encouragement of managerial behaviour to lower performance across industries, and to collude with results. This would hardly be in the interest of good corporate governance.

5.3 *Executive remuneration theories*

A number of theories have been developed over time to explain executive remuneration. As is to be expected due to the ever-changing nature of the field, there is not yet a faultless theory. A number of these theories advanced will be analyzed in terms of its strength and shortcomings in explaining executive remuneration. Annexure E lists a more comprehensive explanation of the

different theories that explain the composition and importance of executive remuneration packages.

The dominant approach in the executive pay-setting process has for some time been the “optimal contracting” approach, in which pay arrangements are set by boards that aim to maximise shareholder wealth and reduce agency costs. It is therefore an instrument to combat the agency problem. In contrast, the “managerial power” approach suggests that boards do not act at arms’ length and that executives have the power to influence their own remuneration. These two approaches are not alternatives, but could work together (Bebchuk, *et al.*, 2002). There is no known contract which would align the interests of managers and owners perfectly. Research has shown that managerial power and the incentives and ability to camouflage rent extraction is significant in a scenario where boards are captured. The optimal contract is therefore one that minimises agency costs, and displays the following three mechanisms:

- Boards select value maximising compensation arrangements at arms’ length;
- Executives are constrained by market forces to behave in a self serving manner; and
- Effective shareholder activism blocks sub-optimal executive remuneration.

5.3.1 Agency theory

Traditional organisations were characterised by owners who were also managers. With the development of the modern corporation, a separation between ownership and management control was created due to the impracticality of diversified shareholders to participate directly in the management of the corporation. In order to protect the interest of shareholders, representatives were appointed to oversee management actions, and to report thereon to shareholders. A principal-agent model was therefore established, and popularised by the leading works of Berle and Mains in the 1930's. Kakabadze, *et al.*, (2004) state that agency theory has underpinned the modern theory of the firm, as well as corporate governance thought, including executive remuneration, since its conceptualisation.

Agency theory postulates that shareholders (owners) delegate the management of the corporation to executives (agents), who manage the corporation on their behalf. A separation of ownership from control inevitably leads to a potential conflict of interests between owners and executives, which is an inherent and most critical difficulty underlying this theory (Jensen and Meckling, 1976). Agency theory seeks to address this conflict of interests by means of incentivisation of managers to align their actions with the interests of shareholders rather than their own interests. The costs incurred through such incentives and interventions are commonly referred to as “agency costs” (Allcock and Pass, 2006), which is minimized in instances where owners have complete knowledge of the affairs of the corporation and of management's actions, and board monitoring is optimal. Kakabadse, *et al.*, (2004) suggest that

alignment of executive actions with the interests of shareholders is often most optimal when executive incentives are tied to company performance.

Practically though, it is not always clear what the interests of shareholders are. There are significant conflicts between short term and long term investment interests of shareholders, as are there conflicts between majority and minority shareholder interests. This agency view also does not properly consider societal interests in the long term sustainability of the corporation.

To a great extent, agency theory still dominates current considerations of the executive pay question (Ferrarini and Moloney, 2005). It generates two competing views. The first view is that it remedies agency costs generated by the conflicts between shareholder and executive interests, through proper incentivisation, which is viewed as a powerful way of attracting, motivating and retaining executives to pursue shareholder wealth creation. The second view is that incentivised executive remuneration can constitute agency costs in itself.

Ferrarini and Moloney (2005) compare the applicability of these two viewpoints in companies characterised by differences in ownership structure, and come to the conclusion that the agency problem is far more prevalent and significant in companies with dispersed ownership structures than in those with block holding structures. In dispersed ownership structures the levels of executive remuneration are commonly higher than those in block holding companies, to ensure proper alignment of interests between dispersed shareholders and executives. In block holding companies, owners should be sufficiently powerful to properly monitor executive actions, and to withstand any form of executive self-dealing. This accords with the view expressed above that corporate

governance needs are not uniform across business structures, and that ownership structure therefore influences the design of appropriate governance control measures which are appropriate for the specific corporate environment.

The inequity in respect of access to accurate and timely information between executives and owners, and the impact thereof on setting performance targets for executive incentives, create increased agency costs in dispersed ownership structures. Executives have the positional power to manipulate the sharing of important information to serve their own interests best.

Agency theory therefore predicts that the separation between ownership and control of corporations could inherently lead to a conflict of interests where executives prefer to pursue their own interests above those of shareholders. This often includes risk-free and excessive executive remuneration that is not necessarily linked to performance. This necessitates governance frameworks to establish safeguards against executive self-dealing.

Despite the compelling logic of agency theory in dispersed ownership structures, there is little empirical support for the effectiveness of the theory to balance conflicting interests by means of executive remuneration (Kakabadse, *et al.*, 2004). Executive remuneration is however only one control measure in a larger corporate governance system which seeks to balance interests of different stakeholders. It should not be evaluated in isolation, but rather in conjunction with all other control measures in an inclusive governance system. Although its individual contribution may sometimes seem negligible, it may serve as an essential trigger or catalyst for the effective operation of other

control measures. Viewed in this way, the benefits of agency theory should not be discarded in any form of organisational structure.

5.3.2 Social comparison theory

As a result of the inability of agency theory to explain executive remuneration in all instances, social comparison theory was advanced as an alternative. Kakabadse, et al., (2004) explain that social comparison theory holds that executive remuneration could be determined by means of comparisons of observable executive performance across institutions and industries. Such comparison could be enhanced significantly where there is cross-representation by executive and non-executive directors across different companies. This practice is however simultaneously the biggest drawback of the theory in that it leads to potential benchmarking against peer remuneration levels instead of against performance objectives. The ratcheting effect of this kind of benchmarking causes undue and excessive executive remuneration increases, and executive migration to the detriment of shareholder and other interests in the organisations performance.

5.3.3 Stakeholder theory

Stakeholder theory of executive remuneration postulates that broader sets of stakeholder interests and relationships outside the immediate environment of a company need to be considered in view of greater globalisation and a changing socio-political context (Kakabadse, et al., 2004). The limited focus on shareholders' financial and economic interests within the governance

framework of a company is, according to the stakeholder theory, not in line with practical reality. Corporations form the basis of modern society, and provide employment for a large group of societal members, who have a direct interest in the long term sustainability and prosperity of the organisations. This is often in direct conflict with the short term interests of shareholders who seek quick returns on their investments. There is a general tendency globally, including in South Africa, towards increased considerations of corporate social responsibility and broad stakeholder interest in the modern executive pay debate.

5.3.4 Managerial power theory

Bebchuk and Friend (2004) refer to managerial power theory as a practical reality check on the agency theory. This theory recognises that executives are overwhelmingly motivated by self-interest when their remuneration is at stake. In terms of this theory, executives occupy immensely powerful positions where they can manipulate boards through social structures, influence relationships, and cause inequity in respect of access to information. Any attempts to redress the power imbalance between executives and shareholders by means of remuneration practices will simply cause uncontrollable upward spiralling of executive pay. Managerial power theory therefore highlights the inherently conflicted process of pay-setting for executive remuneration.

5.3.5 Tournament theory

Tournament theory proposes that executive remuneration is a function of a series of “tournaments” executives have to progress through in a corporate

hierarchy (Pepper, 2006). These tournaments include career promotions inside and outside an organisation, which is often linked to incentivised aspirations to climb the corporate ladder. Under tournament theory, a larger remuneration gap between consecutive executive positions would inspire persons in lower positions to increase their efforts, in order to rise the corporate ladder to higher positions (ICGN, 2002). Tournament theory typically emphasizes that the key drivers of executive remuneration should be specific job attributes rather than personal competencies, knowledge and experience. McConvill (2005) adds that it is not necessarily only monetary reward that motivates executives, but rather their relative positions in relation to other executives. This is especially relevant in respect of comparisons in the lifestyles of the rich and famous. It would however be more appropriate to compare the social and performance superiority of one company above another, which would lead to sustainable social value creation, than to compare individual executives to one another, which inevitably lead to ratcheting of executive remuneration which is not necessarily aligned to increased performance.

5.4 Problems associated with executive remuneration

There has been heated debate over general concerns that excessive executive remuneration could be damaging to a company and all of its stakeholders, as well as worker morale and the economy generally. Hill (2006) argues that the central concern about executive remuneration was the potential conflict of interest in the setting of executive remuneration packages, which are generally fixed by the board, on recommendations by its remuneration committee. This argument highlights the three most fundamental problems associated with

executive remuneration, namely conflicts of interest, ineffective pay-setting processes, and governance failures.

Stabile (2000) is of the opinion that current executive pay-setting processes do not sufficiently represent shareholder interests. There is certainly merit in this view, but it does not address whether the executive pay setting process represents the interests of other stakeholders in the organisation, which is at least as important as the interests of the shareholders. Mongalo (2007), in attempting to identify the problems associated with executive remuneration, incorrectly describes the symptoms of excessiveness, unrelatedness to performance, and non-transparency as the problems. These symptoms are nonetheless common in respect of the problems identified by Hill. Yablon (1992) convincingly suggests that, in its most simplistic form, there are two basic arguments in support of the contention that executives earn excessive remuneration, namely “unfair price” that relates to the levels of remuneration, and “unfair process” that relates to the pay-setting process.

5.4.1 Excessive executive remuneration

The controversial issue of excessive executive remuneration is not a phenomenon of the modern era. The President of Bethlehem Steel was for example paid \$1,65 million in 1929, which translates to more than \$15 million in 2003 (Grant, 2003).

Critics have referred to executives' salaries as madness, while defenders have countered that executives are worth every cent paid to them (O'Reilly, *et al.*,

1998). The differences in these two comments are often directly related to the extent to which executive remuneration is linked to performance. Performance is an important determinant of executive remuneration because the CEO is ultimately responsible for the performance of the firm, and rewards should be contingent thereto. Certain non-economic factors however also play a role.

Becht, *et al.* (2005) ascribe the current high levels of executive remuneration to extra-ordinary gains in shareholder wealth since the 1990's. Incentive pay through the allocations of stock and stock options has been identified as a particularly strong driver of executive remuneration during this period. Lowenstein (2000) however cautions that the allocation of stock and stock options could dilute shareholders interests in the long run and especially if it is not properly related to performance targets. He also warns that increase in executive remuneration levels could lead to an unjustifiable ratcheting of executive remuneration levels generally, in an increasingly competitive market for executive talent. This has already been identified as one of the unintended consequences of applying the social comparison theory incorrectly.

Stabile (2000) makes an interesting comparison between executive remuneration and a partnership scenario, and concludes that although the partnership analogy does not hold up perfectly, it could still be used as a roadmap to improve the executive pay-setting process. Some of these important lessons include:

- The sharing of gains between owners and managers at predetermined formulae;

- The inclusion of significant downside risk in executive remuneration contracts, to avoid any possible short term manipulation of results by managers;
- Arms' length negotiations between owners and managers;
- More equitable and justifiable use of remuneration consultants and pay surveys;
- Limited pendulous legislative and regulatory interference; and
- Equilibrium in the currently competitive market for executive talent.

Although there may be merit in this proposal in some instances, it does not offer a principled solution of general application. An integrated framework built upon universal principles of governance, which allows some flexibility in the design and mix of control measures would be far more effective as a general corporate governance system. These control measures could then also include some of the above lessons from a partnership scenario.

5.4.2 Conflicts of interest

Traditionally it has been assumed that the main problem with executive remuneration related to the divergence between the interests of shareholders and self-serving executives (Hill, 2006). Many recent developments have attempted to align those competing interests through different methods of incentivisation. Such development is supported by Allcock and Pass (2006), who regard mechanisms to motivate executives to align their own interests with those of shareholders as remuneration best practice. Although there is certainly merit in such a suggestion, there is often difficulty in assessing the nature of

shareholder interests, which might range between short term returns and long term growth.

At a more fundamental level the question arises whether shareholders' investment interests should be regarded more prominently than long term stakeholder interests in the sustainability of the company. As have been indicated above, modern theory in this regard seems to suggest a need for broader stakeholder consideration in determining remuneration policy in an organisation. Chambers (2005) supports this view by suggesting that short term wealth maximization interests of some investor shareholders might be detrimental to the long term sustainability of an organisation, the latter of which clearly benefits a broader stakeholder society.

The underlying principle of allocating executive incentives to ensure alignment of executive interests with those shareholders, as assumed owners of the corporation, should therefore be questioned. Are shareholders owners of the corporation, or merely investors in a separate legal entity? Should executive interests be aligned to those of investors or those relating to long term sustainability of the company in its own right? In terms of traditional theory the requirement has always been for executive interests to be aligned to those of shareholders, as owners of the corporation (Goobey, et al., 2003). This belief may however have become dated in view of the increased prominence of broader stakeholder interests in organisations.

Ferrarini, *et al.*, (2003) aver that there is evidence that executives are able to manipulate performance indicators linked to incentives (such as share price

values) due to their access to and control over relevant information. The timing of the release of information that might impact positively or negatively on performance indicators could for example be critical in respect of vesting of incentive-based portions of executive remuneration. In addition to this, Kakabadse, *et al.*, (2004) does not consider the allocation of share options as an incentive to align executives' actions to shareholder interests to be effective if there is no downside risk for executives, in terms of which they are penalised for poor performance. The fact that there is no downside risk allows executives to take severe risks which might not be in the best long term interest of the company. The fact remains that there will always be at least a potential conflict between dispersed owners and managers in a corporation, and that effective and appropriate control measures have to be applied for the specific situation in which the organisation finds itself.

Handy (2002) refers to a 2002 Gallup poll which showed that 90% of Americans did not trust executives to properly look after the interests of shareholders, and that 43% believed that executives only looked after their own interests. The author concludes that the explosion in the use of stock options as an executive incentive, from an average 2% of a total pay package in 1980 to 60% in 2002, has contributed largely to the popular view that executives are self-serving, which in turn creates public mistrust in corporate executives. The benefit of share options as a reward element for executives however lies in the timing of allocations thereof, and has a more direct correlation to general market movements than to individual performance. There is often no or little option value for good individual performance in a poor performing general market, and great value in poor individual performance in a well performing general market.

The South African market has mirrored the global market post the economic downturn of 2009 in replacing share option schemes, which would predictably be under water for the next few years, with share and cash based schemes which provide immediate value despite the negative economic conditions. This illustrates how executives could hedge themselves against downside risks, by taking value despite poor performance.

Mintzberg (2004) ascribes this phenomenon to a culture of leadership that is dragging modern business down through their self-interest. He proposes a possible solution that companies might need less leadership, or leadership of a different kind, to support employee initiatives which could add sustainable value to the company. There is strong merit in the author's suggestion that the dysfunctional separation between ownership and management should be abolished, and replaced by a common leadership that is diffused throughout the organisation. This also supports the view that broader stakeholder interests, which includes the employees of the organisation, should be known and considered in especially reward practices.

5.4.3 Setting of executive pay

The process of setting executive remuneration takes place in an inherently adversarial arena between executives and shareholders who each wish to advance their own interests (Ferrarini, *et al.*, 2003). The potential conflict situation is exacerbated in dispersed ownership organisations, and where the board has surrendered control to powerful executives. Under such conditions the executive pay-setting process can easily turn into an executive wealth-

skimming process where negotiations do not take place at arms' length. In order to restore the balance of interest, corporate governance control mechanisms are required.

It is important to remember that the ultimate aim of an executive remuneration strategy is to attract, motivate and retain suitable management skills, which are a globally rare commodity. Miller and Vaughan (2001) ascribe the increasing need for professional managers worldwide to rapid industrial expansion and globalisation. The design of attractive and market-related remuneration packages that present prospects of significant gains is a highly successful tool in this regard. Caution should however be exercised that executive remuneration levels do not spiral uncontrollably upwards as a result of the fact that most companies, in an attempt to attract, motivate and retain key talent, apply a remuneration strategy that aims to pay above market levels. Although the market is generally a fair indicator of appropriate executive remuneration, and a link between increases in executive remuneration levels and industry performance has been shown in a number of empirical studies (Kakabadse, *et al.*, 2004), there is still a caution that benchmarking of this kind could lead to a ratcheting of remuneration levels that is unrelated to performance.

Executive remuneration designs are often ineffective in addressing the link between performance and reward (Ferrarini and Moloney, 2005). This alone raises the need for effective governance and disclosure practices. Kakabadse, *et al.*, (2004) question the underlying assumption that executive actions are directly and solely related to improved company performance. They contend that general market forces, legal, political, social and economic forces, as well

as the human capital of an organisation have at least an equal influence on company performance. This view is shared by the International Corporate Governance Network which suggests that the assumption that company performance should be ascribed to executive actions, is often in practice supplemented by an unmotivated assumption that a decline in performance should be ascribed to factors beyond the control of executives (ICGN, 2002). Such an assumption underlines the significant positional power executives enjoy to influence popular thought, and it is this risk that ought to be reduced or eliminated through effective corporate governance control measures.

One of the dangers of ignoring external influences on company performance is that poor executive performance may be rewarded in periods of general market growth, or conversely, that excellent executive performance may not be rewarded in periods of general market decline. Ferrarini and Moloney (2005) propose that such unintended consequences could be resolved by linking executive performance and remuneration to peer group indices in such a way that executives are only rewarded if they outperform the competition. Although this view is compelling, it is silent in respect of the need for appropriate target setting upfront by the organisation. It is quite conceivable for executives to still manipulate the comparisons if those targets and comparators have not been clearly set out and communicated in upfront performance contracts with executives.

It is common practice in most companies that executive remuneration systems are loaded firmly on the upside, with no or very little downside risk (Chong, 2004). This is especially relevant in respect of share options where executives

elect to exercise their options if share prices have risen above the pre-determined strike price, but simply elects not to exercise when share prices have not risen to such extent. This implies a lack of punishment for poor executive performance.

Mongalo (2007) confirms that it is clear that investors increasingly require executive remuneration to be linked to real contribution to wealth creation. This implies that executive incentives should be aligned to shareholder interests in such a way as to benefit executives when their performance is good, and to punish executives for poor performance. If effective and appropriate performance measures are established for the purpose of determining executive remuneration, agency costs may be reduced when executives are rewarded for good performance, and punished for bad performance. Practically though, executive incentives are not readily determined with sufficient downside risk to punish poor executive performance. Mongalo (2007) adds in this regard that companies often seem to reward executives for failure when lucrative severance packages and “golden parachutes” are paid to terminate their employment. The King Report on Corporate Governance in South Africa, 2002 (King II Report) requires fuller disclosure to guard against any possible abuse that might occur in respect of the payment of high severance packages to executives, merely to get rid of them.

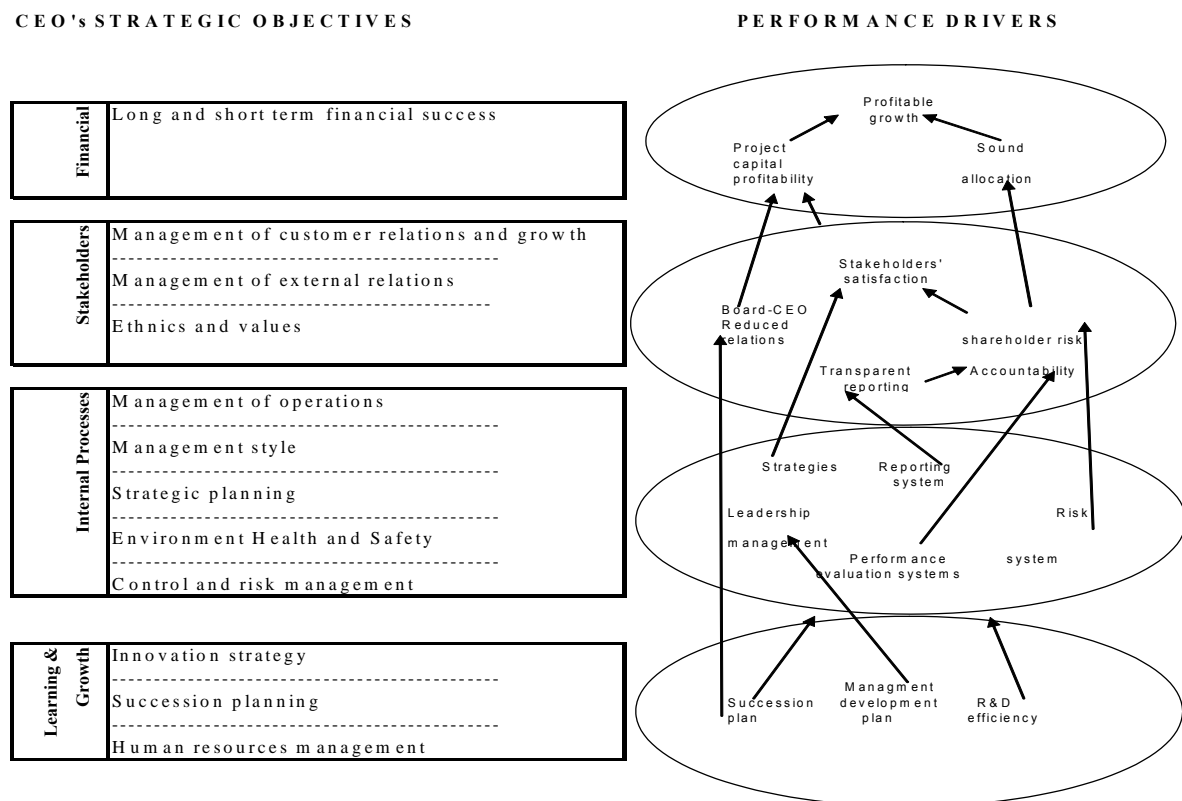
An interesting question is raised (ICGN, 2002) by asking whether it is only financial compensation that drives executive performance towards alignment with stakeholder interests. The argument is made that such a view would be inconsistent with the long vesting periods applicable to share options if

compared to the significantly shorter average tenures of executives in specific companies. In addition thereto, the increased use of perquisites, such as personal drivers and club memberships for executives, in especially French and Japanese firms, would indicate otherwise. It is therefore paramount to determine clearly and upfront what motivates executive performance, before designing incentives that may not have the desired impact. The form of incentive will generally determine executive behaviour. A strategy of formulating and quantifying flexible total rewards packages in accordance with individual needs, which also incentivises executives more personally to achieve performance targets, would be far more effective than offering standard reward elements (which may not be aligned to what executives want to encourage their increased performance).

Epstein and Roy (2005) suggest that an unduly high emphasis is placed on financial measurements of performance, which they consider as only one aspect of performance measurement that needed to be considered. They argue for a broader definition of corporate performance, which includes clearly identified multi-dimensional performance criteria, such as contained for example in the balanced scorecard, which would present a far more appropriate measure of executive performance in relation to corporate strategy. They propose the scheme in Figure 6 below as a possible link between executive performance and the achievement of corporate strategy, in terms of balanced scorecard framework. What is especially compelling in their argument is that there is a great degree of flexibility which could be built into such a scorecard, depending on the individual situation in which the organisation finds itself. The corporate environment may be such that the achievement of a certain non-financial

objective is more critical than reaching financial targets at a specific point in time, and vice versa at a different point in time. The balanced scorecard approach also allows companies to drive performance from different perspectives, thereby facilitating different stakeholder expectations better.

Figure 6: The causal relationships in an executive balanced scorecard



(Source: Epstein and Roy, 2005)

Remuneration practice, and especially in respect of executive remuneration, is a fast developing field, where new schemes are continuously developed to attract, motivate and retain scarce managerial skills. This development causes many complexities, and raises the potential for conflict between shareholders and executives (ICGN, 2002). Ferrarini, *et al.*, (2003) acknowledge the current complexities in executive remuneration, but caution against invasive legislative interventions into this minefield. They add that current pay-setting practices are

characterised by a number of structural defects that make it possible for self-serving executives to hide vast wealth transfers from shareholders, despite the role of ineffective boards in the design process. No single control measure, or fixed combination of a number of different control measures, would however be universally effective in addressing this problem. A plausible solution is to have a principled governance framework which allows companies the flexibility to design control measures which are appropriate for their situation and needs. The principled approach of King III in South Africa, of “apply and explain”, goes a long way to entrenching this view. In terms thereof, companies are required to apply the principles contained in the King III Code, and to explain how and why they have been applied.

5.4.4 The role of boards

Although executive remuneration policy and levels are ordinarily determined by boards on the recommendations of their remuneration committees, it is ultimately the responsibility of the board *per se* to take accountability for it (ICGN, 2002). Various governance guidelines and practices have been established, as more fully discussed below, to address this responsibility, but practice has shown that even the most noble of intentions in board governance is susceptible to manipulation by self-interested executives.

The King II Report makes the point eloquently that human behaviour and ethics cannot be regulated by means of legislation to avoid failure. This is especially so in the inherently conflicted criteria of executive remuneration design, characterised by a desire to align executive actions to the achievement of

shareholder interests. Bebchuk and Friend (2004) suggest that prospective non-executive directors should have a clear understanding of their roles, and what is expected of them, before taking up these positions. This is especially the case in strictly legislated environments, and would conceivably be a key requirement in South Africa under the new proposed Companies Act, of which various drafts have been tabled in parliament in 2009 and 2010.

5.5 *Modern trends in executive remuneration*

The most significant and common global trend in executive remuneration is the explosive growth of executive pay packages in relation to ordinary wage increases and market growth rates. The question however remains whether this could be ascribed to increasing roles for executives, global scarcity of executive talent, recognition for increased performance, positive markets, or skimming of wealth by powerful executives. This research considered excessive executive remuneration in relation to performance as one of the potential symptoms of a deeper corporate governance problem, and sought to understand how disclosure of executive remuneration, as one of the potential governance control measures in an inclusive corporate governance system, could contribute to reduce or eliminate both the causes and symptoms of this deeper problem.

Crotty and Bonorchis (2006) refer to a 2006 Independent Remuneration Solutions survey which revealed that the average total remuneration package of a FTSE 100 chief executive officer rose by 230% between 1998 and 2005, while ordinary salaries rose by an average 38% over the same period. They ascribe this to the globalised effect of massive increases in executive

remuneration in the USA, which found its ways into corporations across the world, as the fight to attract, motivate and retain key executive skills intensifies. Krugman (2006) however suggests that executives have always had the power to pay themselves lavishly, but that their self-enrichment was limited by what Bebchuk, *et al.* (2002) call the "outrage constraint", in the form of unions, the press and other forms of activism. He adds that such an outrage constraint has been conspicuously absent of late, and that this is due to mainly hard handed corporate strategy to achieve this. With particular reference to the USA, he suggests that the proceeds from its economic growth during the past decade have rather found its way to executives' pay packages, which have grown by 279 times, than to a broad cross section of the labour market, which have fallen in real terms. Executives also clearly have the upper hand in executive pay-setting processes all over the world, as a result of the high demand for their skills (Miller and Vaughan, 2001). Although there is merit in this view, it does not automatically make a case for increased executive pay where the particular executive is remunerated beyond the level of value he or she brings to the organisation. This problem is especially acute in South Africa where executives are often appointed to advance transformation targets, rather than for their executive skills, and where these individuals are remunerated at the same levels (or even at premiums) as other well experienced and skilled executives. This practice increases the likelihood of undue pay ratcheting which is unaligned to corporate or individual performance.

Bussin and Fletcher (2007) is of the opinion that executive remuneration in South Africa is generally linked to some measure of performance which is in line with stated international best practice. It is however not clear how effective

performance measures are defined, or whether some vague statement to the effect is made in companies' remuneration policies to hide the skimming of wealth by executives. Holburn (2007) however refers to a very interesting 2001 CSI survey in Australia that seems to support a realisation that stock options, as long term incentive aimed to align executive interests to those of shareholders, was open to abuse by executives. According to the survey, the award of long term incentives to CEO's dropped from 24% in 2000 to 17% in 2001, while such incentives to other executives dropped from 17% to 14% in the same period. Empirical evidence shows that the form rather than the level of executive compensation motivates managers to increase firm value, and that equity based remuneration is positively related to firm performance.

The phenomenal worldwide increases in the levels of executive remuneration, which has widely been attributed to the efforts of powerful, self-serving executives, is tantamount to questionable executive ethics, which has the potential to distort business culture (Handy, 2002). Ferrarini and Moloney (2005) however caution against aggressive interventions and strict compliance requirements, which could be counter productive due to the sensitivity thereof in a domain ruled by very powerful executives. Aggarwal and Samwick (1999) propose that a plausible solution would be to tie the ratio of compensation based on own firm performance to rival firm performance, but that evidence shows this ratio to decrease in line with increased competition. They however caution that relative performance pay may incentivise managers to lower industry performance by implementing too aggressive pricing policies. A combination of own and rival firm performance may be an optimal measure, but may be difficult to design. Although this may be practically difficult to apply, it

would be more achievable where professional and dedicated reward practitioners are appointed by organisations to manage remuneration in their businesses. This study especially examined the differences in remuneration practices in companies where there are dedicated and professional reward practitioners against those companies where remuneration management is fragmented between different divisions or employees, who do not have it as their primary responsibility to apply globally accepted best practice science to their rewards practices.

Crotty and Bonorchis (2006) argue that globalisation, international comparisons facilitated by increased disclosure, and the growing use of remuneration consultants have caused immense increases in executive remuneration in the USA, and consequent exportation thereof across the world. They suggest that this trend will increase until such time as public outrage and activism, more effective regulation, or a resurgence of cultural and structural factors constrains this growth.

Not all commentators agree that convergence of executive remuneration practices will converge along the lines prevalent in the USA, which is characterised by strong pay-for-performance features and a heavily weighted upside. Many believe that divergence will persist, and may even widen (Cheffins, 2003). Propagators of convergence theory believe that changes in ownership structures, a global labour market, cross-border mergers and acquisitions, and disclosure laws will make convergence inevitable. Differences in cultures and socio-political practices may however work against such convergence. What seems more practicable is a convergence at the level of

remuneration and governance principles, but with an element of flexibility at the level of specific practices and control measures, to allow for environmental differences.

With regard to the role of activism in executive remuneration, Romano (2000) records that it presents only a small fraction of the total focus of activism. They suggest that it is not always in the interest of shareholders to pursue an activity which would publish competitive information to rival stakeholders. It also demoralises management, which in turn could lead to poorer performance. Romano (2001) supports this view by reference to three studies in this regard.

- Johnson, Porter and Shackell: Compensation levels and sensitivity of pay to performance decreased for firms targeted by activists, but no significant effect was found on compensation or performance.
- Thomas and Martin: Compensation of targeted firms did not increase as rapidly as others, but the difference is not statistically significant.
- Prevos and Wagster: Shareholder activism involving executive compensation is non-value maximising, because availability of information puts pressure on pay-for-performance sensitivities.

These studies however focused on the outward manifestation of activism rather than also considering the fundamental principle upon which activism, as a governance control measure, is founded. What is important at a principled level is that stakeholders should have symmetrical information to that held by executives, in order for them to make informed decisions. This does not mean that they would in all instances differ from or influence executive actions, but

that stakeholders would have equal information to make informed decisions to protect their interests effectively.

5.6 Conclusion

This is an interesting time to be involved with executive remuneration, when new corporate governance standards and increased activism play a developmental role that transcends traditional executive remuneration into a new paradigm (Chingos, 2004). Companies are pro-actively considering wider stakeholder perspectives in both remuneration philosophy and planning, and are seeking stakeholder input earlier in the process.

Well publicized corporate collapses and scandals of late have focused attention on executive remuneration. This has led to increased importance and consideration of corporate governance measures to curb executive greed. Executive responsibilities are often better defined, penalties spelt out more clearly, and corporate watchdogs appointed. Handy (2002) however argues that these measures amount to nothing more than plasters on an open sore. What needs to be addressed is the cause of this disease that lies at the heart of corporate culture and governance, rather than the symptoms.

Bebchuk (2002) explains that a combination of remuneration design flaws and overwhelming executive power and control in the pay-setting process, may give conflicted executives the opportunity to skim wealth from shareholders, while disguising it in complex remuneration structures. This would obviously increase the extent of the agency problem in corporations. There are however promising

indications that global executive remuneration practices are converging towards a system where dispersed owners become more activist in monitoring executive actions. One of the reasons advanced for this phenomenon is the increased access to relevant information caused by increased disclosure requirements (Ferrarini, *et al.*, 2003). There is a growing belief that the increased access to comparative information resulting from disclosure makes it possible for companies to link executive remuneration not only to own firm performance, but also to the performance of rival firms (Rappaport, 1999), always bearing in mind that this would ensure executive reward for real long term performance rather than as a result of generally favourable market conditions.

Goold (1996) proposes that the processes of incremental learning and deliberate planning should be intertwined throughout the organisation to achieve sustainable growth. This is particularly relevant in the learning process in respect of executive remuneration setting processes, and the consequent implementation of good corporate governance mechanisms to ensure alignment of interests between owners and executives, and reduce or eliminate related conflicts of interest. But the author warns against taking planning too far until it becomes strict and invasive regulation, which is dangerous. He adds that the required perspective in the ever changing field of executive remuneration should rather be managerial ("what should be done now"), than historical ("how did this situation arise"). A case in point is the strict executive remuneration regulations contained in the Sarbanes-Oxley Act in the USA, which did not prevent powerful executives from large scale abuses and wealth skimming by circumvention of the strict prescripts of law.

Strategic management thinking is required to work out appropriate responses to changes in executive remuneration, corporate governance reform, and globalisation. A good starting point is to establish a framework of underlying principles which ought to inform all corporate governance and executive remuneration practices, and to build situation appropriate mechanisms and practices within such framework for individual organisations or jurisdictions. It is encouraging to note that the King III Code in South Africa has moved towards such a principled approach, away from the previous mere compliance tick-box approach. The comprehensive practice notes to King III sets out best practice standards as a flexible guideline and sense check for South African organisations to consider in the process of designing appropriate practices and control measures in their businesses.

6 DISCLOSURE OF EXECUTIVE REMUNERATION

“Improvement of corporate governance standards has been at the forefront of international debate in recent times, and compensation of directors and executives is a key issue in this debate. Adequate disclosure is widely recognised as the linchpin in effective regulation governance practices.”

(Hill, 1997:60)

The general un-observability of executive actions often leads to information asymmetry in relation to corporate information. Holström (1979) suggests that a natural remedy to this problem is to invest resources into the monitoring of executive actions, which causes agency costs. Healy and Palepu (2000) aver that this information asymmetry and agency conflicts between managers and shareholders create a need and demand for disclosure. They however suggest that, in view of the virtual non-existence of empirical research on the regulation of disclosure, that it is necessary to consider whether disclosure presents investors with new and timely information, and if so, what the cost-benefit results thereof would be. Blair and Ramsay (1992) add that it is not in the interest of investors to disclose information if the cost outweighs the value thereof.

Disclosure therefore always presents choices between costs and benefits for both the organisation and its stakeholders. As with most other aspects of corporate governance and executive remuneration, it is often required to apply art rather than science to resolve these choices.

The most fundamental requirement for reporting on executive remuneration is transparency. The concept of transparency has however not been universally accepted, and the extent of transparency to an even lesser degree. In many countries disclosure and transparency of remuneration is still against the prevailing culture, while in others a clear distinction is made between transparency and illumination (ICGN, 2002). There is consequently little consistency around the world regarding disclosure practices. Although there has been a global trend towards more disclosure of executive remuneration policies and levels in recent years, it has been at the expense of clarity and simplicity. The complexity that often characterises modern disclosures has led to a general lack of proper analysis and monitoring by investors and analysts alike. This lack of clarity and simplicity in disclosure of executive remuneration often leads to investor and stakeholder distrust of companies, and as has been disclosed in the McKinsey report (2002) to consequent unwillingness of investors to invest in companies where they have lacking information in. Most corporate governance codes advocate that transparency is the basis on which trust between the company and its stakeholders is built.

Ferrarini, *et al.* (2003) propose that there are two prominent issues in the disclosure debate, namely whether disclosure remedies or aggravates executive remuneration problems, and whether disclosure amounts to additional agency costs. Although both of these issues are directly relevant in the executive remuneration debate, it is fair to question whether it presents a *numerous clauses* of issues to be considered. Ablen (2003) goes further to suggest that disclosure of executive remuneration policy and levels is significant in that it articulates the pay-setting process, and allows for executives to be held

accountable for their actions. The author adds that disclosure has both intended and unintended consequences. The intended consequences of disclosure consist of the informative value and regulatory technique thereof, while the unintended consequences relate to privacy deprivation and ratcheting pay benchmarking practises. Ablen concludes that informed and active shareholder oversight, enabled by sufficient disclosure, is required to balance these consequences. Although the principle of disclosure as a corporate governance control measure is sound, differences between environments of companies would conceivably require differences in the form and extent of their disclosures.

This chapter analyses the underlying reasons why companies may need or choose to make disclosures, as well as the factors which influence differences in the form and extent of these disclosures. It also investigates modern trends in disclosure practices.

6.1 *The reasons for disclosure*

Aboody and Kasznik (2000) hypothesize that corporate information asymmetry leads to executives opportunistically manipulating the timing of information disclosures to advance their own interests. In particular, executives have the power and opportunity to delay publication of good news and rush publication of bad news to gain maximum benefits for themselves. Such a strategy results in a decrease in stock value before awards to executives and a rise of value after the executive awards, and consequently in financial gains to the executives. Becht, *et al.* (2005) consider such a practice as self-dealing.

The need for mandatory disclosure has been the subject of considerable theoretical debate. Some commentators have questioned the value of mandatory disclosure rules by suggesting that unfettered market forces will produce optimal disclosure. Others argue that disclosure is necessary to overcome market failure (Blair and Ramsay, 1992). The authors list the arguments for and against voluntary disclosure as appear in Table 2 below.

Table 2: Arguments for and against voluntary disclosure

FOR DISCLOSURE	AGAINST DISCLOSURE
<ul style="list-style-type: none"> • Increased management credibility • Increased share value • Increased number of investors • Increased analyst following • Improved access to capital • Increased PE ratios • Decreased share volatility • Increased share liquidity • Improved relations with suppliers • Reduced political intervention 	<ul style="list-style-type: none"> • Disclose proprietary information to competitors

Holburn (2007) states that the disclosure of executive remuneration has produced both positive and negative effects in that it provides shareholders with sufficient information to evaluate executive remuneration practices and levels, but simultaneously creates a potential negative ratcheting effect of benchmarking against other disclosed executive remuneration levels. This does not mean that disclosure should be avoided, but rather that a balancing approach is required, based on the individual situation of the company.

Hill (2006) lists three basic reasons for disclosure of executive remuneration. Firstly, disclosure could regulate the risk of self-dealing and conflicts of interest. In this regard it reduces the opportunity for concealing self-dealing abuses by

executives, promotes executive accountability for corporate performance, and creates a corporate environment characterised by fairness, rational and open policies, and good labour relations. Secondly, disclosure is less interventionary than other methods designed to control executive remuneration, such as statutory limits for remuneration. Thirdly, disclosure protects investor confidence and interests. The King II Report in South Africa suggests that the adoption of a philosophy of disclosure has at least two primary benefits. Firstly it has a shrinking effect in that it deters the incidence of malpractice and excessive executive rewards. Secondly it highlights misconduct and non-performance. It therefore encourages increased disclosure levels to an extent greater than what is required by the statutes. What seems beyond debate is that proper disclosure both reduces the opportunity for abuse and also uncovers instances of abuse, which highlights its potential effectiveness as a multi focused governance control measure.

There is a general acceptance amongst commentators that the fundamental reason for disclosure of executive remuneration is to provide accurate and timely information to shareholders to protect their interests against agency-related problems (Ablen, 2003). Ferrarini, *et al.* (2003) adds that, in view of the high complexity of the executive remuneration setting process, inaccurate or untimely disclosure of information may detract from shareholders' ability to perform proper oversight over executive actions, which could create opportunities for self-serving executives to manipulate the pay-setting process by virtue of their positional power. Effective and timely disclosure will however induce and enable shareholder activism and control.

However plausible this might sound, the benefits of increased activism should be weighed against possible negative public and political reaction to executive remuneration levels and practices. This might materialise in direct labour reaction, or conservative pay-setting in fear of such reaction. Mongalo (2007) cautions that excessive increases in executive remuneration, and the timing of the announcement thereof, could have a negative impact on the morale within the company, which could lead to labour instability. A fair balance needs to be found. Ferrarini, *et al.* (2003) suggest that disclosure which makes it easy to assess the link between executive remuneration and performance will not generally attract adverse reaction to the pay-setting process, and will remedy some of the structural and process weaknesses of the executive remuneration setting process. In this regard, disclosure has increasingly become a key mechanism for managing executive remuneration across the world (Ferrarini and Moloney, 2005).

Ferrarini and Moloney (2005) suggest that effective corporate governance in both dispersed ownership and block holding companies depend on effective disclosure to induce boards to justify executive pay and hold executives accountable for their performance. They add that such disclosure leads to informed shareholder activism, which in turn leads to deterrence effects and lowered agency costs. The flexibility that can be applied within a disclosure framework, allows for a cost-effective way to provide shareholders with the company-specific information needed in order for them to protect their interests in a limited and less invasive manner than would be the case under legislative regulation.

The benefits of disclosure of executive remuneration should however be weighed against any possible disadvantages. One of the possible disadvantages could be the direct or indirect costs of disclosure. Direct costs include cost of recording, processing, auditing, printing and reporting, whereas indirect costs are incurred when useful information cannot be published for some legitimate reason (Blair and Ramsay, 1992), or as a result of public or political pressures (Murphy, 1994). Some would argue that the invasion of executives' privacy through disclosure of their remuneration packages would be justified in view of their accountability towards the shareholders in the corporation. Slane (1997) however questions whether a less invasive mechanism could not achieve the same result. He suggests that disclosure of executive remuneration could cause the internal dynamics of a company to be upset through personal rivalries, reduced morale, and embarrassment. He therefore proposes a disclosure regime in terms of which shareholders have the choice whether to require disclosure or not. This option would however not be available in any of the many systems where public companies are compelled to disclose executive remuneration by virtue of different listing requirements.

Slane (1997), after acknowledging the corporate governance motivation in favour of disclosure, lists the invasion of executives privacy, the fear of undesirable attention, additional reporting costs, potential ratcheting effects, and practical challenges in a company's ability to attract, motivate and retain key executives, as potential disadvantages of disclosure of executive remuneration. Ablen (2003) however argues that, although the invasion of executives' privacy is a common argument against disclosure, that public interest, such as elimination of conflicts of interest and self-dealing, should far outweigh any

private considerations. This view is in accordance with an Australian court judgement in *Re Australian Newsprint Mills Ltd (1988) 6 ACLC 1205*, where the court rejected the argument that a company should be relieved of its disclosure obligations because of the possible invasion it would cause to an executive's privacy. Blair and Ramsay (1992) refer to the following quote from the second reading of the Corporate Law Reform Bill (No 2) of 1992 to indicate the importance attached to disclosure rules by the Australian government:

“The government considers it essential that there be timely disclosure of relevant information about the financial position and prospects of entities in which Australians invest. It is essential to enable informed judgement on investment decisions, whether made by individual Australians or by large institutional investors. In every case the principal is the same – disclosure of relevant information and access to such information, either directly or through advisors, is necessary to ensure an equitable and efficient investment system. In essence, a well informed market leads to greater investor confidence, and in turn to a greater willingness to invest in Australian business.”

Ferrarini, *et al.* (2003) summarises that the role of disclosure in remedying agency costs lies in the fact that it may sharpen shareholder monitoring and activism, and the exposure of executive remuneration to public scrutiny may induce executives to exercise greater care. The ultimate rationale for disclosure is therefore either informative (to present information investors need for decision

making purposes) or regulatory (to monitor execution actions and to protect shareholder interests). Murphy (1994) states that disclosure is therefore not meant to know what executives are paid, but rather to monitor their performance for, amongst others, remuneration purposes. The King II Report aptly refers to this last mentioned characteristic as a “shrinking effect”. It also adds that there is a need for increased and informed shareholder activism in South Africa, similar to those in the USA and UK where activists have had a significant impact on the behaviour of companies and executives. The report records the current inertia of South African shareholders for being responsible for the non-enforcement of the breach of duties by executives. The absence of effective and informed shareholder activism in South Africa therefore seriously undermines good levels of executive compliance to corporate governance principles.

Literature has decidedly focused on the symptoms for disclosure rather than the underlying principle it seeks to address, namely the protection of stakeholder interests through symmetrical information. This principle seems correctly to be unchallenged. It is however the balance between intended and unintended, or positive and negative, consequences that need to be balanced in individual organisations. In order to find an optimal balance, it is necessary for organisations to understand not only who their stakeholders are, but also the different needs and interests that these different stakeholders may have. This is a strategic decision which requires dedicated focus and informed activism.

6.2 The nature and extent of disclosure

Conyon, *et al.* (1995) aver that the current extent of corporate disclosures is woefully inadequate. Disclosure of relevant information is often discretionary. The lack of disclosure consistency does not always facilitate adequate comparisons within even the same industry.

Ideally, disclosure of executive remuneration should enable investors and analysts to understand the nature, expected outcomes, costs and benefits of remuneration policies, and the link between executive remuneration and performance (ICGN, 2002). There is however currently significant inconsistency amongst countries in respect of their disclosure regimes and requirements, which do not always allow for informed stakeholder decisions. Often the devil is in the detail insofar as disclosure is concerned with making sufficient information available to enable shareholder decisions. Ablen (2003) state that shareholders have a legitimate interest in the disclosure of all elements of executive remuneration, as it controls agency conflicts by allowing shareholders to gage the level of divergence between shareholder and executive interests, and the link between remuneration and performance. Successful disclosure therefore rests on its ability to convey meaningful information that is useful to stakeholders to protect their interests.

The form of disclosure is as important as the content thereof. It should be simple, clear and standardised to make it comprehensible. Hill (2006) however suggests that self-serving executives would often disclose executive remuneration in exceedingly complex manners to camouflage any traces of self-service. Contentious aspects of executive remuneration are for example often

disclosed in the chairman's reports in the annual reports of companies, in order to escape shareholder votes thereon. This is indicative of the inherently conflicted arena within which executive remuneration is determined and disclosed, and the significant positional power enjoyed by executives, who are often resistant to full disclosure.

A system of mandatory disclosure should ensure that all stakeholders have equal access to information, and should present simplified and standardised information that is easily understood (Blair and Ramsay, 1992). This statement is however based on two assumptions that have been criticized before, namely that ill-informed investors need protection, and that additional disclosure is the appropriate form of protection.

Hill (2006) further contends that developments in executive remuneration practice, some of which are directly attributable to the attempts of executives to hide their self-service in complex systems, have outpaced the required developments of traditional legal and governance frameworks, which should be developed to deal adequately with modern remuneration practice credible. Such a development is without a doubt, necessary in view of the statements in, amongst others, the Greenburg Committee Report in the UK, and the King II Report in South Africa, that disclosure of executive remuneration is the key means to promote corporate accountability and legitimacy.

The disclosure requirements under the SEC rules in the USA is viewed by Hill (2006) as the international best practice benchmark. These rules require, amongst others, that the board, through a remuneration committee, should

report annually to shareholders on the company's remuneration policy, individualised executive remuneration levels, and all components of executive remuneration packages, in standardised tables and graphs. The underlying principle is that disclosure is not meaningful *per se* unless it is presented in a clear, comprehensible and comparative form, and in a meaningful context which enhances managerial accountability. The approach in terms of the SEC rules is however strongly prescriptive in terms of specific governance control measures which may not be practical universally. A principled approach, supplemented by a flexible set of best practice guidelines, as preferred in the King III Code in South Africa, is more suited to be applied across diverse organisations and industries.

Donham (1922) already suggested that there are vast learning opportunities in the disclosure of information. According to the author, information is king, but only to the extent that it is sufficient to lead to meaningful action. Epstein and Roy (2005) state that disclosed information should enable boards to determine whether executive remuneration strategy meets its objectives, and figures alone will not achieve this. The popular practice of companies to disclose only remuneration levels instead of the factors which have informed those levels is therefore highly questionable.

In some European countries it is still a prevailing culture to disclose the minimal required information. Ferrarini, *et al.* (2003) ascribe this to entrenched cultures of non-disclosure, and corporate ownership structures characterised by block holding, but suggest that there are some indications that European companies are converging towards fuller disclosure similar to levels in Anglo-American

systems. The comprehensive disclosure requirements contained in the UK Combined Code is indicative of this shift.

Ferrarini and Moloney (2005), after studying the disclosure regimes across a number of EU countries, conclude that there are two distinct groups in respect of disclosure systems. On the one hand there are countries such as UK, France, Ireland, Italy, the Netherlands and Sweden which require maximum transparency, detailed and individualised remuneration disclosures, full disclosure of remuneration policy, and a remuneration governance system based on the “comply or explain” principle. On the other hand the remainder of EU countries such as Germany, Austria, Spain, Belgium, Luxembourg, Denmark, Finland, Greece, Portugal, where companies are generally characterised by block holding ownership, require minimal, aggregate disclosure of total executive remuneration, which is attributable to prevailing privacy and cultural preferences. The predominance of aggregated disclosure across the EU, combined with inconsistent disclosure practices, makes accurate direct remuneration comparison, and determination of pay trends very difficult. The authors however observe that less sophisticated disclosure practices were directly linked to governance failures. They therefore conclude that full disclosure is the link between executive remuneration design flaws and effective corporate governance, as well as between pay and performance.

These two different disclosure systems seem to be representative of a similar distinction across the world. Finsch (2006) refers to the relatively new mandatory full disclosure system in Australia, which requires annual disclosure of both executive remuneration policy and individualised levels of remuneration

linked to performance criteria, by all listed companies. The author concludes, after a study of Australian firms listed on the ASX in 2006 that there is a high degree of uniformity of disclosure amongst Australian firms, and a much higher quality of disclosure amongst those firms with a higher market capitalisation. In New Zealand however, Sheffield (2007) found that the minimal disclosure requirements in the country were not aligned with international best practise, which potentially impacted on New Zealand companies to remain competitive in the market for executive talent.

Shim (2006), in accepting that full disclosure has both advantages and disadvantages, proposes a hybrid model for disclosure, in terms of which voluntary codes would be supplemented by formal legislative regulation if companies do not disclose adequately in accordance with its own circumstances. The legislative imposition of maximum caps to executive remuneration in the USA in 2009, following federal support to companies struggling to survive the global economic meltdown of the time, is a prime example of how public opinion influences legislative interventions. Self serving executives have become the frog in the pond, and society is cooking the water by means of increased legislation and regulation.

The question could however be asked whether legislation is a practical a tool to supplement a voluntary code, or whether the opposite is the case. In most instances, legislation sets out the minimum formal requirements (“letter of the law”) while codes set out practical guidelines to give effect to such legislation (“spirit of the law”). Although it is inevitable for legislation to be imposed where codes and self regulation fail to encourage required actions from executives, it

seems unlikely that formal legislation would ever serve to support voluntary codes as a form of governance regulation.

Irrespective of which disclosure regime is in operation in a country, disclosure is often flawed because it is either incomplete, piecemeal or unclear in its reach. Hill (2006) argues that any disclosure regime that does not fully disclose a company's remuneration policy and individualised executive remuneration packages, to which information shareholders have a legitimate right, is fundamentally flawed in that it leads to inequities in respect of access to information, and consequently to agency problems. Adequate disclosure could serve a vital role in addressing these flaws. Meek, *et al.* (1995) composed a voluntary disclosure checklist, copied as Annexure D hereto, which contains 85 items in 12 sub-groups of 3 groups. This list is a most helpful tool towards the design of an effective disclosure system for a company. These items should however only serve as a guide from which companies design disclosures that are appropriate for their individual needs.

Disclosure in itself is however never sufficient as an effective governance tool, but needs to enable shareholder action and activism to reap the benefits intended for shareholders (Mongalo, 2007). The interaction between different corporate governance measures, as have been developed in the model contained in Annexure B, underscores this view. In addition, it is important to consider the most appropriate time for disclosure of information. Although continuous disclosure contributes to transparency and openness, it could force a short term view of performance which might not contribute to the long term sustainability of the organisation. Furthermore, disclosure of information on

executive remuneration on inopportune times may lead to resistance and mistrust amongst employees and other stakeholders (Ablen, 2003).

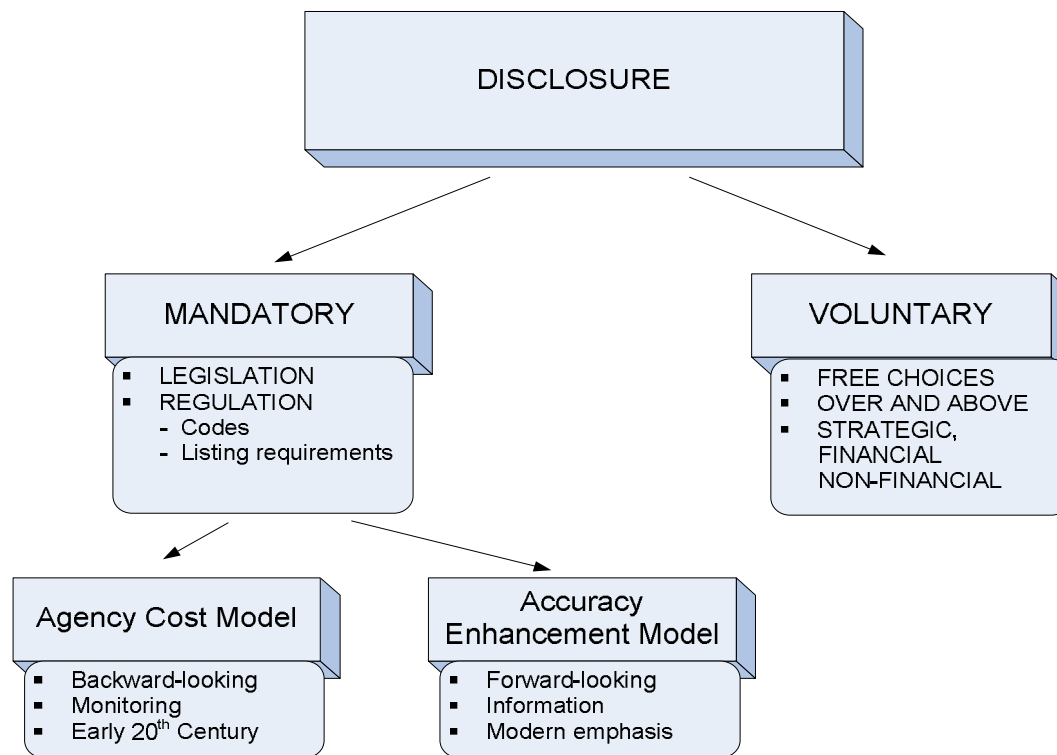
In the UK it became clear that the disclosure regime under the Greenbury Report of 1995 did not achieve the objectives of transparency, accountability and linkage of pay to performance. As a result of this improved regulations were promulgated in 2002 for disclosure of executive remuneration, which left the determination of executive remuneration levels, and the disclosure thereof, to individual companies, within a strictly “comply or explain” regulatory framework. These regulations have now been incorporated in the UK listing requirements. The impact of these changes was immediately observable in terms of preparedness by shareholders to act against ineffective remuneration committees. The success of this increased shareholder activism seems likely to spread very quickly across the world.

Spanos (2005) explains the “comply or explain” principle, which features prominently and increasingly in countries following the Anglo-American model of remuneration governance, as a principle that forces companies to formally disclose the reasons for any deviation from prescribed governance practices. Bhasa (2004) supports this principle on the basis that differences countries in political, economic and governance structures in different countries make it highly unlikely for a complete convergence to an identical governance structure across the world. The author adds that it would not be appropriate to simply copy an existing governance structure from one country to another, without making the necessary changes to accommodate differences in structures and needs. He described the current trend towards convergence in terms of outsider

mechanisms to address executive remuneration problems as an economic fad which would come to pass once the realisation sinks in that compliance with it will never be complete. This insightful view highlights how the current popular reform focus on specific control measures that address problematic symptoms of governance failures, rather than on principles that directly address the causes of governance problems, will not provide sustainable solutions in the long run.

Mahoney (1995) contrasts two distinct models to explain the nature and justification for disclosure. The “accuracy enhancement model” contributes to information efficiency by enabling investors to have access to the relevant information they need to base their investment decisions upon. This model, according to the author, has no competitors as an efficiency justification for disclosure. Although critics have not challenged this model, they have questioned whether laws have achieved what is intended under the model. In contrast, the “agency cost model” contends that the principal purpose of mandatory disclosure is to address agency costs that arise from the separation of ownership and control. It is therefore clear that the “agency cost model” justifies the traditional backward-looking model of mandatory disclosure, whereas the “accuracy enhancement model” presents forward-looking information that facilitates informed investment decisions. Figure 7 below sets out this disclosure model.

Figure 7: Disclosure model



The distinction between the “agency cost” and “accuracy enhancement” models seem plausible. The following aspects should however be considered in the design of an efficient disclosure system.

- Agency information is limited in scope, not costly to produce, and relevant across firms. Accuracy enhancement information is vast, complex and varies significantly across firms, and is costly. Therefore, a disclosure system based on accuracy enhancement is much more costly, but its social benefits are greater.
- Mandatory disclosure is a plausible solution to the limited set of agency problems it was originally meant to address, but not to the more general problem of information asymmetries among stakeholders. It was fine for

traditional 19th century needs, but as a result of significant developments and globalisation, it has to change.

- Forward looking disclosure can be unregulated because it has nothing to do with the agency problem. Individual firms could decide the extent of its disclosure.
- The accuracy enhancement model of mandatory disclosure explains why a disclosure system that required disclosure of all value relevant information simultaneously to the whole market could be efficient. The fact that mandatory disclosure started off as a means to monitor agency problems does not mean that it should not be extended to achieve the goal of accuracy enhancement if it can do so cost effectively.

It appears that the international trend is to view financial information as being backward-looking in terms of the “agency cost” model, but that stakeholders increasingly require forward-looking information to enhance their decision making abilities. This will require companies to publish, at least in its annual reports, information relating to how the operations of the company have impacted both positively and negatively on the economic and social environments within which it operates, and how the company intends to improve thereon.

Ferrarini, *et al.* (2003) concludes that disclosure is only a tool in the process of establishing good corporate governance in a firm, and not a corporate governance measure in itself. It is unable to achieve any results itself, but leads to significant action if it is clearly and timely, and assists shareholders and investors to make informed decisions. This supports the inclusive view of

corporate governance depicted in Annexure B. Sethi and Emelianova (2006) support the view that there is a need to develop a disclosure framework within which companies could find an appropriate balance between flexibility and regulation. They outline the following steps that are required in the process:

- Establish clear-cut best practice standards;
- Establish minimum standards of conduct;
- Review policies and practices from compliance with minimum standards;
- Develop aligned internal codes;
- Create criteria for performance evaluation; and
- Ensure maximum transparency in public disclosures.

Although this approach is plausible, it ought to follow as a next step after the formulation of those principles that underpin and inform disclosure as a governance control measure.

6.3 *Disclosure trends*

While corporate governance rules are often controversial, most observers agree that disclosure forms an integral part of any corporate governance framework (Berglof and Pajuste, 2005). Despite a pattern of emerging capitalism around the world, which is, amongst others, characterised by controlling shareholders and elements of entrepreneurialism, there is still substantial differences in disclosure practices. Strong country effects are evident. One of the main reasons for such differences is the trade-off that is often required between costs and benefits. Some of the other influencing factors are firm size, financial

leverage and asset structures (Chow and Wong-Boren, 1987), as well as the regulatory environment and cultural beliefs.

Blair and Ramsay (1992) suggest that the USA requirements for disclosure constitute an international benchmark. The current disclosure dispensation in the USA is derived from a major revision of the SEC rules in 1992, to include a summary compensation table, which identified all components of executive remuneration. It recognises that information given in context is more meaningful. In many ways these disclosure arrangements have been copied, albeit to different extents, into other countries. The European Union adopted disclosure directives that prescribed minimum standards for transparent disclosures. Some individual states have voluntarily taken on additional disclosures. Rules are however not strictly enforced, and Annual Reports commonly show that countries in Central and Eastern Europe do not always follow disclosure laws and regulations. Again, the focus is on individual control measures, which may not be ideal to copy from one environment to another. Instead, principled frameworks allow for flexibility in selecting the best mix of control measures for a given situation.

There are ever increasing calls for more extensive disclosure requirements along the lines of SEC requirements in the USA, in an attempt to keep managers, boards and especially remuneration committees on their toes to avoid public scrutiny or embarrassment. These benefits however have to be considered carefully against the additional costs it could generate, and the risk of causing a ratcheting effect of executive remuneration levels generally (Lowenstein, 2000).

Following escalating executive pay levels and an increased focus on justifying executive pay practices since the mid 1990's, shareholders in Europe have been demanding more comprehensive information on executive remuneration levels, compensation package designs and performance assessments for business executives. In October 2004, the EU Commission therefore recommended that companies disclose their policies on executive remuneration, as well as the levels and composition of individual executives' remuneration packages, to ensure that shareholders are given adequate information and control over executive remuneration schemes (Roberts, et al, 2007). Countries such as the UK, Ireland, the Netherlands and France now disclose individual executive remuneration packages as well as remuneration policy information, while countries such as Finland, Spain, Portugal and Denmark still only provide aggregate compensation disclosure with limited policy information. Table 3 below indicates the current and expected future disclosure practices in the most prominent European countries, while Annexure G presents a more detailed comparison of executive remuneration disclosure practices across Europe.

Table 3: European disclosure trends

Current disclosure	Level	Country	Anticipated future disclosure
Individual disclosure Detailed pay policy	High	UK Ireland Netherlands France	More information required on the link between pay and performance, and a focus on peer groups
↑	Medium	Sweden Germany Switzerland Italy Norway	Pressure to disclose information on individual board members rather than just the CEO/highest paid executive, with more information on remuneration policies
Aggregate disclosure Limited pay policy	Low	Finland Spain Portugal Denmark	Pressure to provide individual disclosure and increased information on remuneration policies

(Roberts, et al, 2007)

Although the EU Commission recommendations rather constitute guidelines, which could be adhered to voluntarily, than strict legal prescriptions, the Commission stated that it would closely monitor the application of its recommendations to identify whether additional measures might be desirable in future. Roberts, *et al.* (2007) quote as follows from the EU Commission recommendations: *“Proper disclosure and giving shareholders effective control are essential to restore confidence in EU companies and securities markets. But we are not interfering in companies’ internal affairs or individual decisions on remuneration. This is about providing guidance to Member States in ensuring that shareholders know what is going on and can get things changed if they do not like them.”*

These EU Commission recommendations cover the following four areas:

- **Remuneration policy.** All listed companies should publish a statement of its policy on executive remuneration for the following year. The information should include a breakdown of fixed and variable remuneration, performance criteria and the parameters for annual bonus schemes or non-cash benefits. The statement should also explain the company's contract policy, but companies do not have to disclose commercially sensitive information.
- **Shareholders’ meeting.** The executive remuneration policy should be on the agenda of the shareholders’ general meeting. To increase accountability, the policy should be submitted to a shareholder vote, which may be either binding or advisory.

- ***Disclosure of the remuneration of individual executives.*** Disclosure of each individual executive's remuneration should include at least detail regarding the cash compensation and perquisites of individual executives, stock or options granted to executives, contributions made to pension funds, and any loans, advances or guarantees made to each executive.
- ***Approval of stock awards and stock option plans.*** Variable remuneration plans under which executives are paid in shares, options or any other entitlement to acquire shares should be subject to prior shareholder approval at the annual general meeting.

There has been an increased focus on disclosure of executive remuneration in both the USA and almost all European markets since the much publicised corporate failures of late. This could be ascribed mainly to increased shareholder and broader stakeholder activism in the area of executive remuneration. The strict disclosure rules adopted by the USA through the Sarbanes-Oxley Act and SEC Rules may also drive changes in some European countries in this regard. The US changes primarily led to increased disclosure requirements and a focus on executive earnings during the year, with more detail demanded about how and why compensation was awarded and more transparency regarding peer groups used for benchmarking of executive remuneration packages and levels.

Table 4 below indicates the current drivers of executive remuneration disclosure developments in European countries.

Table 4: Drivers of executive remuneration disclosure reform in Europe

Country	Current disclosure drivers
Denmark	The Copenhagen Stock Exchange has released good practice guidelines requiring a greater level of disclosure. To date, few companies have complied with these guidelines.
France	President Nicolas Sarkozy presented a draft law to parliament directed at curbing excessive executive severance arrangements and focusing on performance-related pay, new rules on stock options and greater transparency. Some companies in France currently provide information well beyond the disclosure requirements.
Germany	For the first time in 2006, annual reports of listed companies had to disclose individual executive compensation practices. Only a small number of companies are providing full disclosure. Germany is one of the few countries with a binding vote on executive pay.
Ireland	The disclosure requirements in Ireland are similar to those that were in place in the UK a few years ago. Therefore, a move toward the current UK levels of disclosure is expected.
Italy	An increase in disclosure of performance plans, compensation philosophy and long-term incentive values and criteria, in accordance with the recent regulations of the "Consob" Authority, is observed.
Netherlands	In December 2006, the Dutch Monitoring Committee Corporate Governance Code advocated more uniform disclosure of executive compensation practices in annual reports, with more transparency and a clear link between pay and performance.
Norway	The Norwegian code of practice on corporate governance recommends detailed remuneration disclosure. It is fairly new so not all companies have taken all the recommendations into consideration or implemented them fully. The main corporate governance principle is to "comply or explain." A move toward the level of UK and US disclosure practice, with more transparency and details on incentives, policies and peer groups, is expected.
Portugal	Companies listed on Portugal's stock exchange are obliged to disclose executive compensation, but many are failing to do so. The stock market regulatory authority, CMVM, will presumably increase enforcement of executive compensation disclosure over the coming years.
Spain	Increased public scrutiny and forcing them (and others) to pay closer attention to compensation issues and disclosure.
Sweden	Companies currently provide this information only for the CEO, with other executives' pay provided as an aggregate amount. Nordic countries move toward the level of US disclosure.
Switzerland	Some major Swiss business leaders have been pushing for a national vote to change Swiss law and provide greater transparency on and accountability for executive pay.
UK	There is already a high level of disclosure required in the UK under the Companies Act and other regulations. There may be an additional requirement to disclose the annual value of long-term incentives, as is required in the US.

(Roberts, et al., 2007)

The United Nations issued a guidance document on good practices in corporate governance disclosure in 2006 (United Nations, 2006). The guidance document is intended to be a technical aid for regulators and companies in developing countries and transition economies, which focuses on widely applicable issues of general application. It draws upon the recommendations for disclosure relevant to corporate governance contained in such widely recognized documents as the revised OECD Principles of Corporate Governance (OECD Principles), the International Corporate Governance Network (ICGN) Corporate

Governance Principles, past ISAR conclusions on this matter, the Commonwealth Association for Corporate Governance Guidelines (CACG Guidelines), the pronouncements of the European Association of Securities Dealers (EASD), the EU Transparency Directive, the King II Report on Corporate Governance for South Africa, the Report of the Cadbury Committee on the Financial Aspects of Corporate Governance (Cadbury Report), the Combined Code of the UK, the United States Sarbanes-Oxley Act, and many others. The recommendations issued under the United Nations guidance document include:

- Directors should disclose the mechanism and process for setting directors' remuneration, as well as its structure and levels.
- A clear distinction should be made between remuneration for executive directors and non-executive directors.
- Disclosure should be comprehensive enough to demonstrate to all shareholders and stakeholders how executive remuneration is linked to the company's long-term performance.
- Disclosure of individual executive remuneration packages should be broken down into components which clearly distinguish between salary, bonuses, pensions, share payments and all other benefits, financial or otherwise, as well as reimbursed expenses.
- Where share options for directors are used as incentives but are not disclosed as disaggregated expenses in the accounts, their cost should be fully disclosed using a widely accepted pricing model.
- All material issues relating to corporate governance of the enterprise should be disclosed in a timely fashion.

- Disclosure should be clear, concise, precise and governed by the “substance over form” principle.

The focus of these guidelines constitute disclosure principles which are flexible enough to apply differently in accordance with individual needs. They could be universally applicable to a greater extent than individual control mechanisms, which may be effective in one scenario but not in another. An increased reform focus on formulating a comprehensive set of these types of principles, supported by flexible control measures, will impact positively on the greater corporate governance systems in organisations. Current reforms focus on specific control measures, which are inappropriately enforced through strict legislative prescriptions, will continue to encourage executives to find loopholes in circumventing these prescripts.

6.4 Conclusion

Although it is common cause that disclosure of executive remuneration forms an integral part of a corporate governance framework, there are still major differences in the approaches to disclosure practices around the world.

Disclosure ordinarily occurs as a result of either legislative / regulatory prescripts (mandatory disclosure) or in accordance with additional individual needs of the organisation (voluntary disclosure). The extent to which an organisation discloses information is informed by what it seeks to achieve by such disclosure. An “agency cost” focus seeks to limit agency costs by monitoring executive behaviour and performance, to ensure alignment thereof

with shareholder interests. An “accuracy enhancement” focus generates and publishes information relevant to investor decision making. Rahman (2002) suggest that a balance should be found by tailoring disclosures to the needs of an individual firm in its operating market, which is often influenced by a cost-benefit analysis for the individual firm.

Effective disclosure is therefore based on an organisation’s understanding that disclosure always requires a balance between competing interests – whether between costs and benefits, different stakeholder needs, or between transparency and competitive advantage. The key to successful disclosure lies in the extent to which those competing interests are effectively balanced.

Most recent reports and commentary on disclosure of executive remuneration view disclosure as perhaps the most important element of best practice in corporate governance in this area. There is a clear international trend, particularly in following developments and practices in the USA, towards more stringent and standardised executive remuneration disclosure rules, which facilitate comparison across different companies and industries (Hill, 2006).

Time will however tell whether this focus on addressing symptoms of corporate governance failures is just another phase or fad. A more sustainable approach would be to focus on the formulation of universal disclosure principles, and to set out flexible guidelines on what control measures may be implemented in accordance to differing needs to address individual problems.

In an attempt to formulate some of these potential disclosure control measures, the ICGN (2002) suggests that companies should make the following annual disclosures in respect of executive remuneration in order to ensure alignment of executive and shareholder interests:

- The remuneration policy applied in the organisation;
- All monetary and non-monetary rewards paid to executives;
- The anticipated link between executive remuneration and performance outcomes; and
- The rights of shareholders to vote on executive remuneration at an AGM.

De Beer (2005) adds the following proposals for a general improvement in executive remuneration disclosure practises:

- There should be increased disclosure of the actual percentiles of fixed remuneration, short term and long term incentives, and a summary of the performance measures and vesting conditions for the payment of incentives; and
- A statement of the governance principles applicable to the award of short term and long term incentives to executives.

It must however be understood that these lists only contain some suggestions which may be supplemented or changed in accordance with what would be most effective in satisfying the desired information needs of different stakeholders. These lists should rather be a secondary focus after the universal principles have been identified and agreed.

Disclosure of executive remuneration *per se*, whether effective or not, is not a sufficient mechanism to ensure good corporate governance and the alignment of conflicting interests in an organisation. Although disclosure may have a shrinking effect on executive remuneration levels, it needs to enable informed stakeholder action and activism to be effective. Herawaty and Hoque (2007) support this view, but add that one of the most crucial difficulties in this regard relates to a general lack of public interest in annual reports. Without such interest, the disclosure of executive remuneration information will not on its own bring balance to the conflicting interests of shareholders and executives.

Although there are still significant differences in the extent to which disclosure is applied in many countries and companies, there are some promising signs of a convergence to a more principled uniform disclosure practice, which still allows for some flexibility within its framework. The King III Code in South Africa is a primary example thereof. Such a development will surely be beneficial to both general corporate governance mechanisms, and global benchmarking of executive remuneration.

7 THE ROLE OF DISCLOSURE OF EXECUTIVE REMUNERATION IN A CORPORATE GOVERNANCE FRAMEWORK

Bussin and Fletcher (2007) ascribe the prominence of executive remuneration as a topical issue in the corporate governance debate to the need by shareholders to understand remuneration structure and processes, and the fact that remuneration committees should ensure that companies comply with both the letter and spirit of the law, in respect of both rules and principles. The increased implementation of corporate governance codes and best practice guidelines has placed executive remuneration central to the corporate governance debate (Ablen, 2003). The focus of attempts to address corporate governance problems associated with executive remuneration has however historically been mainly on eliminating some of the apparent symptoms, rather than on the underlying causes of these problems. Some of these potential symptoms include excessive remuneration and flawed pay setting processes. One of the generally accepted underlying principles of this debate is that companies should remunerate executives fairly and responsibly. This principle has been copied into the King III Code in South Africa as the first and most important of only three principles dealing with executive remuneration. The other two principles require that companies should disclose the remuneration of each individual director and certain senior executives, and that shareholders should approve the company's remuneration report in a non-binding vote at its Annual General Meeting.

Ablen (2003) proposes that, in order for companies to ensure that they reward their executives fairly and responsibly, companies should:

- disclose executive remuneration policy and packages to enable investors to understand the link between performance and reward;
- establish remuneration committees to advise on executive remuneration;
- make a clear distinction between the roles of executive and non-executive directors;
- ensure that executive remuneration is in accordance with shareholder approved pay plans; and
- comply with both the letter and spirit of applicable regulations.

These suggestions clearly have merit, but ought not to be considered as a *numerous clausus* of control measures to ensure compliance with the principle of fair and responsible reward. The issuing of Practice Notes under the King III Code in South Africa, which set out practical guidelines for companies to consider when designing their own frameworks of control measures to comply with the stated principles, is more plausible. The test will however lie in the extent to which companies apply their minds to developing an integrated system of control measures which is optimal for its own situation. The solutions offered by Ablen above, those included in the King III Practice Notes, and any other relevant mechanisms could be considered as potential parts of the individualised solution.

The significant differences in executive remuneration practices across industries and organisations are a clear cause of concern (De Beer, 2005). Any

democratic, capitalist system rests on the economic principle that both individuals and organisations should be left to their own devices as far as possible, but within a flexibly regulated framework. Enforced compliance to strict rules would be undesirable. Nothing however prevents organisations and institutions to suggest best practice guidelines to inform business, while the application thereof is still at the discretion of individual companies. Opportunity for congruence, which probably will link the fields of executive remuneration and corporate governance directly, must be sought.

In South Africa, executive remuneration aspects of corporate governance is in principle informed by the King I, II and III Reports, applicable labour laws, trade unions, activism, accounting requirements, legislation, and JSE listing requirements. It is necessary for companies to know the minimum requirements, as the rules of the game. Ilbury and Sunter (2001) sees this as the first step in a scenario planning process which takes one from a situation of absence of control to one of control, which improves the quality of decision making. For corporate governance to be effective, it needs to ensure such a framework, where different stakeholders could make fully informed decisions to protect their interests in the corporation.

This chapter examines the interrelatedness of executive remuneration, disclosure of executive remuneration and corporate governance, in order to understand how these constructs operate together in an inclusive governance framework in an organisation. In particular, it focuses on the alignment of conflicting stakeholder interests, and effective mixes of internal and external corporate governance control measures, in such a framework.

7.1 *Executive remuneration and corporate governance*

The relationship between executive remuneration and corporate governance is ultimately borne out through the regulatory response in which regimes pursue conflicts of interest, good governance and disclosure practices in modern business (Ferrarini and Moloney, 2004).

The International Corporate Governance Network (ICGN) approved a set of best practice guidelines for global executive remuneration in July 2002. These guidelines are not strict “comply or else” type legislative compliance requirements, but rather serve as best practice guidelines. The ICGN however did not state what governance or executive remuneration principle these guidelines seek to support. Although some of these guidelines may be applicable in most instances, they might not be universally applicable in all situations. A more appropriate suggestion would have been to identify the principles which need to be applied, followed by best practice recommendations which serve to assist organisations in choosing the most appropriate control mechanisms for their individual circumstances. The above ICGN guidelines include:

- Executive remuneration schemes should be designed and managed by remuneration committees composed of independent directors;
- Annual reports should contain board approved remuneration reports, which should in turn include a statement on expected outcomes of the remuneration strategy and structure;
- Remuneration consultants should only be appointed by remuneration committees;

- All components of executive remuneration should be disclosed to investors (including salary, benefits, incentives, perquisites, and other cash or non-cash rewards);
- Key executives should hold substantial, direct shareholding in the company;
- Executive remuneration should be clearly linked to appropriate short and long term corporate performance measures; and
- Share options should not be the only long term incentive.

The relationship between executive remuneration and corporate governance will be best examined by considering how it potentially impacts on the objective of alignment of conflicting stakeholder interests, and in developing an appropriate mix of internal and external corporate governance control measures for specific organisations.

7.1.1 The alignment of conflicting interests

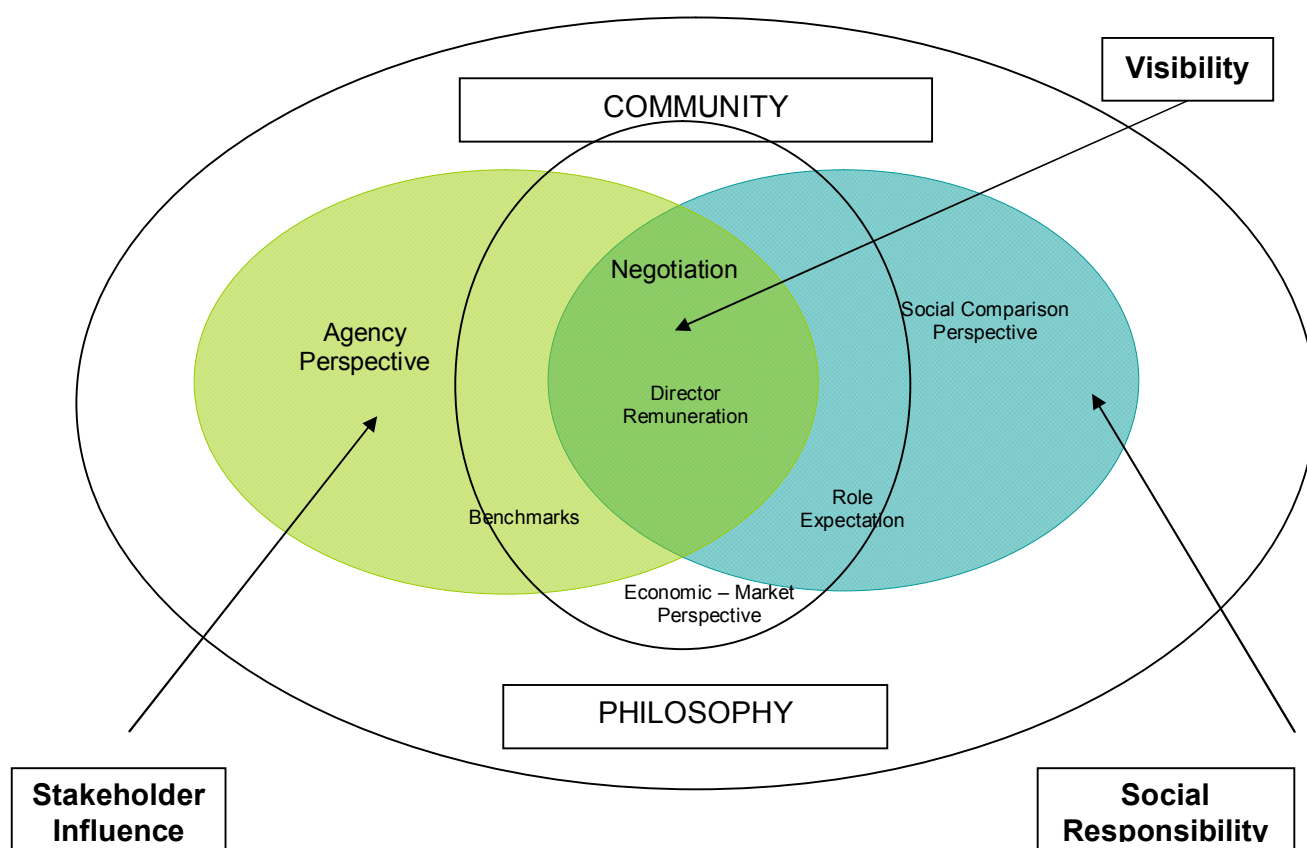
Academics and consultants have over the years developed multitudes of management tools to measure executive and company performance (Epstein and Roy, 2005). Most of these measures are based on the development of strategic objectives and performance measures (financial and non-financial). The Balanced Scorecard is one of the most popular such tools in the modern trend to supplement traditional financial measures with non-financial measures.

The central tenets of agency theory have however proven to be difficult to achieve in practice, and this has caused increased agency costs for

shareholders, who in turn only benefit from a portion of the benefits resulting from executive actions. Martin and Nisar (2007) suggest that investor activists, who are often viewed as interfering bullies with personal agendas, by executives, have the power to influence executives to make strategy and organisational changes, and to change corporate governance practices. They observe that empirical studies have failed to date to demonstrate a link between shareholder activism and company performance, and ascribe this to possible conflicts of interest amongst activists which inhibit their objectivity and engagement, and activist engagements that focus more on institutional change than measurable financial performance. Another reason for the lack of focused success of activists may lie in the extent of information asymmetry between corporations and activists therein. Access to relevant and meaningful information may quite conceivably improve the success rate of activists. The corporate governance model developed in Annexure B demonstrates how effective stakeholder activism is dependent on both effective internal and external corporate governance control measures.

In drafting an executive remuneration model that incorporates broader stakeholder consideration, attention should be given to agency, social comparison and stakeholder theories (Kakabadse, *et al.*, 2004). Figure 8 below sets out the authors' view on how different perspectives of those theories fit together in a single model that seeks to explain executive remuneration.

Figure 8: Geopolitics of executive remuneration



(Source: Kakabadse, *et al.*, 2004)

Pepper (2005) studied the relationship between corporate governance and executive remuneration in France, Germany, Switzerland, the UK and the USA, which he summarises comparatively as set out in Annexure H hereto. He explains that economists have traditionally sought to explain executive remuneration in terms of agency theory, and the separation of ownership from control in corporations. Agency theory suggests that shareholders can exercise control over executives by offering executive incentives intended to align their conflicting interests with those of shareholders, and through monitoring executive actions in terms of good corporate governance practices. The author is of the opinion that agency does not properly explain all aspects of the

relationship between shareholders and executives, and therefore proposes that “ultimate behaviour game theory”, which incorporates systems and procedures designed to show that trust exists between shareholders and executives, as a more complete explanation of the relationship. The added complexity of adding stakeholders other than shareholders to the network of key relationships in an organisation is however not addressed in this suggestion.

Ferrarini and Moloney (2005) state that although many studies have failed to identify the link between bad governance and suboptimal executive pay structures, the link between optimal shareholder interests alignment and good corporate governance, drives current executive remuneration and corporate governance reforms. In this regard, the management of a company benefits from the asymmetry of information that exists between executives and shareholders. Access to relevant and timely information is key to the successful alignment of any conflicts of interest between shareholders and executives. This asymmetry is more acute in organisations characterised by dispersed ownership structures where comprehensive director monitoring and control by shareholders is not possible.

Access to accurate and timely information could lead to increased involvement and activism by investors, who however currently is perceived to focus on only corporate governance improvements, which cannot in itself be associated with superior corporate performance. Although there have been significant global increases in shareholder activism in the field of corporate governance, through both direct engagements and the developments of best practice guidelines, it would not have been possible without full and transparent information.

Despite the recent increase in shareholder activism and interest in executive remuneration, the power of shareholders to challenge executive remuneration plans is generally weak (Hill and Yablon, 2002). Randall (2001) suggests that shareholders actually only have three options to challenge executive remuneration, namely to vote on it, sell their shares, or litigate in court. All three of these options must however be exercised from a locus of informed decision making processes. Access to relevant and meaningful information through, amongst other mechanisms, effective disclosures will play a significant role in this decision making process.

Hill and Yablon (2002) note that there is a widely held view that alignment of interests between executives and shareholders is both desirable and possible, but that the devil is in the detail. They state that the environment for setting of executive pay packages is deficient in that it is firstly not always truly performance related, and secondly often based on inappropriate benchmarks. This position is exacerbated where executives are allowed to insulate their interests against downside risk, by means of, amongst others, the re-pricing of stock options. Aboody and Kasznik (2000) add that executives therefore not only have the incentive to manipulate performance results, but also have the capacity to manipulate it subtly as a result of their advantageous position in relation to disclosure of corporate information.

An alternative view is that executives influence the setting of their own pay as a result of their power positions in the modern corporation (Bertrand and Mullainathan, 2000). The authors distinguish between a contracting view and a skimming view of executive remuneration. Under a contracting view, executives

are paid for performance that is incentivised to achieve shareholder wealth, thereby using executive remuneration to solve the agency problem. Under the skimming view, executive remuneration is regarded as a consequence or cost of the agency problem, with executives effectively setting their own pay and often receiving pay for luck. They conclude that the skimming view is found more commonly in poorly governed firms, whereas the contracting view fits better in well governed firms. Where pay under the contracting view is seen as an attempt to solve moral hazard, pay under the skimming view is seen as the result of moral hazard. Although the manner in which governance control measures have to be designed for organisations in these two scenarios are vastly different, the principle it ought to support being exactly the same, namely fair and responsible remuneration for executives who are tasked to manage stakeholder interests in the organisation.

Despite its shortcomings to explain executive remuneration completely, agency theory remains the most dominant model for determining executive remuneration in dispersed ownership structured companies, where executive remuneration is viewed as a remedy for the agency costs generated by conflicts of interest (Ferrarini and Moloney, 2004). The core question is how wealth-maximizing shareholders ensure that managers with conflicting goals act in their best interest. In agency theory executive incentives are considered necessary to achieve alignment of executive and shareholder interests. The simplest way of doing this, is through performance indicators linked to the known share price of the company's stock as indicator of the future value of the company to investors. This has led to an explosion of incentive-based executive remuneration since the early 1990's, which has popularised the view that

executive remuneration in itself is an agency cost. As such, executive remuneration could be viewed as a symptom of a wider failure to address defects in corporate governance practices, rather than as being the problem *per se*. One possible solution is to not only link incentive to share prices, but to peer group indices (Ferrarini and Moloney, 2004). In doing so, executives will only be rewarded if their contribution to financial and non-financial performance fall above those of competitors. This would be consistent with the view of Ferrarini and Moloney (2004) that there is a closer relationship between governance systems and the sophistication and rigour of the regulatory responses to executive remuneration. Becht, *et al.* (2005) add that incentive pay should also be tied to relative and comparative peer performance instead of only own firm performance. This will eliminate pay for luck under generally favourable market conditions. Gibbons and Murphy (1990) refer to earlier studies which indeed show a negative relation between executive remuneration and industry performance at the same time as it shows a positive relation to own firm performance.

Peer group benchmarking will however only be defensible if the respective benchmarks are firstly objectively appropriate, and secondly set and agreed independently upfront. This would go a long way towards eliminating the potential manipulation of benchmarking by executives. One possible drawback of this approach would be the extent to which appropriate benchmarking data is available to an organisation. Whereas some information would be generally available in respect of publicly listed companies, the same does not apply to private, unlisted companies. Benchmarking of this nature is therefore not always feasible. This does not however mean that it ought to be discarded for all

situations. It may be a highly effective mechanism in benchmarking practices where comparative information is legally available, such as in listed companies. There are however two cardinal disadvantages with using shares and share options as executive incentives, as is the case in an overwhelming majority of incentive design schemes. Firstly, the issuing of shares to executives dilutes shareholder wealth, as it reduces their percentage holding in a company when more shares are issued. Secondly, share options allocations may induce executives to take short term risks, or commit crimes, to maximise their own wealth creation. This risk is significantly increased when there are no downside risks attached to the share option allocations, or re-pricing is allowed. The unequal distributions of risk imply that there is not proper alignment between shareholder and executive interest.

What seems beyond doubt though is that executive remuneration is an essential part of a corporate governance framework. The art thereof however lies in the extent to which control measures are applied to ensure that such remuneration is both fair and responsible, as a tool to ensure that executives manage the organisations in the interests of its stakeholders, and in accordance with performance targets and standards which have been independently and objectively set upfront.

7.1.2 Internal and external corporate governance mechanisms

Corporate law uses three techniques to control conflict of interest in executive remuneration, namely fiduciary self-constraint, corporate governance practices (such as remuneration committees and non-executives directors), and

incentivised alignment of conflicting interest (Hill and Yablon, 2002). Corporate governance reforms of late have tended to prefer the last two options. This paradigm shift has been criticized by a number of commentators at both a theoretical and practical level. At a theoretical level it is argued that the traditional assumptions of agency theory are not always relevant in modern corporations, and that broader stakeholder interests should be considered rather than only shareholder interests. At a practical level, the unclear link between performance and reward is acknowledged, and in particular the lack of downside risk, and external influences on corporate performance. The ICGN (2002) add that it is exceedingly difficult for outsiders to judge with any precision what the levels of executive remuneration in a company should be, but that it is far easier to determine ex post facto, and with the benefit of hindsight, what mistakes or errors of judgment have been made.

Several commentators divide corporate governance mechanisms into two components, namely internal mechanisms that relate to the relationship between directors, executives, shareholders and stakeholders, and external mechanisms that relate to legal, regulatory and administrative frameworks (Bhasa, 2004; Shim, 2006). As a general statement, it seems that external mechanisms such as disclosure are favoured in Anglo-American systems, while internal mechanisms such as remuneration committees are favoured in continental European systems.

The disclosure requirements in the USA and UK are of the most comprehensive around, and serve as best practice benchmark across the world. Pepper (2005), after studying the corporate governance and executive remuneration systems in

a number of EU countries, comes to the conclusion that a global best practice model for corporate governance, as it applies to executive remuneration, is perhaps beginning to emerge. He suggests that a workable combination between existing external disclosure (USA) and internal standards for board independence, effective remuneration committees and separation between the role of CEO and board chairperson, might be the answer, but that only time will tell. The model developed in Annexure B however shows how internal control measures, external control measures, and activism are interrelated in an inclusive corporate governance framework. It may not be appropriate to assume that a particular mix of control measures in one environment would be as effective in another. It would therefore be surprising if any potential convergence to a particular corporate governance structure would extend to a practical level, where there is convergence towards universal application of specific control measures, or even specific mixes of control measures.

The inherently adversarial nature of the executive pay-setting process requires an optimal mix of corporate governance mechanisms to balance the conflicting interest of executives and shareholders in a way that is flexible enough to properly fit in with unique environmental and cultural factors. Whereas internal board dynamics and strict disclosure requirements might be appropriate to establish an alignment of interest towards improved corporate performance in the USA or UK, it might not be equally successful elsewhere without necessary adjustments for unique requirements. Nonetheless, Ferrarini and Moloney (2004) suggest that increased globalisation is causing some measure of convergence to a system that is characterised by both corporate governance framework, and flexibility for individual circumstances. This is consistent with

the view expressed by Hill and Yablon (2002) that neither non-executive directors, remuneration committees or consultants on its own would be a sufficient safeguard against executive superiority and control, but that it has to be fused with all other appropriate corporate governance practices to have a positive effect. This process is greatly enhanced by the increased role of institutional investor and activists, who are more informed as a result of their exposure to relevant and timely corporate information. This acknowledges the three components of the inclusive corporate governance model depicted in Annexure B.

Each individual corporate governance mechanism, whether internal or external in nature, is less than sufficient to address traditional problems in the executive remuneration and corporate governance debates on its own. Core, *et al.* (1999) argue that firms with weaker governance structures have greater agency problems and generally perform worse than companies that foster strong corporate governance practices. Chingos (2004) add that companies with strong corporate governance structures will ordinarily incorporate as many shareholder-friendly features into their executive remuneration programs as possible. However, the impartiality of non-executive directors is questioned, the extent to which boards exercise oversight over executives is not clear, the costs associated with disclosure distracts from its use, and the link between performance and reward is exceedingly complex.

Where a combination of these mechanisms is used however, the likelihood of these risks occurring decreases dramatically. The added likelihood if investor

attraction and activism if such a combination is implemented would be in the long term interest of the corporation and its stakeholders.

7.2 *Disclosure and corporate governance*

Disclosure may be the least costly and least invasive way of intervening in conflicts, by giving sufficient and timely information to shareholders to protect their interest through informed decisions (Ferrarini and Moloney, 2004). Although extensive disclosure requirements are set in the USA and UK through the development of strong codes, legislation and listing requirements, the position is quite different in several European countries, where only minimal or aggregate disclosure of executive remuneration is required. This is based on a long tradition of privacy of remuneration issues, and the belief that the disclosure of executive remuneration could trigger adverse public and political reaction, and uncontrolled ratcheting remuneration increases. Two distinct thought groups have materialised, namely those in favour of full disclosure, and those in favour of limited disclosure.

Although the merits of full disclosure of both remuneration policy and individual executive remuneration packages are increasingly accepted across the world in terms of corporate governance codes and legislation, it is important to assess whether such disclosure remedies or aggravates executive remuneration problems (Ferrarini and Moloney, 2004). It is however important to consider that, although disclosure may aggravate executive remuneration problems in some instances, it may equally remedy it in others. Disclosure should therefore not be disregarded as a potential governance control measure simply because

it could create problems in some cases. It should rather be replaced by more appropriate control measures in such cases, and still used in those cases where it offers a remedy.

A recurring theme in literature is the role of disclosure in balancing access to corporate information required to protect the interest of shareholder against those executives. Effective disclosure can be a highly successful mechanism to arouse shareholder attention and activism, which could in turn reduce agency problems associated with modern dispersed ownership structured businesses. Although disclosure may be one of the least costly ways of intervening in conflicts, it inevitably involves some agency costs, which impacts on the returns on investment of shareholders. In some instances cost-benefit analyses would show that it might not be financially beneficial for some companies to pay the expenses related to disclosure. On the other hand though, disclosure might lower agency costs through its deterrence effect, or through what King II refers to as “shrinking effects”. In the end, it is for the organisation to find the most appropriate balance amongst control measures to achieve the desired state of governance, where stakeholder interests are protected and corporate objectives achieved.

Ferrarini and Moloney (2004) suggest that the benefits of remuneration shrinkage and stakeholder activism associated with effective disclosure, should be weighed against the increased costs of disclosure and possible public or political reaction against the information disclosed. In most instances disclosure that explains the rationale for executive remuneration levels and practises with reference to expected performance outcomes is likely to be accepted more

readily by all stakeholders. This would simultaneously address current tendencies for firms to benchmark their executive remuneration levels against the published numbers of other firms alone, without necessarily comparing executive remuneration on the basis of comparative corporate performance. Crotty and Bonorchis (2006) state that it is clear that the most significant determinant of executive pay levels in South Africa presently is the prevailing level of pay in the peer groups, as published in companies' annual reports. Most often these peer groups include high earning executives in the USA and UK, which appears to be the generally accepted global executive remuneration benchmark.

The field of executive remuneration is complex. Powerful, self-interested executives often contribute to the complexity of the field by developing remuneration schemes designed to hide the extent to which the executives skim wealth from shareholders. Opaque disclosure will generally not generate effective shareholder oversight and activism, and will increase the agency gap between self-serving executives and shareholders. Enhanced, full disclosure on the other hand may induce shareholder oversight and activism through their ability to make informed decisions.

There is however some evidence that executives manipulate disclosure of the remuneration practices and levels, in order to maximize their own interests above those of shareholders (Ferrarini and Moloney, 2004). Such manipulation is often possible as a result of:

- Poor alignment-of-interests incentivisation;

- A weak link between pay and performance;
 - Low performance targets;
 - Favourable remuneration packages;
 - No downside risk;
 - Repricing of options; and
- Poor control and oversight over executives.

Yablon and Hill (2000) aver that, depending on the motive for manipulation of disclosed information, such manipulated disclosure may be unlawful or illegal. They concede however that this is a legislative grey area that is often clouded by differences between the letter of the law and the spirit of the law.

Although disclosure is appealing as a less aggressive form of corporate governance intervention in bridging the gap between corporate governance and executive remuneration it is, in itself, not a sufficient measure to do so. Disclosure that does not lead to some consequences, such as shareholder activism or informed investor decision, serves very little purpose, if any. Where effective disclosure cannot be generated through best practice guidelines and codes, it might be necessary to impose direct legislative interventions. Such intervention may however impact negatively on the measure of flexibility that companies require to conduct their business competitively in a specific environment. In the end, executive remuneration should be set by a correctly functioning market, and it should reflect the unique requirements of the company. It should not be artificially imposed by government (Ferrarini and Moloney, 2004).

7.3 Conclusion

The outstanding feature of regulation of executive remuneration is the extent to which it reflects the interconnection between pay and corporate governance. Kakabadse, *et al.*, (2004) suggest that activism by investors and other stakeholders of a business is gaining momentum throughout the world. They ascribe this to increased awareness of the impact of conflicts of interest between powerful executives and shareholders on maximization of long term shareholder wealth. The agency problems created by the separation of ownership from control in modern organisation have led to corporate governance developments aimed to ensure an alignment of the inherently conflicted interests of executives and shareholders.

Internal corporate governance measures that refer to the relationships between directors, executives, shareholders and stakeholders, as well as external measures that refer to the legal, regulatory and administrative corporate governance framework in a company, have been developed loosely for each different country. As a result of increased globalization however, there is a clear recent trend toward a convergent system that sets out a framework for best practice, but allows for a measure of flexibility according to individual needs. This system is commonly referred to as a “comply or explain” structure.

Where the corporate governance framework is based on a set of underlying principles which have to be applied in order to achieve good corporate governance, and which is supported by sets of suggested best practice control measure guidelines, it is commonly referred to as “apply or explain”. In terms of this system of governance, companies have to apply the principles contained in

regulatory codes, or explain the reasons for their failures to do so. The King III Code introduced this system of governance in South Africa in 2010. A possible refinement, or even improvement, of this system would be to require companies to “apply and explain”. In terms of this suggestion companies would be required to apply the set principles, and explain how they were applied in their businesses.

Regulation therefore has not managed to reduce the growth in executive remuneration, but has altered the structure of pay by, amongst others, awarding profitable incentives to executives in addition to basic salaries. Yablon and Hill (2000) conclude that the structural features of an executive remuneration dispensation can contribute significantly to the effectiveness of a corporate governance framework. In this regard they suggest that both legislation and litigation have a role to play. The question is how to maximise benefits while simultaneously minimising risks and costs. A balancing exercise is required for each individual organisation.

Although it is beyond doubt that disclosure of executive remuneration could be a highly effective corporate governance control measure, in conjunction with other control measures, there are related negative aspects of disclosure. In a framework however as the one developed in Annexure B, an integrated balance amongst different control measures could be found to address specific fundamental principles of governance. This would allow companies to develop tailored and flexible control measures within an integrated corporate governance framework, which satisfy both forward-looking (informative) and backward-looking (monitoring) aims of corporate governance.

8 CONCLUSIONS FROM LITERATURE REVIEW

Although the debate around corporate governance and executive remuneration has been around since at least the 1930's when the theory relating to the modern corporation, characterised by a separation of ownership from control, was developed, its prominence was brought to the fore as a result of widely published corporate collapses and scandals of the last decade. Executive remuneration is widely considered to be an essential component of a corporate governance framework.

The most dominant theory used to explain the separation of the ownership from control in modern organisations, and the role of executive remuneration in the process is agency theory, which considers incentive-based executive remuneration as essential tools in establishing alignment between self-interested executive actions and the interest of shareholders. An assumption is made that the market in general, and performance based executive remuneration in particular, would counterbalance executive self-interest. Over time it became clear that agency theory did not offer an all-inclusive explanation for executive remuneration in the corporate governance context, which led commentators to a wider societal focus. One of the most prominent theories developed to give effect to this increased focus is stakeholder theory, which considers the alignment of executive actions with the interest of a wider group of stakeholders, of which shareholders constitute only one part thereof.

The most fundamental issue in the executive remuneration debate relates to the alignment of conflicts of interest between shareholders and executives, who enjoy opportunities to serve their own interests above those of shareholders as a result of their positional power and control in organisations. A number of different internal and external corporate governance measures have been developed over time, and imposed through direct regulation, listing requirements and voluntary codes of best practice, but have been described as plasters on an open sore, which will not necessarily heal the underlying cause of the executive remuneration problem.

One of the corporate governance measures developed, and implemented to varying degrees across the world, is the disclosure of executive remuneration. The underlying objective sought to be addressed by such disclosure is to create transparency with regard to executives in an organisation, which is both forward looking and backward looking. Forward looking objectives involve information symmetry which allows stakeholders of the organisation to make informed decisions in the protection of their interests. Backward looking objectives on the other hand allow stakeholders to monitor executive actions to ensure alignment thereof with their own interests. Disclosure of both executive remunerating policy and individual executive remuneration packages will enable shareholders and other stakeholders to gauge the level of discrepancy between executive and shareholder interests, which would enable them to make informed decisions in the process of protecting their own interests.

Disclosure of executive remuneration however has both positive and negative consequences. The intended positive consequence of disclosure relate to the

informative value and regulatory techniques thereof, while the unintended or negative consequences relate to privacy deprivation, ratcheting benchmarking practices, and disclosure costs.

Disclosure practises around the world could generally be grouped as either full disclosure (Anglo-American) or limited disclosure (continental Europe). Although there are still significant differences in the extent of disclosure amongst different countries, based mainly on economic, political and culture variables, a convergent trend towards a more uniform approach to dealing with executive remuneration and corporate governance is observable. One of the strongest reasons advanced for such convergence is the increase in globalisation and the global market for scarce executive talent.

There is general consensus amongst commentators that disclosure of executive remuneration policy and packages *per se* would not be sufficient to address the problems with executive pay practices and levels. Disclosure is only a tool that enables further action, of which the most significant would be the ability of shareholders and other activists to exercise more informed oversight over executives, and to make more informed investment and other decisions. Its potential role in an integrated corporate governance framework, as set out in Annexure B, should however be understood and applied in a case appropriate mix in individual organisations.

A number of corporate governance mechanisms have been developed over time to regulate the conflicts of interest between shareholders and executives. These regulatory interventions range from direct legislation, such as the

Sarbanes-Oxley Act in the USA, to voluntary codes of best practice guidelines, which are often formalised in terms of listing requirements applicable to public companies. Such corporate governance mechanisms can be divided into internal and external measures. Internal measures refer to those mechanisms dealing with the relationship between directors, executives, shareholders, and other stakeholders. In contrast, external measures refer to the legal, regulatory and administrative frameworks for corporate governance in the company (including disclosure and other outside control measures to protect shareholder interests). Although a measure of global consistency in respect of a principled corporate governance framework is required, there should be some flexibility to allow individual companies and countries to operate competitively in their particular environments. An appropriate mix of internal and external corporate governance measures should therefore be applied flexibly within a guiding global framework of corporate governance principles to be applied.

Ultimately, the most fundamental issue in executive remuneration should be the purpose for which the remuneration is paid to executives. The intended outcomes of executive remuneration practices need to be clarified. A historic belief that the ultimate outcome was to establish alignment of executive actions with the best interest of shareholders might not hold any longer as a result of modern developments in business ownership structures and stakeholder bases. Although the notion of alignment of executive remuneration to the achievement of long term growth and sustainability of the company cannot be faulted, the latter concept needs to be clarified to make the link meaningful.

9. RESEARCH PROPOSITIONS

The primary assumption for this DBL research is that modern corporations have developed away from the traditional assumption that the primary purpose of the corporation is the creation of wealth for its shareholders, as owners of the corporation, towards a position where broader stakeholder interests could even outweigh the interests of shareholders. The implication thereof is that, since executive remuneration is used as a mechanism to align the interests of executives, who manage the corporation on behalf of its owners, with the interests of shareholders, there is a need to review this most fundamental aspect of executive remuneration.

The question that should be answered in the process is to which interests executive actions should be aligned. In terms of the above assumption, it should be to the interests of a broader group of stakeholders, rather than only the shareholders of the corporation. The role of executive remuneration, which is traditionally considered to be a mechanism to align the interest of executives (managers) with those of shareholders (owners), therefore needs to be reconsidered. Disclosure of executive remuneration levels and the process for determination thereof is key in such alignment process, in that it both aligns executive actions with stakeholder interests, and provides stakeholders with the necessary information to hold executives accountable for their actions.

Propositions were developed for this study, rather than hypotheses. This was deemed more appropriate in a study where statements about concepts such as

corporate governance, executive remuneration, and disclosure, had to be tested as either true or false in relation to observable phenomena, rather than as tentative or conjectural statements as the case is in respect of hypotheses.

Four propositions were developed from the literature review.

9.1 First Proposition

Corporate governance failures result from ineffective internal and external control measures and systems.

Annexure B shows an integrated systems view of corporate governance, in which different sub-systems interrelate with each other to form a holistic structure intended to ensure good corporate governance in an organisation. Internal and external corporate governance control measures form two of these sub-systems within a corporate governance framework. Figure 2 above shows how both internal and external corporate governance control measures, together with activism, interact with each other to form a corporate governance framework and system in a corporation.

Although public comment has laid the blame for many corporate collapses and scandals at the door of corporate governance generally, it is necessary to consider whether, and if so, how ineffective corporate governance control measures impact on the success or failure of a corporate governance system. In essence this would investigate the cause of the problem rather than a symptom thereof.

9.2 Second Proposition

Both the levels of executive remuneration and the process for determination thereof are symptomatic of the failure of corporate governance control measures.

The impact of a failure of, or ineffectiveness of, a corporate governance control measure, whether internal or external, on executive remuneration needed to be clarified. Much has been written in academic journals and public comment documents on the high levels of executive remuneration, which is often attributed to corporate governance failures. It was however necessary to investigate whether the high levels of executive remuneration are not indeed symptomatic of some deeper cause. In doing so, the process for determination of executive remuneration needed to be investigated.

In an effective overall corporate governance system, corporate governance control measures should be effective enough to ensure justifiable, transparent and fair remuneration levels and determination processes. No single corporate governance control measure can be effective on its own to ensure compliance with a desired governance principle. The extent to which different governance control measures are integrated to provide an effective solution to the governance objectives of an organisation needs to be investigated. Whether companies in South Africa however understand the need for such integration of sub-systems, or apply such theory is however needed to be seen.

9.3 Third Proposition

Effective disclosure of executive remuneration determination processes and levels, as a corporate governance control measure, contributes to a more effective overall corporate governance system in organisations (i.e. there is a positive correlation between disclosure and good corporate governance).

The aim of disclosure of executive remuneration should be clarified to ensure that there is not only an understanding of the extent of disclosures required for corporate governance control measures to be effective, but also an understanding of the underlying principles that ought to govern a disclosure strategy.

A study of the disclosure practices of listed companies in South Africa, to which strict disclosure rules apply, would show whether there is such a common understanding of the nature and extent of disclosure required, and the ultimate reason for requiring disclosure in a good corporate governance framework.

The manner and extent to which disclosure of executive remuneration, as one potential governance control measure, is integrated into an overall corporate governance system, and its effect on good governance, needed to be investigated.

9.4 Fourth Proposition

Disclosure of executive remuneration is one of the control measure sub-systems in a larger corporate governance framework, in which different control measure sub-systems interrelate to form an inclusive corporate governance framework.

In a strictly regulated environment, wherein it is expected that a majority of companies would seek to comply with regulated governance requirements, it is necessary to consider whether the aim of disclosure is intended to be more than merely a “tick-the-box” compliance exercise, or whether there is a more strategic aim. In this regard, one has to question what the intended consequences of disclosure are for individual organisations.

Differences between backward-looking (monitoring) and forward-looking (informing) reasons for disclosure had to be investigated, as well as how both of these types of disclosures interrelate with other external and internal corporate governance control measures, to result in an integrated and inclusive corporate governance framework.

10. METHODOLOGY

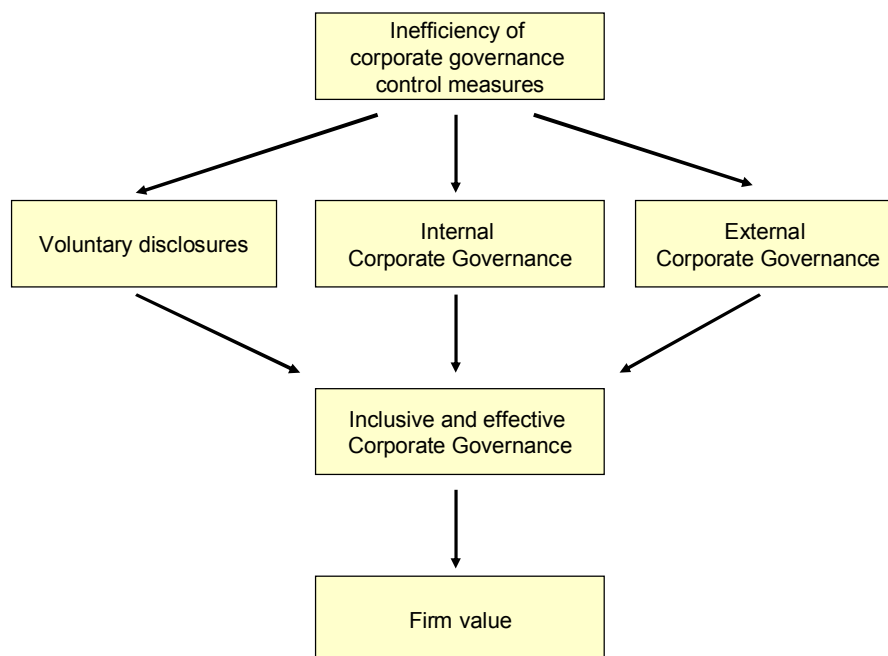
Corporate governance research to date has been both quantitative and qualitative. A central challenge to any such studies, and especially quantitative research, is to obtain the most current and accurate data, given the sheer pace of reform in the field. After first collating the disclosure requirements set for companies listed on the Johannesburg Stock Exchange (JSE), content analysis of disclosures in annual reports of those companies was conducted to establish baseline knowledge for the disclosure policies and practices of the companies selected to form part of the research sample. The data was further analysed for the level to which it informs stakeholder decision making, and whether it eliminates or reduces current inequities in relation to the access to information between executives and shareholders. Appropriate sampling was required, and was selected in such a way as to allow for learning from different experiences across institutions and industries.

In a discipline that is often described as more of an art than a science, due to the influence of human behaviour in complex situations, academic contributions can bring the art of executive remuneration disclosures closer to a science, by applying scientific research methodologies and processes to the data. Scientific business research, as have been applied in this study, is characterised by the rigor of the analytical tools and techniques applied by the researcher, and should therefore be distinguished from ordinary investigations. Cooper and Schindler (1998) identify the following as characteristics of scientific business research:

- The purpose of the research must be clearly defined;
- The research process must be detailed in a research proposal;
- The research design must be well planned;
- Research limitations must be identified and stated clearly;
- Data analysis must be adequate to show its relevance and significance;
- Methods of data analysis should be appropriate;
- Research findings must be presented unambiguously; and
- Conclusions must be justified, and supported by the research data.

The process for determining the role of different governance control measures in creating value through an inclusive and effective overall corporate governance system could be as appears in Figure 9 below.

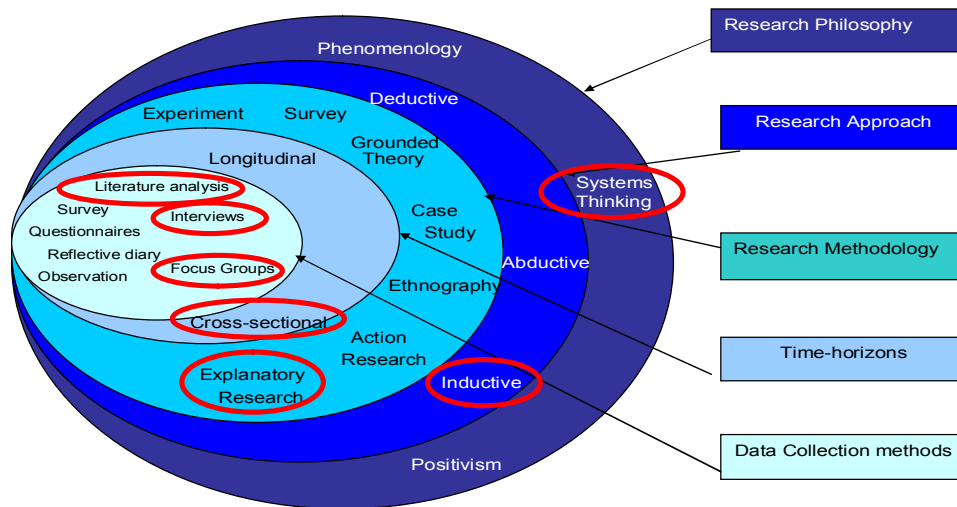
Figure 9: Value add through inclusive and effective corporate governance measures



De Vos (2002) states that a research methodology should be defined in terms of the process, instruments, and procedures that is used in the research project. Saunders, Lewis and Thornhill (2003) suggest that the research process should be designed in the same way as one would peel off the layers of an onion, and that each layer represents a specific phase before the data collection process could be started. Figure 10 below depicts their proposed research process onion. In terms thereof the first outer layer deals with the issue of selection of a research philosophy. The second layer considers the subject of the research approach that follows from the philosophy. The third layer deals with the research strategy. The fourth layer refers to the time horizons for the research, and the fifth layer finally deals with the data collection methods.

The red circles drawn in on the research process onion in Figure 10 indicate how this study has been designed in following the proposed research onion approach. The research philosophy for this study is based on systems thinking, while the research approach is inductive. The research methodology is essentially explanatory, while the time horizon is cross sectional. Data collection for this study is in terms of literature analysis, interviews and focus groups. The research process, as well as the reasons for selecting the above options, for this study is set out more fully in the paragraphs below.

Figure 10: The research process onion



(Adapted from Saunders, *et al.*, 2003:85)

10.1 Research methodology and design

The research methodology and design followed in this study was similar to the process suggested by Saunders, *et al.* (2003) as depicted in Figure 9 above. In particular, it was important to first develop a research philosophy, approach and strategy before the process of data collection, analysis and interpretation could be started.

10.1.1 Research philosophy

The research philosophy informs the way in which the research will be conducted, and ultimately how knowledge will be developed. Saunders, *et al.* (2003) identify three different philosophical approaches, which are not always completely exclusive of each other, namely:

- Positivism;
- Phenomenology; and
- Systems thinking.

A philosophy of positivism generally requires observable social realities that can be replicated by means of a highly structured methodology. Statistical analysis of quantitative data is usually required in this process (Gill and Johnson, 1997). A positivism philosophy therefore would not have been appropriate for the purpose of this study, which was primarily qualitative in nature.

Remenyi, *et al.* (1998: 35) argue that a phenomenological approach is best suited when the research intends to discover “the details of the situation, to understand the reality or perhaps a reality working behind them”. A phenomenological approach therefore is often most appropriate where the uniqueness and complexity of business issues, which can often not be reduced to strict generalisations, are central characteristics of the research subject. In this study, a phenomenological approach was most suited in relation to exploratory and explanatory objectives of the study to understand the concepts of disclosure, executive remuneration, and corporate governance. It is however not sufficient on its own to explain the interrelationship of these constructs or sub-systems in a larger corporate governance system in an organisation.

A research philosophy based on systems thinking views the organisation as a larger system made up of several sub systems that interrelate with each other in such a way as to produce organisational results. In this regard, Senge (2006) suggests that a sub-system cannot be healthier than the larger system on which it depends. He concludes that there is no right model for a complex system, but that the criterion that ought to be used is usefulness rather than accuracy, and that this requires an insight of how systems work and fit together to solve a problem. This also accords with the view expressed before, that companies have to develop situation appropriate control measures within a principle based corporate governance framework, to the extent to which those control measures are useful and appropriate in their individual circumstances.

In response to the research problem identified earlier, a systems based view of corporate governance control measures, of which disclosure is but one, was required, to analyse the overall effectiveness thereof. The model developed in Annexure B formed the basis of such analysis.

10.1.2 Research approach

A typical research approach could be either deductive or inductive. In terms of the deductive approach the researcher develops a theory and propositions, after which a research strategy is developed to test those propositions. The inductive approach requires the collection of data followed by the development of theory as a result of the data analysis. Saunders, Lewis and Thornhill (2003) suggest that the deductive approach is often best suited to a research philosophy based on positivism, while an inductive approach is often most

suited in the case of a phenomenological research philosophy. They however correctly remark that such a classification might be misleading, as such direct linkages do not always make sense, and often a combination of these approaches may be more appropriate.

Whereas the deductive approach often generalises relationships between two or more events or concepts quantitatively, the inductive approach seeks to rather understand the way in which people experience social issues differently. In this way, the inductive approach is more concerned with the context within which certain events take place. This often implies that, under an inductive approach, a small sample that produces qualitative data may be more appropriate than the large sample required under the deductive approach. Table 5 below indicates the major differences between the deductive and inductive approaches.

Table 5: Differences between deductive and inductive approaches

Deductive approach	Inductive approach
Scientific principles	Gaining an understanding of the meanings humans attach to events
Moving from theory to data	A close understanding of the research context
The need to explain causal relationships between variables	A more flexible structure to permit changes of research emphasis as the research progresses
The collection of quantitative data	The collection of qualitative data
The application of controls to ensure validity of data	A realisation that the researcher is part of the research process
The operationalisation of concepts to ensure clarity of definition	Less concern with the need to generalise
A highly structured approach	
Researcher independence of what is being researched	
The necessity to select samples of sufficient size in order to generalise conclusions	

(Saunders, *et al.*, 2003: 91)

Creswell (1994) suggests that the nature of the research topic, and the availability of the data from which propositions could be developed should direct the choice of research approach.

This study lent itself more to an inductive approach where theory was only developed after collection of qualitative data in an area where there is a general paucity of existing data and theory. It was specifically intended to gain a non-generalised or individualised understanding of the meaning people attach to constructs such as disclosure and corporate governance in different contexts. A more flexible research structure was required to allow for changes in emphasis as the research progressed.

10.1.3 Research strategy

Although some research strategies are commonly more suited to an inductive approach and others to a deductive approach, it is more important to carefully select a strategy which is most appropriate for the particular research question despite the approach followed. Table 6 below sets out the prominent features of the most common research strategies.

Table 6: Research strategies

Strategy	Characteristics
Experiment	<ul style="list-style-type: none">• Theoretical propositions• Allocate samples to different experimental conditions• Measure variables after introduction of planned changes
Survey	<ul style="list-style-type: none">• Collect extensive data from large population• Often more quantitative than qualitative• Offers process control, but time consuming and limited
Case study	<ul style="list-style-type: none">• Detailed knowledge about existing single or related cases• Creates an understanding of phenomena• Various data collection methodologies possible
Grounded theory	<ul style="list-style-type: none">• Theory building through a combination of induction and deduction• Theory is developed from data collected• Data lead to predictions which are tested further
Ethnography	<ul style="list-style-type: none">• Interpret the social world through inhabitants' interpretations• Time consuming and long term• Not dominant in business research
Action research	<ul style="list-style-type: none">• Focus on specific actions, such as change / knowledge transfer• Researcher is directly involved in actions• Has implications beyond immediate context
Cross sectional and longitudinal	<ul style="list-style-type: none">• <u>Cross sectional</u>: Snapshot of a phenomenon at a particular time, or comparison thereof across organisations• <u>Longitudinal</u>: Measures change over a period of time
Exploratory, descriptive and explanatory	<ul style="list-style-type: none">• <u>Exploratory</u>: Clarify the understanding of a problem• <u>Descriptive</u>: Accurate profile of phenomena, persons, events or situations• <u>Explanatory</u>: Establish causal relationships between variables

It is often beneficial to use multiple strategies in the same study. Different strategies might be more appropriate for different purposes in the same study project. It also enables triangulation to ensure accuracy and validity of the study.

The most appropriate strategy, in terms of the above characteristics, for the purpose of this study was therefore a combination of systems thinking, a cross sectional timeframe, and exploratory, descriptive and explanatory study.

This study was mainly explorative and explanatory, as it had as its goal to clarify the understanding of effective disclosure of different aspects of executive remuneration in an effective system of corporate governance control measures in an organisation, and to interpret and explain the relationships that lead to causality between different variables in a corporate governance system in an organisation. The study was however also descriptive to the extent that it described the observed relationships between such variables.

10.1.4 Research process

The research process followed in this study could be summarised as depicted in Figure 11 below. In the planning phase of the study, the research problem, research objectives and research questions were identified and formulated. A literature review was conducted as a basis from which propositions were formulated.

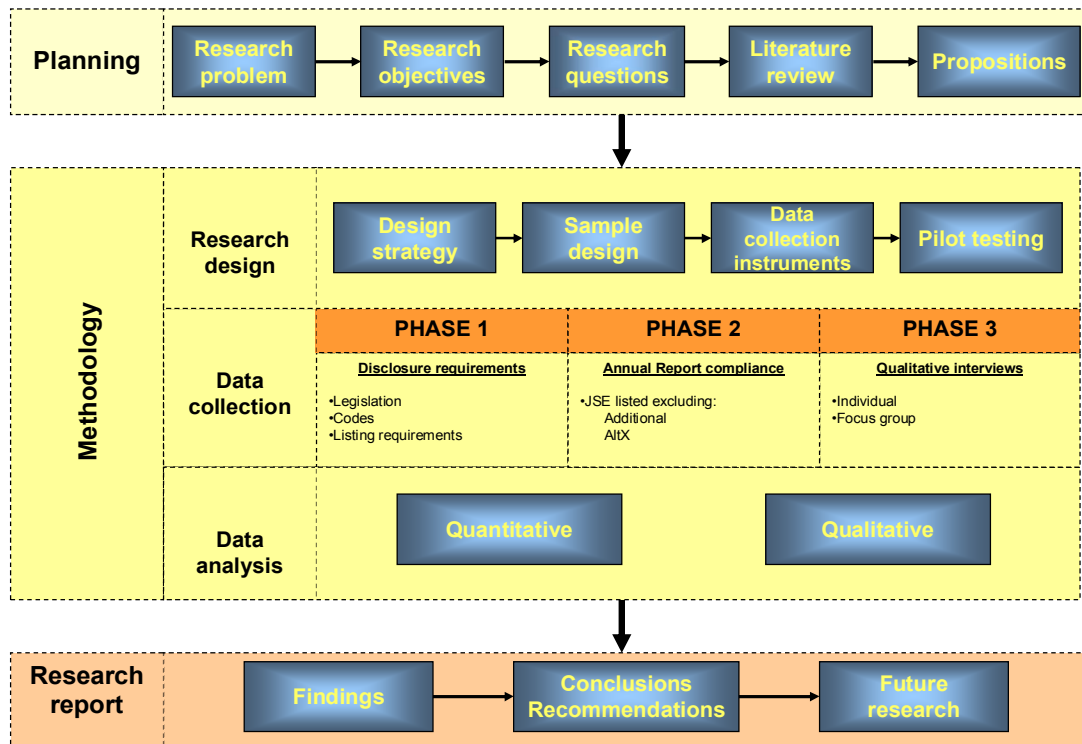
After formulation of the research propositions, a research methodology was developed. This firstly entailed the formulation of a research strategy, which included the type, purpose, time frame, scope and environment for the study. Thereafter a sample frame and sample were determined from the research population. The next step was to design data collection instruments for both the quantitative and qualitative components of this study, and to pre-test those instruments during a piloting phase.

A multi phased data collection process was followed. In the first phase all executive remuneration disclosure requirements that apply to South African

listed companies on the JSE were collated, where after the specific executive remuneration disclosures of all JSE listed companies in South Africa, as appears in their 2007 Annual Reports, were compared to the collated minimum disclosure requirements. In the final data collection phase, the researcher personally conducted all qualitative interviews with applicable members from the sample companies, as well as with a focus group, in order to gather deeper and more meaningful disclosure data.

A mixed methodology approach was followed, in terms of which data analysis was done by means of a combination of quantitative and qualitative techniques, in order to make it more robust, where after the research report was drafted.

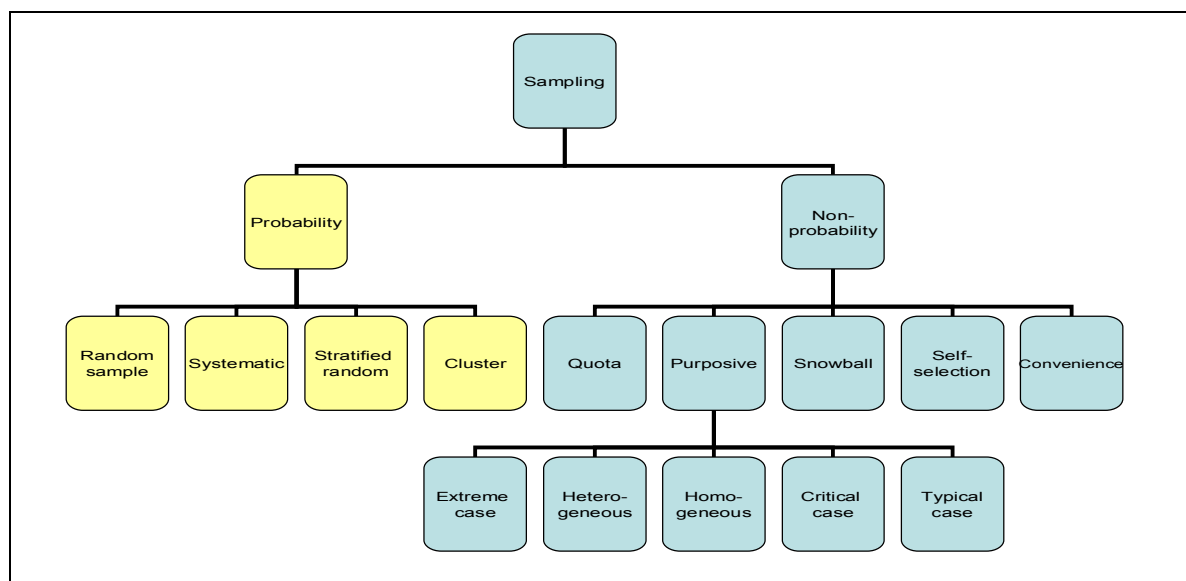
Figure 11: Research process



10.2 Sample selection

Selecting a sample from the research population is appropriate when it is not practical to research the entire population, or where budget or time constraints prevent inclusion of the entire population in the study. There are two basic sampling techniques, namely probability (representative) sampling and non-probability (judgmental) sampling, as set out in Figure 12 below. Probability sampling implies that the probability of a participant to be selected from a population is both known and equal to all other participants. With non-probability sampling such probability is not known, and it is not possible to make statistical generalisations about characteristics of the population. In contrast to probability sampling, non-probability sampling provides alternative subjective techniques where probability predictions are not possible. A tailored combination of both probability and non-probability sampling techniques could be used.

Figure 12: Sampling techniques



(Saunders, *et al.*, 2003: 153)

Probability sampling requires the identification of a sampling frame based on the research questions, the selection of a suitable sample size and technique, and confirmation that the sample is representative of the population. The sampling frame represents a list of all the members of the population from where the sample will be drawn, and is further critical to ensure a representative sample. Selecting a probability sample is therefore a compromise between the accuracy of findings based on the entire population, and the time and money invested into the collection and interpretation of the data (Saunders, *et al.*, 2003). Although Hoinville and Jowell (1985) suggest that the selection of a sample is almost always based on judgment rather than calculation, the choice of a sample should generally be informed by:

- The level to which sample data is representative of the total population;
- The level of accuracy required;
- The number of categories into which data will be divided; and
- The size of the total population.

Table 7 below sets out the prominent characteristics of the most common probability sampling techniques, while Table 8 below sets out the similar characteristics of the most common non-probability sampling techniques.

Table 7: Probability sampling techniques

Sample type	Sample frame required	Size of sample needed	Area to which suited	Relative cost	Advantages compared to simple random
Simple random	Accurate and easily accessible	Better with over a few hundred	Concentrated if face to face contact required, otherwise does not matter	High if large sample size or sampling frame not computerised	Not applicable
Systematic	Accurate, easily accessible, and not containing periodic patterns. Actual list not always needed	Suitable for all sizes	Concentrated if face to face contact required, otherwise does not matter	Low	Normally no difference
Stratified random	Accurate, easily accessible, divisible into relevant strata	Better with over a few hundred	Concentrated if face to face contact required, otherwise does not matter	Low, provided that lists of relevant strata available	Better comparison across strata. Differential response rates may necessitate re-weighting
Cluster	Accurate, easily accessible, relates to relevant clusters not individual population members	As large as practicable	Dispersed if face to face contact required and geographically based clusters used	Low, provided that lists of relevant strata available	Quick but reduced precision
Multi stage	Initial stages geographical; final stage only needed for geographical areas selected	Initial stages as large as practicable; final stage better with over a few hundred	Dispersed if face to face contact required, otherwise no need to use this technique	Low as sampling frame for actual survey population only required for final stage	Difficult to adjust for differential response rates. Substantial errors possible

(Saunders, *et al.*, 2003: 171)**Table 8: Non-probability sampling techniques**

Sample type	Likelihood of sample being representative	Types of research in which useful	Relative costs	Control over sample contents
Quota	Reasonable to high although dependent on selection of quota variables	Where costs constrained / data needed very quickly so an alternative to probability sampling needed	Moderately high to reasonable	Relatively high
Purposive	Low although dependent on researcher's choices (extreme case, heterogeneous, homogeneous, critical case, typical case)	Where working with very small samples	Reasonable	Reasonable
Snowball	Low, but cases will have characteristics desired	Where difficulties in identifying cases	Reasonable	Quite low
Self-selection	Low, but cases are self-selected	Where exploratory research needed	Low	Low
Convenience	Very low	Where very little variation in population	Low	Low

(Saunders, *et al.*, 2003: 171)

In this research the relevant population was all business corporations in South Africa. From this population a sampling frame was drawn in terms of all publicly listed companies on the JSE in South Africa. It was unfortunately not achievable in respect of time, resource and other constraints to engage all South African publicly listed companies for purposes of this research. It was therefore necessary to draw a representative sample from the sampling frame to determine those companies listed on the JSE whose disclosure practices would be evaluated. In doing so, a stratified random sample was determined in such a way as to be representative of all the different industries represented on the JSE index. Annexure I sets out the different such industries and sectors within each, and also indicates the numbers of listed companies within each sector and industry at the time of this study. For the purpose of this study, the companies listed on the “AltX” and “Additional” sections of the JSE index was disregarded as not being representative of a particular industry, but rather a combination of companies from industries already included under some of the remaining sections of the JSE index. While the study analysed the disclosure practices of all companies listed under the remaining industries and sectors of the JSE for the purpose of selecting an appropriate research sample for the final phase of the study, the final phase focused on only the main industries of the JSE. These are classified as Raw Materials, Industrial, Financial, Consumer Goods and Consumer Services. In the process however of analysing the disclosure practices of all JSE listed companies (in the sample selection phase), quantitative analysis across industries was done, which disclosed valuable information relating to differences in disclosure practices of South African listed companies across different industries.

Before a sample could however be determined for this study it was necessary to record the minimum disclosure requirements in respect of public companies listed on the JSE. These requirements emanated from relevant legislation, JSE listing requirements, and the King II Code on Corporate Governance in South Africa. In order to determine the sample thereafter, a preliminary analysis and interpretation was done in respect of the disclosure practices as appears from the 2007 Annual Reports of all of the companies that form part of the sampling frame, in comparison to the minimum disclosure requirements referred to above. Such analysis was done in terms of the Annual Report Disclosure Compliance Index referred to in section 4.5 below, in order to rank companies into one of three categories, namely:

- Those who disclosed more than the minimum requirements;
- Those who disclosed exactly what is required; and
- Those who disclosed less than the minimum requirements.

From this classification, companies in each of the three groups were selected as part of the sample for this study, having regard to representation of a cross section of comparable industries in each group. The size of the sample per group was at least 10% of the total number of companies in such a group. This not only allowed for representative industry analysis within each of the research groups, but also for comparisons across the three different research groups.

10.3 Data collection and preparation methods

Data collection was multi phased in the sense that it used both secondary data sources, such as existing literature, and primary data obtained by means of personal interviews and a focus group. In the first phase the research data collection process started with the collection and study of secondary data from existing literature sources. This was intended to yield valuable background information and direction. After completion of the literature review, the minimum disclosure requirements applicable to listed public companies in South Africa were recorded, to form a basis from which disclosure practices of those companies could be evaluated. This was followed by an analysis of the 2007 Annual Reports of all JSE listed companies (with the exclusion of those companies listed on the AltX and Additional sectors of the JSE), to evaluate their disclosure practices against the set minimum requirements. The expected outcome of this process was to rank such companies into one of the three categories mentioned above.

In the second phase of the data collection process, after companies have been classified into the three categories above, representative samples were selected from each of the categories, which will be both representative of the industries and sectors represented in each category, and which would enable comparisons across these categories. A 10% sample for each group was considered to be appropriate and suitably representative of the group. Once the respective samples had been determined, primary data was collected by means of in depth interviews with individuals and groups from each of the selected samples. This data was finally analysed and interpreted in order to make

findings and recommendations related to the research problem, questions and propositions.

The most common method for collecting qualitative data is by means of semi-structured or unstructured interviews (Musson, 1998). The interviews were conducted as flexibly and fluidly as the interview situation allowed, but in such a way as to direct the interview in the desired direction to obtain optimal data. Care was however taken not to impose a rigid and predetermined framework on the interview situation.

A large volume of data was collected by means of these interviews, as well as from the quantitative analysis of Annual Reports in the second phase of the research process, which required extensive analysis by the researcher. This, amongst others, required arranging the data in terms of common themes, trends and groups that made most sense, and analysis of the context of the interview data in a scientific way.

Content analysis was used as a technique to structure “open-ended” data for meaningful analysis (Harwood and Garry; 2003). It made it possible for the researcher to reduce certain phenomena or events into categories which would make it easier to analyse and interpret the data, by systematically evaluating the symbolic content of all forms of communication at different levels (Kolbe and Burnett; 1991). In this regard, content analysis made it possible to quantify the data communicated between the interviewee and interviewer, within the meaningful context of the interview.

Harwood and Garry (2003) identify some of the levels of classification of interviews in terms of which the meanings of words are inferred from the context within which they were communicated:

- Pragmatical content analysis: analysing likely cause and effect;
- Semantical content analysis: analysing meanings;
- Designation analysis: analysing frequency of references to objects;
- Attribution analysis: analysing frequency of characterisation
- Assertions analysis: analysing frequency of characterisation to certain objects; and
- Sign-vehicle analysis: analysing the frequency of an actual utterance.

Kolbe and Burnett (1991) identify the following potential benefits of content analysis in a qualitative study, which underscored the appropriateness of content analysis for the purpose of this study:

- It allows for an unobtrusive appraisal of communications;
- It can easily assess the effects of environmental variables;
- It provides an empirical starting point for generating new data about the nature and effects of specific communications; and
- It can be used together with other analysis methods in a multi-method study.

After collection, data was arranged, analysed, interpreted, and finally presented in meaningful groups of disclosure influences on corporate governance effectiveness. The process of sorting, coding and interpreting the data collected by means of personal interviews initiated with a thorough reading and consideration of all the collected data to identify themes and patterns. The data was then sorted into homogeneous clusters to which certain metaphors could be attributed to describe the different clusters. These clusters were then critically compared and contrasted to find a deeper meaning for the differences in their composition, while at the same time looking for relationships and links amongst the different clusters. All data collected was analysed by the researcher personally in terms of its validity and reliability, to test whether it measures what it was supposed to (validity) and its consistency (reliability). The nature of this research lent itself to a pragmatical content analysis method because of the fact that cause and effect relationships are central to the research.

10.4 Justification for using these methods

A sound research design was imperative to ensure that there is a reduced possibility of not addressing the main research problem. This implied that the research results had to be both reliable and valid. Reliability refers to the extent that the same research results will be yielded on different occasions, whereas validity refers to the extent to which findings are really what they appear to be.

Harwood and Garry (2003) suggest that reliability takes one of three forms in content analysis, namely:

- Stability: the extent to which the data is immutable;
- Reproducibility: the use of the same coding system under different circumstances;
- Accuracy: the process to conform to a predetermined standard.

They further suggest that validity, in terms of the extent to which the research may be generalised to the entire population, takes one of two forms in content analysis, namely:

- Internal validity: the ability of a research instrument to measure what it is purported to measure
- External validity: the extent to which the research data can be generalised and is consistent with previous and future research, including:
 - Construct validity: the theoretical rationale of the data collected;
 - Proposition validity: consistency of data with expected relationships and theory;
 - Predictive validity: verification of inferences through actual observation; and
 - Semantic validity: agreement on meanings and connotations of language.

It was intended to ensure the validity of this research and its results, through mechanisms in the research design (external validity), data collection (construct validity) and data analysis (internal validity) stages of the research, by planning and design of an instrument, and by methods to ensure that the research measures what it is supposed to in terms of its objectives. Caution was exercised to guard against the threats to reliability and validity, as set out in Table 9 below

Table 9: Threats to reliability and validity

Reliability	Validity
Subject error	Timing of research
Subject bias	Measuring instruments
Observer error	Participation / sample size
Observer bias	Ambiguity
	Generalisation / external validity
	Incorrect assumptions

Reliability assurances were sought by means of checks on the accuracy and precision of the analysis procedures used in the study. In particular, it was necessary to constantly assess whether the analysis was linked to solving the research problem. The same tests and the same instrument were applied at different times and under different conditions for the respective individual and group interviews. Equivalence was obtained through the fact that all interviews were conducted by the researcher personally. This eliminated the risk of variations in interpretation by different interviewers. Data was therefore classified consistently in the same way, and by using the same measurement instrument, for every interview.

Schurink (2003) avers that qualitative research means different things to different people, and ascribes his opinion to the fact that qualitative research is used in almost all recognised social science disciplines and study areas, as a result of which these research methods have to be adapted to fit the particular varying requirements. Qualitative research covers an array of interpretive techniques that seek to describe, encode and translate a particular phenomenon in a manner that is flexible and sensitive to social context. This method seeks to understand the meaning of a phenomenon which is relatively unexplored.

Despite the adaptive nature of qualitative research, it is trite that in depth and unstructured interviews form important methods of qualitative research across different study areas. Bryman (2004) states that there is little doubt that qualitative interviews form a very large part of qualitative studies. The advantage of using personal and group interviews for data collection is that it focuses directly on the topic and provides an in depth focus, as well as causal inferences. There are however some possible disadvantages, which can be eliminated through proper planning, in that a response bias could result from poorly constructed questions, or poor interviewee recall of the event, or reflexivity of the interviewee's responses to questions. According to Krefting (1991), qualitative research emphasizes better than any other research method the uniqueness of the situation. This research therefore falls comfortably within the nature of qualitative research to date.

Bryman (2004) further states that there are certain recurring themes in qualitative studies, which is completely relevant for South African research,

where business leaders are continuously charged with leading significant change processes. He identifies these themes as:

- Securing commitment to the change process;
- Addressing multiple external and internal constituencies;
- Conveying a sense that change is needed;
- Creating a vision for implementation of change; and
- Creating a vision of the future state of the organisation.

This has the benefit that qualitative research seeks for variation in experience, rather than identical repetition. Variability is in fact almost always expected in qualitative research. Qualitative research therefore also tends to focus more on senior leaders in an organisation, such as executives, while quantitative such research tends to focus on different levels in the organisation.

The quantitative component of this research methodology related more to the initial recordal of current disclosure practices in the second phase of the research process, without necessarily analysing the deeper impact thereof on a broader corporate governance framework. This was done by means of analysing the disclosure practices of JSE listed companies, as appears from their 2007 Annual Reports, which, at the time of this study, were the latest consistent reports for all such companies. It was critical to establish a common baseline from which such deeper analysis could be done, and although there were some companies which had already published its 2008 Annual Reports at the time of the analysis, it would have been more valid to compare companies in relation to their Annual Reports covering the same time period. The use of

basic quantitative methods of analysis, such as content analysis and correspondence analysis lent itself to such a methodology.

10.5 Research instruments

Due to the two-phased design of the data collection process of this study, it was necessary to use two different research instruments. In the first phase of the data collection process disclosure practices of JSE listed companies were analysed against the minimum disclosure requirements constituted by, amongst others, legislation, the King II Code, and JSE listing requirements. One of the most fundamental aspects analysed was the effectiveness of communication to all stakeholder groups in terms of the selected disclosure mechanisms. The most important mechanism in this regard is the Annual Report published by the company. It was therefore imperative to design a control sheet of those aspects required to be disclosed (in terms of existing legislation, regulation and codes), and to compare the disclosure practices of companies in the research sample to those requirements. A coding table was used for comparison of the data collected from annual reports.

In a similar study, Berglof and Pajuste (2005) used an Annual Report Disclosure Index (ARDI), in terms of which points were allocated to certain disclosure items required in terms of legislative or regulatory codes. This made it possible to compare disclosure practices according to a uniform test. The starting point for such an analysis is to make a list of what has to be disclosed, to then list these items in order of significance, and finally to compare the firm's disclosure against these items.

In this study the above was achieved through a reference to the disclosures of executive remuneration in the 2007 Annual Reports of each of these companies, which served as a critical reference point before anticipated major amendments to South African company law, and the imminent publication of a King III Code at the time. In order to establish a consistent analysis of these disclosures, a disclosure index similar to the Annual Report Disclosure Index (ARDI) applied by Berglof and Pajuste (2005) was used. An Annual Report Disclosure Compliance Index (ARDCI) was developed for the purpose of this study, as set out in Annexure J.

In the third phase of the data collection process, after companies had been categorised into one of the three research groups based on the comparison of its disclosure practices to the applicable minimum requirements, mainly explanatory data was collected from each of the companies represented in the three different samples. This was done by means of direct interviews by the researcher personally, with relevant representatives at senior managerial and board level, and a selected focus group. The main purpose of these interviews was to form an understanding of the reasons for their respective disclosure strategies, and the benefits gained from them. Annexure K hereto sets out the open ended questions which were posed to the representatives of these companies, in an Interview Schedule. Certain aspects, such as for example the reasons for disclosure or non-disclosure of information items, or the timing thereof, and organisational culture and strategy, could be better analysed by means of qualitative interviews with individual executives and focus groups.

The Interview Schedule contained in Annexure J was designed after the comparison of Annual Report disclosures with the applicable minimum disclosure requirements, for the purpose of conducting personal, semi-structured interviews with members from the selected sample companies. Annexure L sets out a sample interview schedule proposed by Healy and Palepu (2000) in a similar study, which was used as a reference for developing the interview schedule for this study.

The final interview schedule developed for this study contains administrative, general and target questions. The administrative questions were designed to identify the companies interviewed, as well as the industry and sector to which it belongs. The general questions were designed not to directly address the research propositions for this study, but to provide high level data regarding the companies' strategy and approach in dealing with executive remuneration governance. Target questions were designed to specifically address the research questions and propositions directly. These questions included unstructured and open-ended questions, to allow participants some freedom in their responses, while at the same time drawing a clear frame of reference and border for the interviews. It was thought to be prudent not to disclose, before or during the interviews, to the sample interviewees how their respective companies were selected to form part of one of the three categories their companies have been classified into, and which category it falls under. This was important in order to eliminate any potential response bias which might be caused by preconceptions regarding each of the categories, or argumentative justifications and knee-jerk reactions.

Before embarking on the actual interviews and focus group sessions, pilot interviews were held with the remuneration managers from three pre-selected companies to pre-test the questions in the Interview Schedule, and the interview style of the researcher. Such a piloting phase was essential to establish that:

- The questions contained in the Interview Schedule would address all of the research problems and objectives;
- The data collection would be as accurate and relevant as possible;
- The target respondents from the selected sample companies would participate and co-operate as fully as possible;
- The collection and analysis of data would take place as smoothly as possible; and
- The questions would adequately address the research propositions.

The companies selected for the pre-testing phase represented each of the three categories into which companies were divided in phase two of the study, but were not any of the companies selected as part of the final sample for the qualitative interviews part of the study. This allowed for adjustments to the interview questions or approach, where necessary, before embarking on the interviews with the sample population. The final interview schedule was initially developed in line with the interview schedule used by Healy and Palepu (2000), but required to be adjusted after it became clear during the pilot interviews that the original interview questions did not succeed in addressing the research propositions of this study adequately. In particular, the initial questions used in the piloting phase did not elicit appropriate responses to explain the views of companies on disclosure of executive remuneration (levels, determination

processes and factors influencing those). These formed part of companies' overall governance structures, and how it impacted on effectiveness thereof. It was therefore necessary to redevelop questions which were more closely related to eliciting relevant responses to test the four propositions developed for this study.

The data obtained from the pilot interviews have been disregarded in the final phase of this study, as a result of the fact that significant changes to the interview schedule were required, and the potential inconsistencies in the subject matters dealt with during the pilot interviews as opposed to the final sample interviews, which would potentially distort the data collected for the final stage of the research.

Although phase two of this study considered the disclosure practices of all companies listed on the JSE (apart from those listed under the AltX and Additional categories), and irrespective of whether such companies are local South African companies or not, the final phase of the study only focused on those companies primarily based in South Africa. This was not only necessary from a practical cost and logistical point of view, but also to ensure a strong measure of consistency in respect of corporate governance requirements, where offshore companies' governance requirements may conceivably be broader and more extensive than only South African requirements.

10.6 Method for testing propositions

The purpose of testing the stated propositions was to determine the accuracy thereof in view of the fact that only a sample of the total population was used instead of every element of the population. The nature of this research was mainly exploratory to determine certain relationships instead of calculating exact measurements. Although there is generally not a satisfactory all-purpose measure for categorical data, nominal measures could be used to assess the strength of relationships in cross-classification tables, which is often used with chi square tests (Cooper and Schindler, 2003).

The data collected by means of the literature review, annual report screening, focus group, and personal interviews was subjected to content analysis to determine whether the information supports the propositions, or failed to support it. The process followed much the same process as that which is applied in an accusatory justice system, in which evidence is considered *in toto*, to establish the guilt of an accused. In the same way in which it is not expected of an accused to prove his or her innocence, it is not expected to prove a proposition to be incorrect. The research would therefore result in either the propositions being proved, or failed to be proved.

When analysing data in this way, care was taken to look for safeguards to guarantee the validity of the inferences made from it. Two cardinal rules of logic were applied when seeking to make inferences from the data, namely:

- That the inference should be supported by the information collected; and

- That every other possible inference should be excluded as being possible, save the one sought to be made.

Applying these tests to the content analysis of the data collected in this research ensured that the conclusions are both valid and reliable.

10.7 Nature and form of results

The goal of this study was to determine to what extent a better understanding of and improvements in disclosure of executive remuneration levels and practices could contribute to an inclusive and effective corporate governance system in the modern corporation. The literature survey was intended to expose the theory of how different sub-systems interrelate towards the full corporate governance system and all of its control measures. To apply both this theory, as well as the results of a comparison of disclosures in Annual Reports of listed companies in South Africa to the relevant disclosure requirements, to the practical role of disclosure in an inclusive corporate governance framework, semi-structured, personal and group interviews were conducted with a representative sample from listed South African public companies. The information gained from both the review of primary and secondary data sources, and such interviews were thoroughly analysed, and informed the ultimate conclusions and recommendations. The results of this process of analysis provided the basis from where conclusions and recommendations were made in respect of the role of disclosure in an inclusive and effective corporate governance system.

11. ANALYSIS AND RESEARCH RESULTS

The ultimate measure of a man is not where he stands in moments of comfort, but where he stands at times of challenge and controversy. - Martin Luther King

In order to analyse the research data and produce research results to test the propositions developed after the literature review, a three phased approach was adopted.

In the first phase the minimum requirements for disclosure of executive remuneration for companies listed on the Johannesburg Stock Exchange (JSE) in South Africa was collected and collated. The second phase involved the comparison of the disclosure practices of all JSE listed companies with these minimum disclosure requirements, for the purpose of dividing these companies into one of the following three groups:

- Those who disclosed less than the minimum requirements;
- Those who disclosed the same as the minimum requirements; and
- Those who disclosed more than the minimum requirements.

In the third phase, personal interviews and a focus group were conducted with executives, relevant staff and board members of companies selected as part of the sample for each of the above categories.

The data collected by means of the literature review as well as the three data collection phases was then analysed for the purpose of making conclusions regarding the research questions and propositions for this study.

Each one of these phases were intended to produce meaningful outcomes, or results. In the first phase a comprehensive list of the disclosure requirements for listed companies in South Africa at the time of the research was collated. This also informed the content of the Annual Report Disclosure Compliance Index used in phase 2 of the research (Annexure J). The second phase produced both the research sample, as well as meaningful qualitative analysis of disclosed content in the annual reports of companies listed on the JSE in South Africa. The third phase produced qualitative data from the interviews and focus group.

11.1 Phase 1: Disclosure requirements

The minimum executive remuneration disclosure requirements for companies listed on the JSE in South Africa are to be found in relevant legislation relating to public companies, the King Reports on Corporate Governance (King I and King II), and the JSE Listing Requirements. At present, locally listed companies are obliged to comply with the listing requirements of the JSE and the South African Companies Act, 1973. If companies do not comply with King II (and other governance codes) an explanation for non-compliance is expected. Therefore the requirements for disclosure of executive remuneration in South Africa incorporate the minimum requirements referred to in the King II Report, the Companies Act and the listing requirements of the JSE.

The aim of remuneration governance in an organisation is to support an integrated approach for corporate governance, through fundamental principles of sound disclosure of executive remuneration policy and practices. The King II report, which aims to promote the highest standards of corporate governance in South Africa through integrated financial, social, ethical and environmental governance principles, suggests that adopting a philosophy of disclosure is beneficial in mainly two ways. Firstly, it has a shrinking effect in that it deters incidences of malpractice and excessive executive rewards. Secondly, it highlights misconduct and non-performance. Therefore, King II encourages a greater degree of disclosure than that required by statute in South Africa. The corporate governance tendency in South Africa is therefore inclined towards the UK regulatory codes, than the strictly legislated model followed in the USA.

When it comes to disclosure of executive remuneration, the King II Report suggests that good governance means:

- promoting the highest standard of corporate governance, transparency and consistency in the disclosure of remuneration for executive and non-executive directors;
- determining minimum standards for the composition, the terms of reference, and meeting procedures for remuneration committees or other bodies that govern remuneration in the organisation; and
- providing a framework within which the remuneration of executive and non-executive directors can be disclosed, to provide better insight to shareholders or other stakeholders and to promote consistency between organisations.

The following paragraphs set out the requirements for disclosure of executive remuneration in South Africa, as prescribed by relevant legislation, the King I and II Reports on Corporate Governance, and the JSE listing requirements.

11.1.1 Legislation

The South African Companies Act, 1973 (Act 61 of 1973), deals with directors generally in chapter XVIII thereof. This includes aspects such as directors' appointments, duties and responsibilities, disqualification and termination, keeping of registers, and declarations of directors' interests in potentially conflicting transactions of the company. Accounting and disclosure regulations are however contained in chapter XI of the said Companies Act. Companies are, amongst others, obliged to keep such records as may be required to fairly present the state of affairs and business of the company, and to explain the transactions and financial position of the trade or business of the company. The company is furthermore obliged to report annually on certain aspects of its business and affairs, and any misleading or false statement in this regard constitutes a criminal offence by the directors of the company involved.

Amongst the aspects which have to be disclosed in the annual reports of these companies, by virtue of the Companies Act, are:

- Loans to and security for benefits of directors and managers (sections 295 and 296); and
- Directors' emoluments and pensions (section 297).

The particular remuneration disclosure requirements in the annual financial statements of a company, in terms of the above sections of the Companies Act, are:

- In relation to loans and securities to directors, whether made before or after their appointment to the company:
 - the amount and particulars of every loan to each director, including every such loan which has during the applicable financial year been repaid;
 - particulars of every security (and of the transaction to which it relates) which has during the financial year concerned been provided to each director, including every such security which has during the applicable financial year been cancelled;
 - the balance outstanding of every loan; and
 - particulars of every security (and of the transaction to which it relates) provided at any time before the applicable financial year and which is still in existence at the end thereof.
- In relation to annual aggregate directors' emoluments and pensions, while distinguishing between executive and non-executive directors :
 - the amount of the emoluments received by directors for services rendered as directors of the company or of any of its subsidiaries;
 - the amount of the pensions paid or receivable by directors and past directors;
 - the amount of any compensation paid to directors and past directors in respect of loss of office; and
 - details of directors' service contracts.

Directors' emoluments and pensions in terms of the Companies Act include:

- fees paid for services rendered as directors;
- any amounts paid to a director for acceptance of office;
- basic salary;
- bonuses and performance related payments;
- sums paid by way of expense allowances;
- the estimated monetary value of any other material benefits received;
- contributions paid under any pension scheme; and
- gains made on the exercise of shares and share options (the difference between the price paid for the shares and options and the market price of the shares on the date of exercise).

The prescribed financial reporting standards are contained in chapter XVB of the Companies Act, which also establishes a Financial Reporting Standards Council. This Council is tasked to establish and monitor financial reporting standards which promote sound and consistent accounting and reporting practices. The Council has the powers to investigate and report on non-compliance, which is an offence in terms of the Companies Act.

11.1.2 King Codes on Corporate Governance

The King Committee on Corporate Governance was formed in 1992 to consider corporate governance in the context of South Africa, and to promote the highest standards of corporate governance in South Africa. The publication of the King Report on Corporate Governance in November 1994 (King I Report)

institutionalized corporate governance in South Africa. The King I Report went beyond the financial and regulatory aspects of corporate governance, by advocating an integrated approach to good governance through fundamental principles of good financial, social, ethical and environmental practice.

The King I Report emphasized the need to distinguish between accountability (liability to render an account) and responsibility (liability to be called to account). It further developed seven characteristics of good corporate governance, namely:

- Discipline: Commitment to adhere to behaviour that is universally recognized and accepted to be correct and proper.
- Transparency: The measure of making necessary information available publicly, candidly, accurately and timely.
- Independence: Extent of mechanisms to minimize or avoid potential conflicts of interest.
- Accountability: Effective mechanisms to allow responsible parties to render an account for their actions.
- Responsibility: Behaviour that allows for members to be called to account.
- Fairness: Taking into account all those who have an interest in the company and its future.
- Social responsibility: Non-discriminatory, non-exploitative and responsible treatment of environmental and human rights issues.

As a result of many political, legislative and business developments since 1994, the King Committee reviewed corporate governance standards and practices in South Africa, under the following four guiding principles:

- To review the King I Report for currency against local and international developments;
- To review the proposed “inclusive approach” for sustainable success of companies;
- To recognize increasing importance of non-financial issues, and reporting thereon; and
- To recommend how the success of companies can be measured through the “balanced scorecard” approach for reporting.

The King Report on Corporate Governance 2002 (King II Report) was therefore published in March 2002.

Although the King Codes did not formulate specific and detailed executive remuneration disclosure requirements, it nevertheless underscored the requirements for disclosure of executive remuneration as appears in the Companies Act and JSE listing requirements. The King II Report however, in relation to the disclosure of executive remuneration, expanded on the requirements set in terms of the Companies Act in that companies should provide full disclosure of directors’ remuneration on an individual as opposed to an aggregate basis, giving details of earnings, share options, restraint payments and all other benefits. Annexure M summarises the King II guidelines on the components of executive remuneration packages. The overriding principle of full

disclosure by directors on an individual basis should, in terms of King II, also apply to all share schemes and any other incentive schemes proposed by management. The King II Report furthermore requires that companies should establish a formal and transparent procedure for developing a policy on executive remuneration, which should be supported by a Statement of Remuneration Philosophy in its annual report.

On 25 February 2009 a Draft Code of Governance was published for public comment by the King Committee on Corporate Governance. This draft code emphasized the role of ethical leadership, sustainability and corporate citizenship in a good corporate governance framework. After consideration of comments thereon, the King Code of Governance for South Africa, 2009, was published on 01 September 2009, and immediately became known as the King III Report. The King III Report came into operation in South Africa on 01 March 2010. According to Van Wyk (2009) it shows three important changes in emphasis from the King II Code, namely the applicability, structure and focus thereof. He adds that especially the structure of King III reminds more of a handbook on international best practice than quasi legislation, which characterised both King I and King II.

In terms of King III, sustainability reporting is required as an integrated mechanism to enable a broad group of diversified stakeholders to determine the real value of an organisation more easily and effectively. The King III Code emphasizes an inclusive approach to governance by recommending that boards also consider the legitimate interests and expectations of stakeholders other than shareholders, insofar as it is in the best interests of the company.

“The point the Code tries to make is that sustainability does not ultimately lie in the reporting per se, but in incorporating sustainability in the strategy of the organisation. Reporting is therefore only an outcome”

(Lindie Engelbrecht, CEO: Institute of Directors South Africa)

The ultimate aim of the King III Report seems to be to encourage companies to do the right thing, and to leave the monitoring of compliance therewith with the stakeholders of each company (Visser, 2009). The King III Code therefore represents a call for all companies, irrespective of its size, to return to basic business ethics. This conforms to one of the fundamental principles that underscored the development of the King I Report, namely that it is not possible to regulate personal or corporate ethics by means of legislation. It is also in accordance with the literature review (Robins, 2006; Shim, 2006) which showed that strictly legislated corporate governance control measures tend to be counter-productive in that it leads to a strong compliance with the letter of the law rather than the spirit of the law. The self-regulation preferred in the King Codes, as with most other voluntary codes across the world, is deliberately in sharp contrast with the very strictly legislated corporate governance environment in the USA under the Sarbanes Oxley Act which, according to King III is less effective and more costly than a principles-based approach. The Sarbanes Oxley Act was essentially passed in the USA as a direct result of the collapse of major USA corporations due to the failure of its corporate governance control measures to effectively deal with unethical business practices by corporate executives. The King III Report, as well as its predecessors, however only constitutes principles rather than rules, and it is for companies to decide to what extent it will abide with these principles. It is

therefore rather a principles-based code of good corporate governance (as appears from the literature review to be voluntary code best practice), rather than a strictly regulated or compliance driven code which often leads to blind compliance with the letter of the law.

The introduction to the King III Code therefore eloquently suggests that “*Good governance is essentially about effective leadership*”. It adds that, in this view, leadership is based on ethical values of responsibility, accountability, fairness and transparency, through which responsible leaders direct companies towards sustainable economic, social and environmental performance (King III; 2009).

One of the most fundamental developments under the King III Code is the statement that a rules-based corporate governance framework (commonly referred to as “comply or else”) similar to that followed in the USA under the Sarbanes-Oxley Act, would not be practical for all organisations, and would not be effective in terms of the massive compliance costs brought about by it. In contrast, the King III Code prefers and builds on the UK model of setting voluntary principles with which companies should comply, or explain its failure to comply therewith, which approach was also favoured by the King II Report. In common parlance, this has become known globally as the “comply or explain” principle. The King III Code however, in following the Tabaksblat Code in the Netherlands, requires that the principles identified in the code be applied by all business entities, and that the failure to apply those principles be explained. This is described in the King III Code as an “apply or explain” principle.

It is unfortunate that the King III Code did not extend this “apply or explain” to an “apply **and** explain” principle, which could provide not only for an explanation of a failure to apply set principles, but could also provide an explanation of how the principles have been interpreted and applied. The “apply or explain” principle is intended to guard against a mere tick-box exercise as a governance tool. In its introduction, the King III Code states that a “comply or explain” approach could denote a mindless response to the compliance requirements and recommendations, whereas the “apply or explain” approach shows an appreciation that it is often more important how principles have been applied than merely stating that they have been complied with. In the absence of an “apply and explain” process it is at least questionable how this noble ideal would be achieved.

The King III Code also contains practice notes which are intended to direct business entities in how these principles should be applied. These include more details in relation to what ought to be disclosed in respect of executive remuneration. As suggested in the literature review section of this study, such practice notes could serve a very important role in providing potential best practice suggestions for companies to consider in developing their own sets of governance control measures, in a principles based governance framework such as King III sets out.

Table 10 below sets out the nature of the development from a rules-based to a principles-based corporate governance system, as well as the leading countries in each of these three different systems.

Table 10: From rules-based to principles-based corporate governance

Type of system	Leading country	Explanation
Comply or else	USA	Comply with formal rules to avoid punishment
Comply or explain	UK	Explain failure to comply with rules
Apply or explain	The Netherlands	Explain how broad principles have been applied in the organisation

In relation to the disclosure of executive remuneration, and despite the fact that details in relation to the application of those principles stated in the King III Report will be included in practise notes that are yet to be published, the following principles have already been stated in the King III Code:

- Companies should disclose the remuneration of each individual director;
- The remuneration committee should issue a remuneration report to explain the company's remuneration philosophy and how it has been implemented;
- Effective communication with stakeholders is essential;
- Sustainability reporting should be focused on substance over form, and should transparently disclose information that is material, relevant, accessible, understandable and comparable with past performance of the company; and
- Effective reporting should take place at least once a year.

The intention of the King III Report is therefore to provide principled guidelines for **what** is expected in terms of good corporate governance, **why** specific governance practices are adopted by companies, and **how** the stated principles have been implemented or followed (Engelbrecht, 2009).

It is intended that the King III Code will to an extent mitigate the proclamation of the new South African Companies Act, which is expected to include significantly more strict governance control measures. Visser (2009) suggests that the King I Code raised awareness in South Africa of the concept of corporate governance, while the King II Code institutionalised it in corporate South Africa. She adds that the King III Report seems to seek to build an ethical business culture rather than compliance culture. As will be discussed under the third phase of the research results, this research showed support that a strong “letter of the law” compliance mindset was present under the King II era in South Africa. Only time will tell whether the shift to a focus on applying governance principles under King III, rather than complying with certain minimum standards, will impact on the effectiveness of corporate governance in South African organisations. In theory at least, an integrated governance system based on universally applicable principles supported by flexible control measures, potentially leads to a more appropriate protection of stakeholder interests in different organisations.

11.1.3 JSE Listing Requirements

The JSE Listing Requirements, which applies to all companies listed or wishing to list on the JSE, include, amongst others, a pre-listing statement of how the company has applied the principles set out in the King II Report, and which

should provide sufficient explanations for the benefit of its stakeholders and potential investors. Such statement must also explain the reasons for each and every instance of non-compliance with those principles. Where the disclosure of information required in terms of this section cannot be obtained or is considered to be harmful to the applicant, application may be made to the JSE for non disclosure or reduced disclosure. The decision by the JSE in this regard is final.

Section 7.B.7 of the JSE Listing Requirements, which deals with disclosure of executive remuneration, requires disclosure of the following in the annual report of each company listed on the JSE:

“7.B.7 An analysis in aggregate and by director or proposed director, of emoluments paid or accrued as payable during the last financial period by the company, or group of which the company is a member, directly or indirectly, or proposed to be paid by the company, in their capacity as director(s), or in any other capacity, whether determined by the articles or not, distinguishing separately between executive and non-executive directors, of the following:

- (a) fees for services as a director;*
- (b) management, consulting, technical or other fees paid for such services rendered, directly or indirectly, including payments to management companies, a part of which is then paid to a director of the company;*
- (c) basic salary;*
- (d) bonuses and performance-related payments;*
- (e) sums paid by way of expense allowance;*

- (f) *any other material benefits received;*
- (g) *contributions paid under any pension scheme;*
- (h) *any commission, gain or profit-sharing arrangements;*
and
- (i) *in respect of share options or any other right given which has had the same or a similar effect in respect of providing a right to subscribe for shares ("share options"):*
 - (i) *the opening balance of share options, including the number of share options at each different strike price;*
 - (ii) *the number of share options awarded and their strike prices;*
 - (iii) *the strike dates of differing lots of options awarded;*
 - (iv) *the number of share options exercised and at what prices;*
 - (v) *the closing balance of share options, including the number of share options at each different strike price;*
- (j) *any shares issued and allotted in terms of a share purchase/option scheme for employees (or other scheme/structure effected outside of the issuer which achieves substantially the same objectives as a share purchase/option scheme), usually held as a pledge against an outstanding loan to an employee in a share*

purchase scheme trust, which have not been fully paid for, including the number so issued and allotted, the price of issue and allotment, the release periods applicable to such shares and any other relevant information;

(k) without derogating from the generality of 7.B.7 (a) to (j) above, the directors emoluments disclosed in accordance with 7.B.7 (a) to (j) above must include disclosure of all emoluments received or receivable from the following entities:

- (i) the issuer' holding company;*
- (ii) the issuer's subsidiaries and fellow subsidiaries;*
- (iii) associates of 7.B.7 (k) (i) and (ii) above;*
- (iv) joint ventures of the issuer or of 7.B.7 (k) (i) to (iii) above; and*
- (v) entities that provide management or advisory services to the company or any of 7.B.7 (k) (i) to (iv) above”.*

Fees paid or accrued as payable to a third party in lieu of directors' fees are to be disclosed in a similar manner as that detailed above. If the remuneration receivable by any of the directors of the listed company will be varied in consequence of any transaction, full particulars of the aggregate variation in the remuneration of the applicable directors must be stated. If there will be no variation, a statement to that effect must be included in the annual report.

The JSE Listing Requirements also sets out the issues of King II that companies listed on the JSE have to comply with. These include a narrative statement of how it has applied the principles set out in the King II Code, providing explanation that enables its shareholders and potential investors to evaluate how the principles have been applied, and a statement addressing the extent of the company's compliance with the King II Code and the reasons for each and every instance of non-compliance. In particular, such compliance statement must disclose:

- (a) a policy detailing the procedures for appointments to the board;
- (b) a policy evidencing a clear division of responsibilities at board level to ensure a balance of power and authority, such that that no one individual has unfettered powers of decision-making;
- (c) that the chief executive officer does not also hold the position of chairperson;
- (d) a brief CV of each director; and
- (e) the capacity of each director must be categorised as executive, non-executive or independent.

In addition, the JSE Listing Requirements require that all listed companies must appoint an audit committee and remuneration committee and if required, given the nature of their business and composition of their board, a risk committee and nomination committee. The composition of such committees, a brief description of their mandates, the number of meetings to be held annually and other relevant information must be disclosed.

Van Wyk (2009) states that, as the JSE Listing Requirements in South Africa has incorporated the recommendations of the King I and II Reports to give it almost quasi legislative force, so many other countries which have voluntary codes of governance have incorporated the recommendations thereof into their listing requirements. He adds that the credibility and persuasive nature of codes such as King (South Africa), the Combined Code (UK), the Cromme Code (Germany), and the Tabaksblat Code (the Netherlands), have become so overwhelming over the years that unlisted companies voluntarily choose to comply with the set guidelines.

For this reason it does not seem that the expanded application of King III in South Africa beyond only listed companies would be problematic.

11.1.4 Conclusions

Although disclosure of executive remuneration in South Africa is regulated in terms of a combination of legislation, voluntary compliance codes and regulatory prescripts in the form of the Companies Act, 1973, the King Codes on Corporate Governance, and the JSE Listing Requirements, it essentially follows the UK model of regulation rather than the USA model of strict legislation.

Broadly speaking, the remuneration aspects which have to be disclosed in terms thereof must include:

- (a) basic salary or guaranteed pay, broken down into components of
basic salary and all other costs of employment;

- (b) benefits;
- (c) short-term incentives (including high level design principles or targets);
- (d) long-term incentives (including high level design principles or valuation methodology, or any interest in share capital); and
- (e) severance arrangements.

The particular requirements for disclosure of executive remuneration can be consolidated from the sources set out below.

General over-arching principles:

The remuneration committee of a listed company should prepare a remuneration report for the company, which should include a disclosure of the company's remuneration policy, for approval by the board, and subsequent publication in the annual report of the company. Such report should in addition provide full disclosure of director remuneration on an individual basis, giving details of earnings, share options, restraint payments and all other benefits. Performance-related elements of remuneration should constitute a substantial portion of the total remuneration package of executives, in order to align their interests with that of the shareholders, and should be designed to provide incentives to perform at the highest operational standards. The overriding principle of full disclosure by directors, on an individual basis, should apply to all share schemes and any other incentives schemes proposed by management. There must be full disclosure of the direct and indirect interests of the directors in, and the direct and indirect interest of each director's holding in the share

capital of the listed company, distinguishing between beneficial and non-beneficial interests. The statement should include any change in those interests occurring between the end of the financial year and a date not more than one month prior to the date of the notice of the annual general meeting. Any director who, as a result of a shareholding beneficially held either directly or indirectly of more than 5%, needs to disclose this as a potential conflict of interest. Restraint of trade payments and other benefit details must be managed and disclosed. Any payments received for membership of other companies' boards should be disclosed.

Basic salary plus other costs of employment:

The annual report of listed companies in South Africa must disclose information on individualised executive remuneration, which should include:

- (a) basic salary;
- (b) short- and long term bonuses and performance-related payments;
- (c) sums paid as expense allowances;
- (d) any other material benefits received;
- (e) contributions paid under any pension scheme;
- (f) any commission, gain or profit-sharing arrangements;
- (g) fees for services as a director;
- (h) management, consulting, technical or other fees paid for such services rendered, directly or indirectly, including payments to management companies, a part of which is then paid to a director of the company;

- (i) the directors emoluments disclosed must also include disclosure of all emoluments received or receivable from the following entities:
- the annual report issuer's holding company;
 - the annual report issuer's subsidiaries and fellow subsidiaries;
 - associates of the annual report issuer's holding company and/or subsidiaries;
 - joint ventures of the annual report issuer and/or subsidiaries; and
 - entities that provide management or advisory services to the company or the holding company or any associate companies or subsidiaries.

Short-term incentives

In respect of short term incentive schemes or variable pay plans, companies are required to disclose in their annual reports:

- (a) the amount allocated to the directors in the period(s) under review;
- (b) the high level design principles of the scheme supporting the calculation of the bonus awarded, including the performance targets the director had to achieve (including personal and organisational targets); and
- (c) Any amounts deferred from the short-term incentive scheme granted must be disclosed, as well as the terms and conditions of such deferral.

Long-term incentives or interest in share capital

Long term incentives refer to incentives such as shares, share options, phantom schemes and other such financial instruments. Listed companies in South Africa should disclose the following details regarding long term incentives offered to its executives:

- (a) Compliance with the Securities Services Act (often embodied in companies' insider trading policies).
- (b) A summary of the details and terms of options in issue at the beginning of the financial period, cancelled or issued during the financial period, and in issue at the end of the financial period, as well as the number of securities that may be utilised for purposes of the scheme at the beginning of the financial period, changes in that number during the financial period, and the number of securities available for use for purposes of the scheme at the end of the financial period.
- (c) In respect of any right given that has the same or a similar effect as a share option, by providing a right to subscribe for shares:
 - the opening balance of share options, including the number of share options at each different strike prices;
 - the number of share options awarded and their strike prices;
 - the strike dates of differing lots of options awarded;
 - the number of share options exercised and at what prices; and
 - the closing balance of share options, including the number of share options at each different strike price.

- (d) Any shares issued and allotted in terms of a share purchase / option scheme for employees (or other scheme / structure effected outside of the issuer which achieves substantially the same objectives as a share purchase / option scheme), usually held as a pledge against an outstanding loan to an employee in a share purchase scheme trust, which have not been fully paid for, including the number so issued and allotted, the price of issue and allotment, the release periods applicable to such shares and any other relevant information.
- (e) Any equity awards that vest on an accelerated basis for whatever reason must be disclosed with full motivation for such acceleration.

Annexure N proposes standardised disclosure tables in respect of all components of executive remuneration packages which would satisfy the current South African disclosure requirements, as well as short term and long term incentives, which would allow for ease of comparison across companies. This is especially helpful in an environment characterised by dispersed owners who own interests in multiple companies.

Severance arrangements

Companies must disclose the rules of the severance policy applicable to executive directors, as well as any severance payments paid out or allocated to executive directors in the period under review.

Disclosure requirements in South Africa

Based on the requirements of the Companies Act, 1973, the King Reports on Corporate Governance in South Africa, and the JSE Listing Requirements, the collated disclosure requirements in respect of publicly listed companies in South Africa could be summarised as set out in the Annual Report Disclosure Compliance Index, which appears as Annexure J hereto. This Index was used to analyse the compliance of companies listed on the JSE in South Africa, in relation to disclosure of executive remuneration in the 2007 Annual Reports of all JSE listed companies (excluding those listed under the AltX and Additional categories). Such analysis formed part of the second and third phases of this research, as discussed below.

The key principle in disclosure of executive remuneration is the effective link of executive rewards to both executive and corporate performance. It is specifically for the remuneration committee to establish and monitor such a link, and to align the interests of directors and shareholders in promoting the company's progress towards achieving its strategic objectives and increased stakeholder value. The long term performance of a company must however also be a matter of great concern to the shareholders and other stakeholders of the company. Three fundamental principles underlie stakeholder interests in this area, namely accountability, transparency, and linkage to performance (Greenbury Report, 1995).

Some of its recommendations contained in the Reports set out in Annexure C, and in particular in relation to the disclosure of individual directors' remuneration

have been implemented as formal requirements in the JSE Listing Requirements. For the most part, however, they have been implemented as best practice provisions. The same situation appears in the United Kingdom under the Greenbury Code, Hampel Report, and ultimately under the Combined Code. Both the Greenbury Code and the Hampel Report recommended that statutory controls should be unnecessary in this area, but that there should be clear evidence that companies are complying with the spirit of the best practice frameworks. In South Africa, under the King II Report, a similar expression was made that it would be ineffective to formally legislate against ethics, but that the development of a compliance culture, with both the spirit and letter of the law and regulation, would be more effective. The King III Report adopts the same approach, which is extended to the institutionalisation of a governance culture which could be explained as “apply or explain”.

It is important that companies and their remuneration committees adopt a philosophy of full transparency such that shareholders have access to all the information they may reasonably require to enable them to assess the company's general policy on executive remuneration. In the same way, it is necessary for companies to disclose information to current and potential investors, in order for them to make informed investment decisions, which are based on full and equally available information. It is not just a case of putting a spotlight on companies which are not doing a good job of linking pay to performance, but also in order for companies which are achieving an effective link to be seen to be doing so. Shareholders should be invited specifically to approve all long term incentive schemes on the basis that they relate to performance. The key issue is whether institutional investors need increased

leverage in dialogue with companies that will ensure that the link is a good one. Accountability will only be achieved if there is a framework in place which allows stakeholders to exercise their influence effectively over remuneration policy and practices.

Annexure O summarises the guidelines for the disclosure and determination of remuneration for executive and non-executive directors in South Africa.

11.2 Phase 2: Sample selection and quantitative analysis

The process of comparison of disclosure practices to the minimum disclosure requirements was done by means of comparing the executive remuneration disclosures in the 2007 Annual Reports of all JSE listed companies (excluding those listed under the AltX and Additional categories) to the collated minimum remuneration disclosure requirements, as appears in Annexure J. It was necessary to use the 2007 Annual Reports since not all JSE listed companies had published their 2008 Annual Reports at the time of this phase of the study, and in many cases the 2007 Annual Reports were therefore the latest such published reports.

The purpose of the analysis of remuneration disclosures in the 2007 Annual Reports was to divide the selected JSE listed companies into three groups on the basis of its level of compliance with the minimum remuneration disclosure requirements. These groups were:

- Those who disclosed less than the minimum requirements;
- Those who disclosed the same as the minimum requirements; and
- Those who disclosed more than the minimum requirements.

It was also possible to analyse the executive remuneration disclosures in the annual reports of companies quantitatively, to make conclusions regarding, amongst others, disclosure comparisons across industries, and between sectors within the same industry.

11.2.1 Sample selection

In order to select a sample for this study it was necessary to first study the disclosures of executive remuneration in the 2007 Annual Reports of all companies listed on the JSE (excluding those under the AltX and Additional categories). Such disclosures were evaluated against the criteria in Annexure J, to allocate each of these companies to one of the above categories.

Table 11 below sets out the allocation of JSE listed companies, in aggregate, to each of the categories, while Annexure P presents a list of individual companies allocated to the same categories. Table 11 also distinguishes between companies whose primary listing and operations are in South Africa, and companies which operate primarily outside of South Africa. Although disclosure practices in respect of all of these companies have been analysed quantitatively in this phase of the study, the companies operating mainly outside of South Africa were not considered for selection to the final sample for qualitative interviews, due to logistical, practical and financial considerations.

Table 11: Annual Report disclosure results

Industry	Sector	Disclosure category						Total
		Less than		Exactly what		More than		
		SA	Other	SA	Other	SA	Other	
Raw materials	General mining	2		10	1	2	1	16
	Forestry and paper			2			1	3
	Chemicals			4		1		5
	Diamonds and semi precious stones			5			1	6
	Gold mining	3	1	6	2			12
	Industrial metals	2	1	2		3		8
	Platinum	1	1	2	1	3		8
	Coal	1	1					2
	Sub total	9	4	31	4	9	3	60
Industrial	General industrial			6		3		9
	Electric and electronic	1	1	7		2		11
	Industrial engineering			5		1		6
	Industrial transport	1		3	1	2		7
	Construction and materials			18		1		19
	Support services	2		14				16
	Sub total	4	1	53	1	9	0	68
Financial	General financial	4		13		2	1	20
	Banks			3		4		7
	Equity investment instruments	3		5		1		9
	Property	17		13				30
	Life assurance	1		3		2	1	7
	Non-life insurance			4				4
	Sub total	25	0	41	0	9	2	77
Consumer services	General retail	4	1	8		6		19
	Media	1		1		3		5
	Travel and leisure	7	1	6		4		18
	Food and medicine retail	1		1		1		3
	Sub total	13	2	16	0	14	0	45
Consumer goods	Beverages	1		2		1		4
	Household goods					1		1
	Automobiles and parts	1		3				4
	Leisure goods	1		1				2
	Personal goods	2		2			1	5
	Food producers	3		6		4		13
	Sub total	8	0	14	0	6	1	29
Technology	Software	4		9		3		16
	Hardware			1		1		2
	Sub total	4	0	10	0	4	0	18
Venture capital	General	3	1	3	1	1		9
	Sub total	3	1	3	1	1	0	9
Development capital	General	4		1		1		6
	Sub total	4	0	1	0	1	0	6
Telecommunications	Mobile	1				2		3
	Fixed line			1				1
	Sub total	1	0	1	0	2	0	4
Health care	Pharmaceutical			2				2
	Health services	1		1				2
	Sub total	1	0	3	0	0	0	4
Oil and gas	General		1			1		2
	Sub total	0	1	0	0	1	0	2
Total		72	9	173	6	56	6	322
		81		179		62		

The final sample for the qualitative part of this study was determined by first calculating a 10% sample figure for the aggregate of each of the three categories into which companies were divided. For the purpose of this phase of the study, only companies listed under the five major industries on the JSE were considered. These were the Raw Materials, Industrial, Financial, Consumer Services, and Consumer Goods industries. The respective aggregate figures appear in Table 11 above. Again, for logistical, practical and financial reasons, only companies operating mainly in South Africa were considered for inclusion in the final sample for the qualitative part of this study.

The next step in developing the final sample was to make a proportionate allocation of companies in each of the above five industries to the total sample in each of the three categories, and thereafter to make a further proportionate allocation to each sector within each industry. This was done to ensure that the final sample was representative of, and proportionate to:

- each of the three categories into which companies have been allocated for this study, based on their executive remuneration disclosures in their 2007 Annual Reports;
- the five major industries under which listed companies are registered on the JSE; and
- the different sectors within each of those industries.

In determining the final companies selected from the sectors, industries and study categories, an attempt was made to allow for sector and industry comparisons across the three categories into which companies were divided on

the basis of their executive remuneration disclosure practices. Table 12 below displays the composition of the final sample for the qualitative component of this study. It needs to be noted that companies selected for the qualitative interviews on their executive remuneration disclosure practices did not necessarily cover all sectors and categories in a particular industry. For that reason the final sample does not cover all sectors within an industry, but rather such sectors which are representative of the largest number of companies in a particular industry. The final sample per sector has been selected to be both representative of the largest number of companies per sector, as well as to allow for realistic comparisons across disclosure categories.

Table 12: Final sample composition for qualitative analysis

Industry	Sector	Disclosure category		
		Less	Exactly	More
Raw materials	General mining		1	
	Forestry and paper			
	Chemicals			
	Diamonds and semi precious stones			
	Gold mining	1	1	
	Industrial metals			
	Platinum		1	1
	Coal			
	Sub total	1	3	1
Industrial	General industrial		1	1
	Electric and electronic		1	
	Industrial engineering		1	
	Industrial transport			
	Construction and materials		1	
	Support services	1	1	
	Sub total	1	5	1
Financial	General financial		1	
	Banks		1	1
	Equity investment instruments			
	Property	1	1	
	Life assurance	1	1	1
	Non-life insurance			
	Sub total	2	4	2
Consumer services	General retail		1	1
	Media			
	Travel and leisure	1	1	
	Food and medicine retail			
	Sub total	1	2	1
Consumer goods	Beverages			
	Household goods			
	Automobiles and parts			
	Leisure goods			
	Personal goods			
	Food producers	1	1	1
	Sub total	1	1	1
Total		6	15	6

11.2.2 Quantitative analysis of disclosures in Annual Reports

In analysing the content of the executive remuneration disclosures in the 2007 Annual Reports of those JSE listed companies that formed part of the research population for the purpose of this study, it was necessary for the researcher to physically read all Annual Reports of South African companies selected for the second phase of the research. This was especially necessary in view of the lack of uniformity or centrality of executive remuneration disclosures in these reports. Where some companies included specific chapters dealing with all aspects of executive remuneration therein, companies at the other end of the scale made vague, and often meaningless, disclosures in multiple locations in these reports, often with little or no cross referencing. One of the interesting observations in this regard was disclosures in CEO report sections, which are not subject to shareholder votes. This practice at least potentially borders on misleading shareholders by withholding key forward looking (for example potential acquisitions) and key backward looking (for example adjustment of financial targets) information from them.

The executive remuneration disclosures in these annual reports were therefore carefully extracted from wherever they appeared in the annual reports, and compared with the collated disclosure requirements, as contained in the Annual Report Disclosure Compliance Index in Annexure J. From there it was possible to categorise companies into one of the research groups, based on the measure of their disclosure compliance in relation to the minimum requirements.

It was possible from this analysis to identify some trends which distinguished between companies in each of the three research categories. In particular, there were observable differences in relation to the place or places where different aspects of executive remuneration were disclosed in the Annual Reports of companies, and the ease of accessibility of those Annual Reports. Furthermore, significant differences in the disclosure of executive remuneration content were observed. These differences related to both executive remuneration levels and the process for determination of executive remuneration packages.

It was possible to identify aspects which distinguished between companies whose executive remuneration disclosures were less than or more than the minimum disclosure requirements. These differences have been summarised in Table 15 below.

It was also possible to analyse the quantitative data obtained through the analysis of the content of the 2007 Annual Reports of these listed South African companies by means of the chi-squared test, to establish whether there was a relationship between the executive remuneration disclosure practices of JSE listed companies and the different industries under which those companies are listed.

Location of executive remuneration disclosures in Annual Reports

One of the most observable differences in the presentation of executive remuneration disclosures in the 2007 Annual Reports of JSE listed companies was the location where such disclosures were made in these reports. There

was no consistency amongst South African companies listed on the JSE in respect of the location, appearance or content of executive remuneration disclosures. It was in most instances a tedious task to locate the full extent of what executive remuneration disclosures required of companies in terms of the Companies Act, King Reports and JSE listing requirements.

Figure 13 below indicates the sharp differences in the locations where executive remuneration disclosures appeared in the 2007 Annual Reports of companies listed per industry on the JSE in South Africa. It is clear that most companies across all industries made their executive remuneration disclosures only in the notes to their financial statements, except for companies in the Industrial sector where executive remuneration disclosures were predominantly made in multiple locations in their Annual Reports. The second most prevalent trend across most industries was to make executive remuneration disclosures in multiple locations in Annual Reports. This practice was especially prominent in the Industrial, Financial, Consumer Goods and Services, and Technology industries. Although disclosure of executive remuneration in a separate chapter of the Annual Reports was not prevalent in the smaller industries, it was very prominent in at least the Raw Materials industry, where it was the second most prevalent disclosure location after disclosures in the notes to financial statements.

Figure 13: Executive remuneration disclosure locations per industry

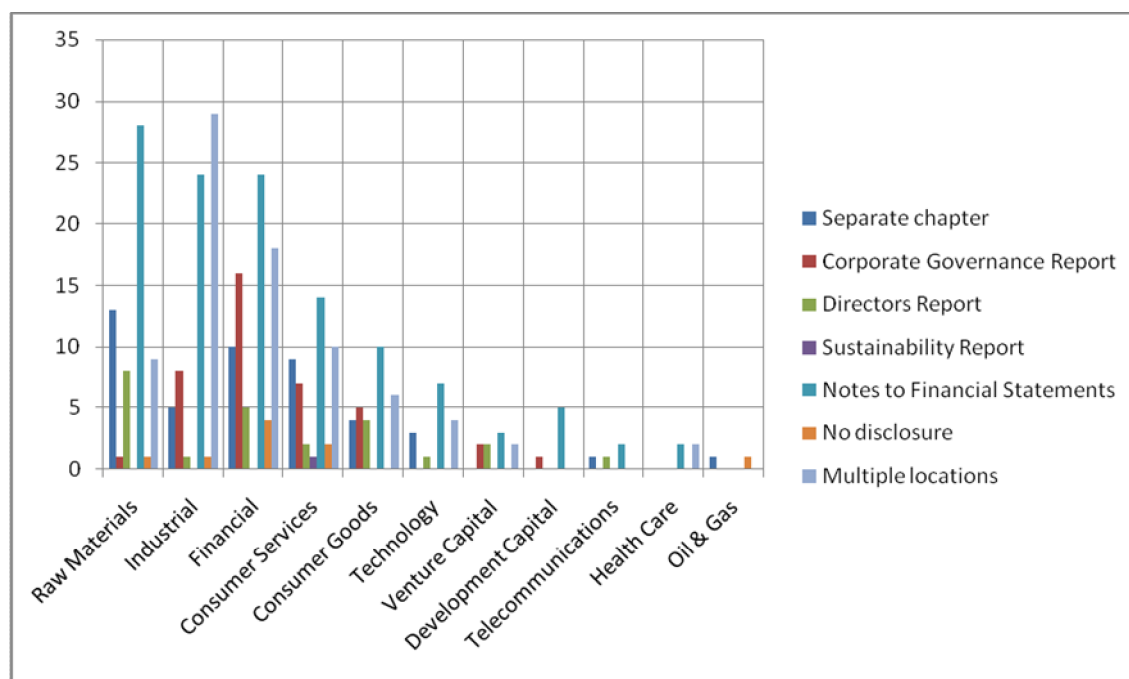
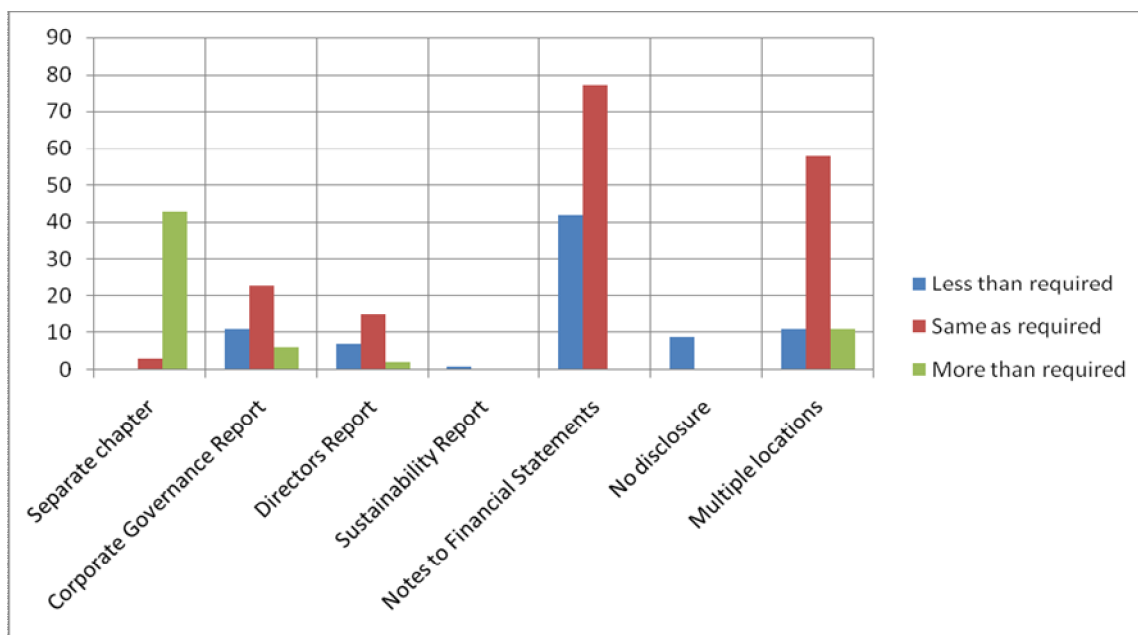


Figure 14 below indicates the differences in locations of executive remuneration disclosures across the three research categories. Amongst companies which disclosed less than the minimum executive remuneration disclosure requirements it was observed that these companies predominantly made such disclosures in the notes to their financial statements, while some made no disclosures at all. Under companies which disclosed exactly what is required such disclosures were made primarily in the notes to their financial statements, and in multiple locations across their Annual Reports. The similar disclosures by companies which disclosed more than the executive remuneration disclosure requirements were predominantly found in separate chapters in their Annual Reports, which chapters dealt with issues related to executive remuneration.

Figure 14: Executive remuneration disclosure locations per research category



Annexure Q displays the analysis table containing the figures per industry in respect of the disclosure locations upon which figures 13 and 14 are based.

Although most companies which fall into the categories where their respective executive remuneration disclosures are either less than or the same as what is required, disclosed the levels of their executive remuneration only in a note or notes to its financial statements, there was nevertheless no consistency in where such a note or notes appeared in relation to other common notes to financial statements. In the case of companies which disclosed less than the minimum requirements, 42 out of 81 companies (51.85%) made executive remuneration disclosures only in the notes to their financial statements, whereas in respect of companies which disclosed exactly what is required, 77 out of 176 companies (43.75%) did the same. In sharp contrast, none of the companies in the category where disclosures in excess of the minimum

requirements were made, only made executive remuneration disclosures in the notes to their financial statements. These companies however showed a strong tendency to consolidate their executive remuneration disclosures in a single and comprehensive remuneration report chapter (43 out of 62 companies, or 69.35%). In comparison, companies which disclosed less than or the same as the minimum requirements show respective scores of 0% (0 out of 81 companies) and 1.70% (3 out of 176 companies) for executive remuneration disclosures in a single remuneration report chapter.

A total of 80 out of 319 companies made their executive remuneration disclosures in multiple locations in their Annual Reports. Portions of such disclosures were typically distributed across the following sections of their Annual Reports:

- corporate governance report;
- directors' report;
- sustainability report; and
- notes to the financial statements.

Cross referencing to additional disclosure items were rarely done. Table 13 below indicates the distribution of the numbers of companies which made executive remuneration disclosures in multiple locations in their 2007 Annual Reports, to each of the individual locations. It is clear that, where companies made their executive remuneration disclosures in multiple locations, 86% of these companies (70 out of 81) made disclosures in the notes to their financial statements as well as in some other section in their Annual Reports. In all of these disclosures in the notes to financial statements, companies disclosed only

the actual levels and components of executive remuneration, without any narrative on the rationale for the composition of those executive remuneration packages disclosed. The disclosures in different sections to the notes on their financial statements were, in most cases, also insufficient for stakeholders to understand the underlying philosophy and metrics used to determine the levels of executive remuneration disclosed in the notes to their financial statements.

Table 13: Location of multiple disclosures

Location of multiple disclosures				Number of companies
Corporate Governance Report	Directors' Report	Sustainability Report	Notes to Financial Statements	
X			X	50
	X		X	12
X	X			11
X	X		X	5
		X	X	3

In addition to these dispersed disclosures, it was often the case that the fractional disclosures were not sufficiently detailed to inform either existing shareholders or other stakeholders of the underlying factors that inform both the levels of executive remuneration and the process for determining executive remuneration packages. A total of 22 companies made aggregated executive remuneration disclosures in relation to the components of the total remuneration packages paid to executives of these companies. It was therefore not possible in these cases to distinguish between salaries, benefits, and other performance related incentives paid to these executives. Table 14 below indicates the location of these aggregated remuneration figures in the relevant Annual Reports.

Table 14: Location of aggregated remuneration tables

Location of aggregated remuneration tables		Total
Notes to Financial Statements	Directors' Report	
20	2	22

In the categories which relate to disclosures which are either less than or the same as what is required, there were almost no cases where there were any set performance criteria disclosed for the payment of short and long term incentives to executives. The result is that shareholders and other stakeholders of these companies were potentially not sufficiently informed regarding executive remuneration from a forward looking perspective.

In sharp contrast to this, companies which have been placed into the category that relates to executive remuneration disclosure in excess of what is required, published a separate and comprehensive single chapter on executive remuneration in their Annual Reports. In almost all of these instances these chapters not only identified comprehensive details regarding the remuneration philosophy applied by the companies in relation to executive remuneration, but also dealt with the metrics that informed the levels of remuneration, short term and long term incentives, the process for determination of executive remuneration, and any performance criteria which informed the allocation of short and long term incentives. Not only the ease of reference of these remuneration chapters, but also the comprehensiveness thereof, allow shareholders and other stakeholders of these companies to both exercise control over executives and make informed investment decisions which are

based on symmetry of information. Forward and backward looking aims of disclosure were satisfied in this way.

Table 15 below summarises the most observable characteristics of the executive remuneration disclosures found in the three categories into which companies have been divided on the basis of its compliance with minimum disclosure requirements.

Table 15: Differences in disclosure characteristics

Less than required	Exactly what required	More than required
Aggregate disclosures.	Fragmented disclosures in Reports.	Comprehensive remuneration chapter.
No stated remuneration philosophy.	Weak statement of remuneration philosophy.	Detailed remuneration philosophy.
No performance criteria.	Weak link between performance and reward.	Details of link between performance and reward.
Different locations.	Different locations.	Single location in reports.
Lacking details of LTI's.	Details of LTI's awarded.	Details of LTI criteria and awards.

The questions contained in the Interview Schedule for the qualitative part of this study have been developed in such a way as to elicit responses from participants on the reasons for these differences. The results thereof are discussed in more detail below.

Content of disclosures

In analysing the content of the executive remuneration disclosures in the 2007 Annual Reports of South African companies listed on the JSE, a combination of both quantitative and qualitative analysis methodologies have been used. In

order to test significance of collected data, one of two types of tests could be applied, namely parametric or nonparametric tests.

Parametric tests are used in respect of interval or ratio measurements, while nonparametric tests are used to test propositions with nominal and ordinal data. Cooper and Schindler (2003) suggest that the researcher should consider the following three questions when choosing a particular significance test. These questions, which also informed the choice of a significance test in this research, are:

- How many samples does the test involve?
- If more than one sample is involved, are the individual cases related or independent?
- Is the measurement scale nominal, ordinal, interval or ratio?

In this part of the study, nominal data was collected from the 2007 Annual Reports of South African companies listed on the JSE. Nonparametric tests are the only ones which can be used with nominal data. Nominal data refer to information on a variable that can be grouped into two or more categories that are mutually exclusive and collectively exhaustive. Nominal data has a classification, but no order, distance or origin.

CONTENT ANALYSIS

Content analysis is a technique which can be used to structure “open-ended” data for meaningful analysis (Harwood and Garry; 2003). It makes it possible for the researcher to reduce certain phenomena or events into categories which

would make it easier for the researcher to analyse and interpret the data, by systematically evaluating the symbolic content of all forms of communication at different levels (Kolbe & Burnett; 1991). It can be used together with other analysis methods in a multi-method study.

For the purpose of this phase of the study, the approach was to analyse the content of the executive remuneration disclosures in the 2007 Annual Reports both pragmatically (analysing likely cause and effect) and semantically (analysing meanings). In this way, it was possible to unobtrusively interpret specific disclosure practices and trends by reducing separate aspects of disclosure to groups which allow for easier analysis. It also provided an empirical starting point for generating valuable data about the nature and effects of specific executive remuneration disclosures, which could serve as a basis for the qualitative interviews in the latter part of this study.

Although the differences in the locations where companies made their executive remuneration disclosures in their 2007 Annual Reports has already been dealt with above, the typical content in each of those disclosure locations needs to be recorded. Table 16 below therefore sets out the commonly disclosed executive remuneration aspects in each of the disclosure locations identified above.

Table 16: Typical content per disclosure location

Disclosure location	Disclosed content
Corporate Governance Report	<ul style="list-style-type: none"> • Composition and mandate of Remuneration Committee • Attendance at Remuneration Committee meetings • Short, broad statement of remuneration philosophy
Directors' Report	<ul style="list-style-type: none"> • Brief remuneration philosophy • Broad performance criteria for incentive awards • Remuneration tables
Sustainability Report	<ul style="list-style-type: none"> • Brief, retention-focused remuneration strategy
Separate Remuneration Report	<ul style="list-style-type: none"> • Membership, mandate and charter of Remuneration Committee • Detailed remuneration philosophy • Strategies for different reward components • Determination process and criteria for remuneration packages • Performance metrics for short and long term incentives • Details of short and long term incentives awarded/exercised
Notes to Financial Report	<ul style="list-style-type: none"> • Tables with levels and composition of remuneration packages • Separate table with details of incentives awarded and exercised

Table 17 below reflects the results of the analysis of the 2007 Annual Reports after the 322 JSE listed companies were divided into one of the three research categories reflecting its executive remuneration disclosure practices relative to the minimum disclosure requirements in this regard. It expresses such divisions both in terms of the number of companies per industry and per group, as well as the relative percentages for each of the three groups per industry.

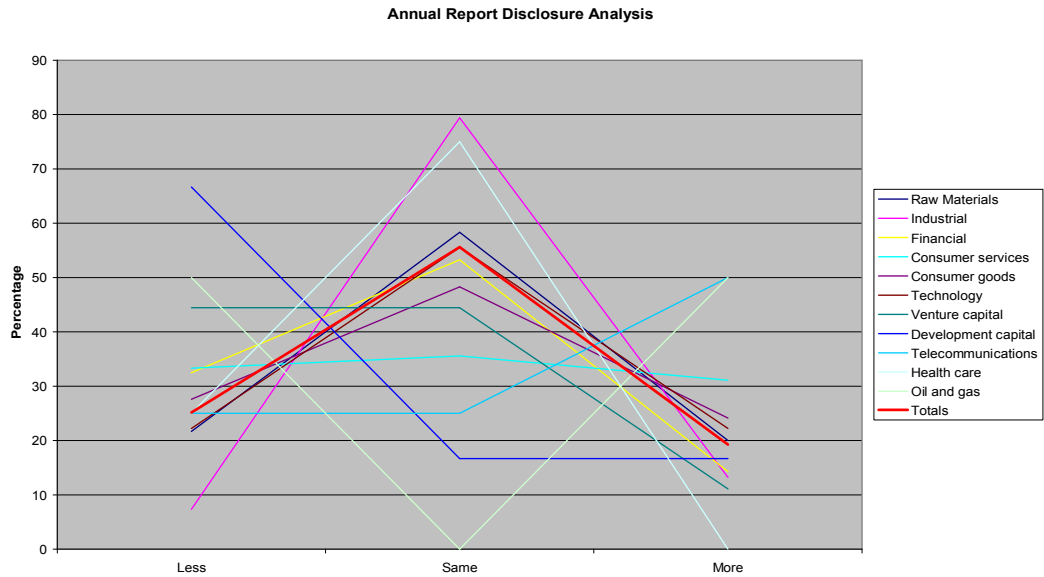
Table 17: 2007 Annual Report Disclosure Distribution

Industry	Executive remuneration disclosure					
	Less		Same		More	
	No.	%	No.	%	No.	%
Raw Materials	13	21.67	35	58.33	12	20.00
Industrial	5	7.35	54	79.41	9	13.24
Financial	25	32.47	41	53.25	11	14.29
Consumer services	15	33.33	16	35.56	14	31.11
Consumer goods	8	27.59	14	48.28	7	24.14
Technology	4	22.22	10	55.56	4	22.22
Venture capital	4	44.44	4	44.44	1	11.11
Development capital	4	66.67	1	16.67	1	16.67
Telecommunications	1	25.00	1	25.00	2	50.00
Health care	1	25.00	3	75.00	0	0.00
Oil and gas	1	50.00	0	0.00	1	50.00
Totals	81	25.16	179	55.59	62	19.25

From the above table it can be seen that 74.84% of South African companies listed on the JSE complied with executive remuneration disclosure requirements for listed companies in South Africa in their 2007 Annual Reports. Figure 15 below shows a fair consistency in the distribution of companies across all industries into the three research categories, with the majority of industries following a pattern of disclosure which was on par with what is required in terms of disclosure.

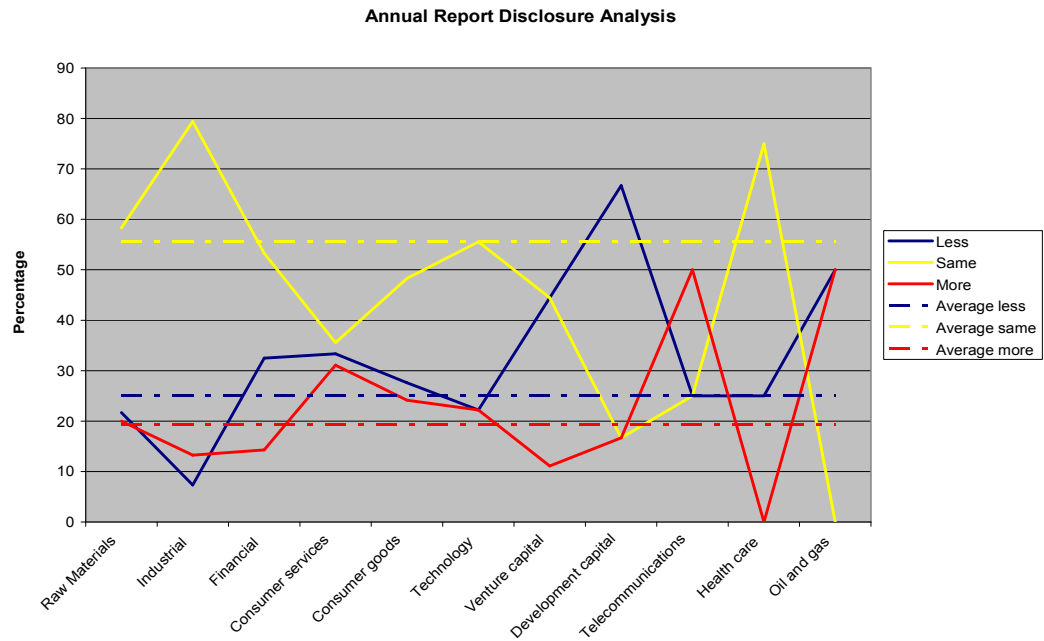
The major discrepancies from the common curves in Figure 15 came from the Oil and Gas, Development Capital, and Telecommunications industries, where there were so few companies that constitute the industry population that even a single exception would distort the relationship. Reasons for distinctions amongst the three research categories became more apparent during the qualitative interview phase, reported on below.

Figure 15: Annual Report Disclosure Analysis per category



When the average disclosure percentages for each of the research categories were added to the data contained in Figure 15 above, the graph appears as in Figure 16 below. Figure 16 shows the deviations per industry from the distribution into the three research categories for all industries combined.

Figure 16: Annual Report Disclosure Analysis per industry



It is clear from the solid yellow line in Figure 16 above that most industries fall more in the research category which relates to disclosures which are the same as what is required. The only exceptions are in the Development Capital, and Oil and Gas industries, where there were six and two companies in total respectively, and which accounts for the deviations.

Annexure R indicates the relative distributions per industry of listed South African companies, into one of the three research categories. The graphs are expressed as a percentage of the total number of companies per industry, to enable comparisons across industries from a common base. Observations regarding each of the graphs have been made and appear underneath the respective graphs in Annexure R.

The following observations and conclusions could be made from the above analysis:

- In most industries and sectors within those industries, companies tended to make executive remuneration disclosures which are on par with the minimum disclosure requirements in South Africa;
- Industries and sectors which are characterised by small numbers showed some deviations from the general trend, which could be attributed to the statistical impact of the smaller numbers in those industries and sectors;
- There was a general sub-trend for more companies across larger sectors and industries to rather disclose more instead of less than what is required, but still fewer companies than those that disclose exactly what is required;

- Companies in the Banking, Media, Household Goods, Oil and Gas, and Mobile Telecommunications sectors tended to disclose more than what is required;
- Companies in the Coal Mining, Travel and Leisure, Oil and Gas, and Development Capital sectors tended to disclose less than what is required;
- A significant number of companies made executive remuneration disclosures in multiple locations in the same report, without any or appropriate cross referencing; and
- Most companies in the categories which relate to executive remuneration disclosures that are less than or the same as the minimum requirements tended to make disclosures in only the notes to the financial statements, whereas companies which disclosed more than the minimum disclosures tended to do so in a separate remuneration report chapter.

It was not possible to make a clear conclusion from the quantitative content analysis of the executive remuneration disclosures in the 2007 Annual Reports of companies listed on the JSE as to the specific reasons for their choices of disclosure practices, or the extent to which these disclosures were strategically considered before publication. These issues could only be explained through the qualitative data obtained during the interviews phase of this research, which is dealt with below.

CHI-SQUARE TEST

In this part of the study, all companies listed on the JSE were considered for the analysis of their respective disclosures of executive remuneration in their 2007 Annual Reports. Propositions have therefore been formed in relation to a population or single sample, which allows for valid testing of the propositions.

A number of different nonparametric tests may be used in a single sample situation, depending on the measurement scale used and other conditions. In the case of measurement of nominal data, either the binomial test or chi-square test could be used. The binomial test is appropriate where the population consists of only two classes, and the sample size is too small to use a chi-square test. The chi-square test is widely used where nominal data is grouped into two or more nominal categories.

The chi-square test is appropriate to determine whether there is evidentiary support for an inference that two qualitative variables are related to each other (Keller and Warrack, 1997). Cooper and Schindler (2003) suggest that the chi-square (χ^2) test is probably the most widely used nonparametric test of significance, and is particularly useful in tests involving nominal data, as in this study. The chi-square test is used to test for significant differences between the observed data distribution amongst certain categories and the expected such distribution, based on the null proposition.

The quantitative data obtained by means of the analysis of the content of the 2007 Annual Reports of South African companies listed on the JSE (excluding those listed under the AltX and Additional categories) was therefore analysed

by means of the chi-square test, which was considered to be the most appropriate nonparametric test for the purpose of this research.

In this research, the two variables tested in relation to each other were firstly listed companies on the JSE, and secondly executive remuneration disclosure practices. The chi-square test is appropriate because of the fact that nominal data was collected, and there were sufficient observations for the data to be representative of the total population of South African companies listed on the JSE.

The chi-square test was performed in terms of the following six steps:

- Developed a null and alternative propositions;
- Used the single sample chi-square test to compare the observed distribution to the expected or hypothesized distribution of data;
- Used a significance level of 0.05, which offers a 95% probability ratio;
- Calculated the expected distribution of data;
- Calculated the critical value at a 0.05 level of significance by using the applicable statistical tables; and
- Interpreted the test results.

The null proposition must be rejected if the calculated value of the chi-square test is greater than the critical value, at a 95% confidence interval. For this part of the study the null proposition was that there was no relationship between JSE listed industries in South Africa and the extent of executive remuneration disclosure practices of companies listed under those industries. The alternative proposition was that there was such an association.

For the purpose of analysing the data from Table 18 below, only the data in respect of the five largest industries have been considered. This was not only consistent with the selection of a sample for the qualitative part of the study, but eliminated the data from industries where there were too few companies to apply a chi-square test to it. Numbers have been rounded to two decimals.

Table 18: Industry Disclosure Cross-tabulation

Industry	Value / Test	Disclosure			Total
		Less	Same	More	
Raw Materials	Observed value	13	35	12	60
	Expected value	14.2	34.4	11.4	60.0
	% within industry	21.7%	58.3%	20.0%	100.0%
	Standard residual	-0.3	0.1	0.2	
Industrial	Observed value	5	54	9	68
	Expected value	16.1	39.0	12.9	68.0
	% within industry	7.4%	79.4%	13.2%	100.0%
	Standard residual	-2.8	2.4	-1.1	
Financial	Observed value	25	41	11	77
	Expected value	18.2	44.2	14.6	77.0
	% within industry	32.5%	53.2%	14.3%	100.0%
	Standard residual	1.6	-0.5	-0.9	
Consumer Services	Observed value	15	16	14	45
	Expected value	10.6	25.8	8.5	45.0
	% within industry	33.3%	35.6%	31.3%	100.0%
	Standard residual	1.3	-1.9	1.9	
Consumer Goods	Observed value	8	14	7	29
	Expected value	6.9	16.6	5.5	29.0
	% within industry	27.6%	48.3%	24.1%	100.0%
	Standard residual	0.4	-0.6	0.6	
Total	Observed value	66	160	53	279
	Expected value	66.0	160.0	53.0	279.0
	% within industry	23.7%	57.3%	19.0%	

The calculated value in terms of this test has been determined by calculating the sum of the square of the observed minus the expected values for each cell over the expected value of the same cell, which could be stated in terms of the following formula:

$$X^2 = \sum_{i=1}^5 \left(\frac{(O_i - E_i)^2}{E_i} \right)$$

Where: i = industry
 O = observed value
 E = expected value

If the standard residuals in Table 18 above were smaller than -1.96 or bigger than 1.96, then there would be an indication of an association between the two variables. It therefore appeared that there was such an association in the Industrial and Consumer Services industries. In the Industrial category the standard residual in the category which refers to disclosures which are less than what is required, was -2.8, while the standard residual in the category which refers to disclosures which are the same as what is required, was 2.4. In the Consumer Services industry standard residual in the category which refers to disclosures which are the same as what is required, was -1.9, while standard residual in the category which refers to disclosures which are more than what is required, was 1.9.

The results of the chi-square tests are therefore as indicated in Table 19 below, and the symmetric measures in Table 20 below. The critical value used in terms of the table in Annexure S amounts to 15.51.

Table 19: Chi-square test results

	Value	Degrees of freedom (Df)	Asymp. Sig. (2-sided)
Pearson Chi-square	28.390 ¹	8	0.000
Likelihood Ratio	30.383	8	0.000
Linear-by-linear association	0.425	1	0.514
Number of valid cases	279		

¹ Zero cells (0.0%) have expected count less than 5. The minimum expected count is 5.51.

Table 20: Symmetric Measures

	Value
Phi	0.319
Cramer's V	0.226
Number of valid cases	279

The symmetric measures measure the strength of the associations between the extent of disclosures and the different industries. The results indicate the strength of association as follows:

- Between 0.1 and 0.3 : Weak association
- Between 0.3 and 0.5 : Moderate association
- Above 0.5 : Strong association

The following conclusions could therefore be made from the data:

- The observed value (28.39) is higher than the critical value (15.51);
- The P-value is smaller than 0.01;
- There is therefore an association between the extent of disclosure of executive remuneration and JSE listed industries in South Africa, based on such disclosures in the 2007 Annual Reports of those companies;
- In terms of Cramer's V the strength of this association is weak; and
- The null proposition that there is no association between the extent of disclosure of executive remuneration and JSE listed industries must therefore be rejected, since there is an indication of such an association in at least the Industrial and Consumer Services industries.

DISTINGUISHING FACTORS

Although it would only be possible to make substantive conclusions regarding the reasons for distinctions between executive remuneration disclosures amongst the three research categories after completion of the qualitative interviews, it was nevertheless possible to make some observations and primary conclusions regarding what distinguished between the disclosures of companies in the three categories.

In respect of companies that disclosed less than what is required in relation to their executive remuneration, it was found that the levels of executive remuneration were often aggregated as opposed to individualised in respect of each executive. Where executive remuneration disclosures were individualised in respect of different executives, there was often no distinction in relation to the different components of their individual remuneration packages. This had the effect that it was not possible to distinguish between, for example, guaranteed salary and performance-based incentives paid to these executives.

In addition, no clear or comprehensive remuneration philosophy followed by these companies had been disclosed, to the extent that it was not possible to evaluate the basis for the levels of remuneration paid to executives in these companies. These companies tended to disclose only details regarding the composition of its Remuneration Committees, the attendance of Remuneration Committee meetings, and a brief mandate of such Remuneration Committee, without necessarily reporting on the substance of the operations of these committees. Details regarding the payment of short term and long term

incentives, as well as income (other than remuneration) paid to executives were lacking. This was especially evident in respect of the disclosures relating to the issue of share options to executives, where only the numbers of options issued in a certain period were disclosed without simultaneous disclosure of other relevant criteria as set out in Table 4 of Annexure M.

It could be concluded from the executive remuneration disclosures of companies which fall into the category of less than required disclosures, that shareholders and stakeholders of those companies would not have sufficient information at their disposal, from the 2007 Annual Reports, to effectively exercise control over executives of those companies, or to evaluate the link between performance and reward of executives in those companies. This lack of information relates to both the forward and backward looking aims of disclosure, as discussed in the literature review above.

In respect of those companies whose executive remuneration disclosures in their 2007 Annual Reports fall into the category of more than required disclosures, the position is significantly different. A common feature of the disclosures of these companies is the appearance thereof in a separate chapter that deals with all required executive remuneration issues comprehensively. Such chapters not only disclose the remuneration philosophy followed by these companies, but also disclose the levels of executive remuneration, the factors taken into account when developing such remuneration packages, the process for determination of executive remuneration packages, and the performance metrics set for payment of both short and long term incentives to executives.

It therefore seems evident that, in these cases, both shareholders and other stakeholders are better informed of not only the levels of executive remuneration paid in these companies, but also the performance measures set for executives to qualify for short and long term bonus payments. In addition, stakeholders are able to readily access sufficient information regarding the process for determination of executive remuneration packages to ensure that the process is fair, transparent and that executives can effectively be held to account for their fiduciary responsibilities to the owners of these companies. The executive remuneration disclosures of the companies in this category enable stakeholders to both monitor executives' annual performance against stated performance criteria (backward looking), and to make informed decisions regarding the manner in which their interests in the company are sustained in the long run (forward looking).

In companies whose executive remuneration disclosures merely complied with the minimum disclosure requirements, different elements of executive remuneration were commonly found in different locations in their Annual Reports. In most cases, details regarding the levels of executive remuneration levels were contained in a note to the financial statements of the company. These notes did not disclose the remuneration philosophy of the company, or any details regarding a link between performance and reward. In those Annual Reports where the last mentioned details are contained, such details appear in different places, and there was no clear trend as to where to find such details in the Annual Report. These details were contained in one or more of either the Directors' Report, Corporate Governance Report, or in the notes to the financial statements. The disclosures made in those sections were however weak, and in

most instances did not provide stakeholders with sufficient information to eliminate risks associated with information asymmetry between executives and stakeholders of the company. Complex disclosures of this nature are at least potentially open to abuse by powerful executives, whose responsibility is to prepare and publish the annual reports of their companies.

It could be noted that most companies that fall into either the categories of less than or equal to the requirements for disclosure of executive remuneration focused almost exclusively on disclosures of the levels of remuneration paid to executives of these companies, rather than also to disclose the criteria which informed such remuneration levels. In comparison, companies that fall into the category of disclosures in excess of what is required, disclosed not only the levels of executive remuneration packages, but also the philosophies that underpin the payment of these levels of remuneration and the performance criteria which have to be achieved by executives to qualify for such payments.

Although it was not entirely possible to accurately predict, after the analysis of the executive remuneration disclosures in the 2007 Annual Reports, the impact of such differences on forward looking and backward looking information symmetry, this could only be explained during the qualitative interviews phase dealt with below.

Another interesting factor that distinguishes between the disclosures of executive remuneration of companies listed on the JSE in South Africa, is the location and ease of access to their Annual Reports. Although most companies' Annual Reports are published on their corporate websites, albeit under different

locations on these websites, some of the companies under the category which relates to less than required disclosures either had no operational corporate website, did not have their Annual Reports published on their websites, or have placed versions of their Annual Reports in locations or formats which present stakeholders with significant difficulties in locating and reading it. If the purpose of the Annual Report is considered to be a mechanism to distribute relevant information on the companies' activities to dispersed shareholders and other stakeholders, then such reports should be readily accessible to all stakeholders.

11.2.3 Conclusions from quantitative analysis

The analysis of the content of the 2007 Annual Reports of South African companies listed on the JSE, as far as it relates to disclosure of executive remuneration, showed significant differences in relation to the location of such disclosures, the content disclosed, and the extent to which shareholders and other stakeholders were able to monitor executives' performance of their fiduciary responsibilities.

Companies which disclosed more than what is required in terms of the South African Companies Act, the King Reports on Corporate Governance and the JSE listing requirements typically disclosed all aspects of executive remuneration in a single and comprehensive chapter in their Annual Reports, which chapter deals exclusively with executive remuneration, whereas companies from the research categories that relate to disclosures which are either less than or the same as the minimum requirements made such disclosures in the notes to their financial statements. Such disclosures not only,

as is the case with most companies which disclose less than or equal to the disclosure requirements, disclosed the levels of executive remuneration paid to executives of the company, but also the factors that inform such levels, and the process for transparent determination of executive remuneration packages in those companies.

In most industries and sectors within those industries, companies tended to make executive remuneration disclosures which are on par with the minimum disclosure requirements for executive remuneration in South Africa. Besides this general trend, more companies across most sectors and industries rather disclosed more instead of less than what is required, but this still represents fewer companies than those that disclose exactly what is required. Companies in the Banking, Media, Household Goods, Oil and Gas, and Mobile Telecommunications sectors tended to disclose more than what is required, whereas companies in the Coal Mining, Travel and Leisure, Oil and Gas, and Development Capital sectors tended to disclose less than what is required.

The results of a chi-square test showed that there is an association between the extent of disclosures of executive remuneration and JSE listed industries, and especially so in the Industrial and Consumer Services industries, in South Africa, based on such disclosures in the 2007 Annual Reports of those companies, but that, in terms of Cramer's V test, the strength of this association is weak.

It was possible to make some observations and primary conclusions regarding what distinguished between the disclosures of companies in the three

categories. In respect of companies that disclosed less than what is required in relation to its executive remuneration, it was found that the levels of executive remuneration were often aggregated as opposed to individualised in respect of the reward components paid to each executive. In addition, no clear or comprehensive remuneration philosophy followed by these companies had been disclosed, to the extent that it was not possible to evaluate the basis for the levels of remuneration paid to executives in these companies. Details regarding the payment of short term and long term incentives, as well as income (other than remuneration) paid to executives were lacking.

It could be concluded from the executive remuneration disclosures of companies which fall into the category of less than required disclosures, that shareholders and stakeholders of those companies would not have sufficient forward looking, or accuracy enhancement, information at their disposal, from the 2007 Annual Reports, to effectively exercise control over executives of those companies, or to evaluate the link between performance and reward of executives in those companies. The disclosures showed a clear bias towards backward looking, or executive monitoring, information sharing, which is an indication of a strong favouring of agency theory in South Africa.

Those companies whose executive remuneration disclosures in their 2007 Annual Reports fell into the category of more than required disclosures, generally made such disclosure in a separate chapter that deals with all required executive remuneration issues comprehensively. Such chapters not only disclosed the remuneration philosophy followed by these companies, but also disclosed the levels of executive remuneration, the factors taken into

account when developing such remuneration packages, the process for determination of executive remuneration packages, and the performance metrics set for payment of both short and long term incentives to executives. In these cases both shareholders and other stakeholders were very well informed of not only the levels of executive remuneration paid in these companies, but also the performance measures set for executives to qualify for short and long term bonus payments. These disclosures therefore satisfy both forward and backward looking aims.

In companies whose executive remuneration disclosures merely comply with the minimum disclosure requirements, different elements of executive remuneration were commonly found in different locations in their Annual Reports. The disclosures made in those sections were however weak, and in most instances did not provide stakeholders with sufficient information to eliminate risks associated with information asymmetry between executives and stakeholders of the company.

It could be noted that most companies that fall into either the categories of less than or equal to the requirements for disclosure of executive remuneration focused almost exclusively on disclosures of the levels of remuneration paid to executives of these companies, rather than also to disclose the criteria which inform such remuneration levels. In comparison, companies that fall into the category of disclosures in excess of what is required, disclosed not only the levels of executive remuneration packages, but also the philosophies that underpin the payment of these levels of remuneration and the performance criteria which have to be achieved by executives to qualify for such payments.

Despite the fact therefore that almost 75% of South African listed companies complied with the executive remuneration disclosure requirements in South Africa, the quantitative analysis has shown that the manner in which they comply differ significantly. In a modern business environment where shareholders' portfolios have been diversified across many different companies and industries, it would be a very strenuous task for such diversified shareholders to analyse and to make cross-comparisons based on these differences in disclosure practices and formats. This at least begs the question whether, as Hill (2006) suggests, shrewd executives who hold positional power to determine, amongst others disclosure practices, do not deliberately create these disparities to protect their own interests above those of shareholders. The question becomes even more relevant where vague disclosures are made in sections in the annual report, such as for example the CEO Report, which is not subject to a shareholder vote on the contents thereof. Only qualitative data could attempt to answer this question.

11.3 Phase 3: Qualitative analysis

At the start of this report, the main problem, which forms the basis for this study, has been stated as the apparent ineffectiveness of corporate governance control measures to keep pace with the development of the modern corporation, which in turn causes symptoms that impact on the core rationale for the modern corporation, such as, amongst others, excessive executive remuneration and defective executive remuneration pay-setting processes.

In the process of considering the main problem, the following questions had to be addressed:

- Is it possible to increase the effectiveness of corporate governance control measures by improving individual sub-systems within the corporate governance framework?
- How do individual sub-systems interrelate in an inclusive corporate governance framework?
- What is the role of disclosure of executive remuneration in an inclusive and effective corporate governance framework?
- How can a better understanding of the strategic role and application of disclosure of executive remuneration improve corporate governance in a corporation?

The main objective of this study was therefore to understand how an effective system of disclosure of executive remuneration, which is both informative (or forward looking) and allows for executive monitoring (or backward looking), fits in an inclusive and effective corporate governance system.

The role of executive remuneration, which has traditionally, in terms of agency theory, been considered to be a mechanism to align the interests of executives (managers) with those of shareholders (owners), and in particular the disclosure thereof to owners and other stakeholders, therefore needed to be analysed. Disclosure of executive remuneration levels as well as disclosure of the process and factors for determination thereof is key in such alignment, in that it both aligns executive actions with stakeholder interests, and provides stakeholders with the necessary information to hold executives accountable for their actions.

The purpose of the qualitative interviews and focus group conducted in this part of the study was therefore to seek a deeper meaning of what caused disclosure of executive remuneration to be an effective corporate governance control measure, and what factors inform such disclosure practices across different industries amongst listed South African companies.

11.3.1 Research process

The data generated and considered for purposes of this research consisted mainly of information obtained from the literature review and from the personal interviews conducted by the researcher with members of the sample of companies listed on the JSE in South Africa. The information obtained from the literature review not only provided a sound basis from where disclosure of executive remuneration, and its role in a corporate governance framework, could be understood before embarking upon the exercise of conducting personal interviews, but also provided a basis for comparison of the information

obtained through the personal interviews and focus group. This enhanced the comparison and analysis of relevant information.

It is also important to comment, at the onset, on the composition and diversity of the sample of companies selected for interview purposes. The composition of the sample for the purpose of qualitative interviews is as set out in Table 12 above. The sample reflects a distribution across all three research categories of 10 percent of the total population in each group, which is deemed to be a representative sample of the population. When the final sample was drawn for the purpose of conducting qualitative interviews, the sample was drawn in such a way as to allow for cross referencing companies in the same sectors and industries across the three research groups.

It was specifically intended to gain a non-generalised or individualised understanding of the meaning companies from different industries and sectors attached to constructs such as disclosure and corporate governance in different contexts. The flexibility offered by qualitative interviews was therefore required to allow for changes in emphasis amongst companies, sectors and industries.

The relevant population for this study constituted all business corporations in South Africa, from where a sampling frame was drawn to include all publicly listed companies on the JSE in South Africa. Representative samples constituting 10 percent of the companies in the sampling frame, and from each of the research categories, were drawn for the purpose of conducting qualitative interviews. In doing so, a stratified random sample was determined in such a way as to be representative of all the different industries and sectors

represented on the JSE index. While the study analysed the disclosure practices of all companies listed under the remaining industries and sectors of the JSE for the purpose of selecting an appropriate research sample for the final phase of the study (in the quantitative analysis phase of the research), the qualitative interviews phase of the research focused on only the main industries of the JSE. These are classified as Raw Materials, Industrial, Financial, Consumer Goods and Consumer Services.

A large volume of data was collected by means of these qualitative interviews, as well as from the analysis of Annual Reports in the second phase of this research, which required extensive analysis by the researcher. This, amongst others, required arranging the data in terms of common themes, trends and groups that makes most sense, and analysing the context of the interview data in a scientific way, and to ultimately allow for addressing the stated research propositions.

The content of the largely “open-ended” data which was collected by means of these interviews were analysed in an attempt to structure it in a meaningful manner. The process of sorting, coding and interpreting the data collected by means of personal interviews initiated with a thorough reading and consideration of all the collected data to identify themes and patterns. The data was then sorted into homogeneous clusters to which certain metaphors could be attributed to describe the different clusters. These clusters were then critically compared and contrasted to find a deeper meaning for the differences in their composition, while at the same time looking for relationships and links amongst the different clusters.

The advantage of using personal and group interviews for data collection was that it allowed the researcher to focus directly on the topic during the interviews, and that it could therefore provide a relevant and in depth focus of all the issues and any causal inferences there might be amongst them.

Mainly explanatory data was collected from each of the companies represented in the three different samples. The interviews were conducted with relevant representatives at senior managerial and board level, while the final focus group was constituted with a cross section of remuneration managers, board level advisers on executive remuneration, and reward consultants appointed to some of the companies selected as part of the final sample. The main purpose of these interviews was to form an understanding of the reasons for the respective disclosure strategies of these representative companies, and the benefits gained from them.

The interview schedule contained in Annexure K was designed after the comparison of Annual Report disclosures with the applicable minimum disclosure requirements, for the purpose of conducting personal, semi-structured interviews with members from the selected sample companies. It was thought to be prudent not to disclose, before or during the interviews, to the sample interviewees how their respective companies were selected to form part of one of the three categories their companies have been classified into, and which category it fell under, in order to eliminate any potential response bias which might be caused by preconceptions regarding each of the categories, or argumentative justifications and knee-jerk reactions. Before this interview schedule was however used in the interviews, it was tested during a piloting

phase to ensure that it was appropriate to elicit responses on each of the research propositions. The necessary modifications were therefore made before the final interviews commenced.

All interviews were conducted with interviewees from businesses in and around Johannesburg and Pretoria in South Africa. This was not only done because of the fact that most of the listed companies in South Africa operate from this area, but also because of limitations in respect of time and costs. A total of 27 interviews were conducted between October 2008 and April 2009 by the researcher personally. The interviewees represented mostly the human resources or remuneration and benefits managers of these companies, who were directly responsible for compiling their executive remuneration disclosures. Three of the interviews were however with executive directors and four with non executive directors serving on remuneration committees of selected companies. This ensured a balanced view from a diverse group of stakeholders in the remuneration management process of companies.

11.3.2 Analysis of qualitative data

In analyzing the data collected by means of the qualitative interviews in a meaningful way it was necessary to consider such data in terms of each of the research propositions stated for this study. The questions developed as part of the interview schedule were specifically aimed at generating responses which would provide deeper meaning in terms of each of these propositions, but also more generally into how different executive remuneration disclosure practices

could contribute to more effective corporate governance frameworks in modern corporations.

The qualitative data is therefore presented with reference to each of the research propositions identified in chapter 9 above.

11.3.2.1 First Proposition

Corporate governance failures result from ineffective internal and external control measures and systems.

In an attempt to test the first proposition above, the following questions were posed to each of the interviewees, without having identified the proposition being tested by these questions before or during the interviews:

- What causes corporate governance failures?
- Which of these causes are related to executive remuneration?
- Why is there a need for regulation of disclosure of executive remuneration?
- What types of disclosure should be regulated and what should not?

The literature review revealed that corporate governance involves the mechanisms by which a business is organised, directed and controlled, as well as the mechanisms by which corporate managers are held accountable for their corporate conduct and performance (Abor and Adjasi, 2007). It already appeared from the McKinsey report (2002) that investors are prepared to pay a premium for companies with good corporate governance practices.

In order to understand corporate governance as a construct holistically, an appropriate balance is required between the alignment of managerial behaviour with shareholder interests, the stewardship and fiduciary role of executives in a corporation, the broader interests of stakeholders of the corporation, and the balance of power of different groups in the organisation.

Corporate governance frameworks

One of the central aspects brought to the fore during the qualitative interviews was that the corporate governance frameworks within which corporations operate are defined by the relationship between the board, executives, shareholders and other stakeholders. In order to be effective therefore, it is trite that corporate governance control measures should effectively:

- Protect shareholders' and executives' interests;
- Mitigate the power that executives enjoy; and
- Provide symmetry of information between executives and shareholders of the corporation.

The separation of ownership from control under the agency theory is still widely regarded in corporate South Africa as driving the need for effective corporate governance control measures. This was evident in all three research categories, but especially so in those companies that disclose either less than or the same as what is required. This view is underscored by the sharp focus placed on such separation by the King I and II Reports. There is a widely held view amongst the majority of South African listed companies that corporate governance control measures are necessary to monitor and regulate the unequal relationship

between shareholders and executives. Agency theory therefore still informs corporate governance in South Africa to a large extent.

Although South Africa enjoys a combination of legislatively proclaimed corporate governance control measures under the Companies Act, 1973, and voluntary corporate governance codes (King I and II), there are still opportunities for abuse of power and open interpretations of those regulatory requirements. The King II Report states in this regard that it is not possible to effectively regulate against bad ethics. Almost all of the interviewees acknowledged the potential abuse of power by executives despite stringent corporate governance measures in South Africa.

Where regulation does not stipulate clearly and unambiguously what has to be disclosed, there is a common view that powerful executives would tend to drive for disclosure which only meets the minimum disclosure standards. This has been confirmed in most of the interviews. One executive from a company in the research category that relates to executive remuneration disclosures that merely comply with minimum requirements, expressed the opinion that governance codes often overemphasize the protection of organisational and shareholder interests over those of executives. He added that this leads to increased risks and deprivation of privacy for executives, who naturally act to counter those personal risks.

In terms of the view that disclosure of executive remuneration is a corporate governance control measure which seeks to protect shareholder interests and guard against self-service by powerful executives, most companies with fuller

disclosure believe that the content of what ought to be disclosed should enable shareholders and other stakeholders to make informed decisions to protect their own interests. They believe that the disclosure should therefore enable more effective activism by both shareholders and stakeholders in the protection of their interests. This accords with the literature review in that disclosure is commonly viewed as a mechanism to cause facilitate action, rather than an outcome in itself (Mongalo, 2007; Ablen, 2003). All interviewees from companies that disclosed more than the minimum requirements, held the view that, in order to be effective, a disclosure framework should therefore not only require comprehensive information relating to the quantum and composition of executive remuneration packages, but also the aims and reasons for the respective package designs, and upfront details in respect of performance targets set for the allocation of such rewards to executives. Only then will shareholders be able to effectively protect their interests both from a backward looking and forward looking perspective.

Only full disclosure of executive remuneration levels, the process for determination thereof, and the principles underlying such process, levels and aims, could achieve shareholder satisfaction in this regard. Most of the companies under the research category that relates to disclosures in excess to what is required, take cognizance of more comprehensive disclosure requirements in other jurisdictions, and especially those in the UK. Directors' remuneration report regulations issued in the UK at the beginning of 2009, under the UK Companies Act of 1985, a copy of which is attached as Annexure T, set much stricter disclosure requirements for UK companies, which not only

require a much more comprehensive disclosure in the UK than before, but also in comparison to South African disclosure requirements.

The UK disclosure requirements are not only far more comprehensive than those applicable to companies listed on the JSE in South Africa, but also more progressive in terms of giving shareholders the same information that executives have access to, to ultimately protect their interests more effectively. The UK regulations also include definitions for the most common remuneration concepts, which enable stakeholders to compare apples with apples when it comes to remuneration disclosures by different companies. In especially one case, the executive remuneration disclosures of one of the companies in the category relating to disclosures in excess of what is required, has to have its draft disclosures vetted by its major shareholder, who is UK based, and has to comply with the stricter UK disclosure requirements. This company's disclosure could however be considered as a benchmark for executive remuneration disclosure which is both informative and allows for executive monitoring.

In particular, the UK disclosure requirements require that a company should publish a remuneration statement, which should include, amongst others:

- a detailed summary of any performance conditions applicable to the allocation of short term or long term incentives to each individual director;
- an explanation as to why any such performance conditions were chosen;

- a summary of the methods to be used in assessing whether any such performance conditions are met and an explanation as to why those methods were chosen;
- a summary of any factors to be used in making any external comparison,
- a description of, and an explanation for, any significant amendment proposed to be made to the terms and conditions of any entitlement of a director to share options or under a long term incentive scheme; and
- if any entitlement of a director to share options, or under a long term incentive scheme, is not subject to performance conditions, an explanation as to why that is the case.

The current disclosure requirements for JSE listed South African companies are fairly comprehensive in terms of the composition and levels of executive remuneration, and almost 75% of listed companies comply therewith. The problem is however that disclosures are presented in such a way that it is difficult for lay persons to understand. It is not enough for companies to disclose only levels of executive remuneration, as most do, but companies should in addition put those disclosures in perspective with reference to both individual and corporate performance. It is also conceivable that governance may be improved where individual and corporate performance are reported in comparison to general market performance over the same period. Disclosing only remuneration levels could lead to negative and unintended consequences, such as undue salary ratcheting, which works against the ultimate aim of an executive remuneration disclosure strategy. There is a clear understanding

amongst companies in the research category dealing with disclosures of more than what is required, that the remuneration content of Annual Reports are often compiled by staff members who do not fully understand the complex field of executive remuneration. The problem is exacerbated where different sections of these reports are prepared by different individuals or departments (often from Finance and Human Resources departments), without necessarily correlating the disclosures with each other. Although no single and coherent reason for the disclosure of executive remuneration in different locations of the Annual Reports could be given during the qualitative interviews, possible explanations for such differentials were:

- a blind following of historical disclosure practices (“the way we have always done it”); and
- the role of different people in preparing different sections of the Annual Report.

In contrast, companies who disclosed more than what was required (typically in a single executive remuneration chapter) could rely on a dedicated and specialised remuneration staff component to prepare its disclosures.

Although none of the interviewees in the category relating to disclosures of less than what is required acknowledged a lack of understanding of intricate executive remuneration practices, there was significant support amongst interviewees in the category that discloses exactly what is required for a naivety regarding the influence of executives in especially the pay setting process.

Common responses across all three research categories as to what ought to be regulated in terms of executive remuneration disclosures therefore included:

- Measures for the establishment of accountability for specified results and outputs;
- Measures to align actions of executives with organisational strategy and the achievement of sustainable shareholder value;
- Measures which would support and facilitate informed decision making;
- The publication of information which would allow shareholders and analysts to understand the nature, expected outcomes, costs, and benefits of executive remuneration policies and principles;
- The link between reward and performance targets and measurement;
- Measures which would limit potential self service by executives; and
- The need for sufficient information to enable informed action by stakeholders.

The current disclosure requirements under the South African Companies Act, the King Codes of Corporate Governance and the JSE Listing Requirements however place a strong emphasis on disclosures in respect of the levels and composition of executive remuneration packages. Although disclosures of this nature are effective in communicating what is being paid to executives, it is less effective in communicating why and what it seeks to achieve. In this regard, companies that disclose more than the minimum requirements believe that the more comprehensive and progressive UK disclosure requirements would succeed better in enabling shareholders and other stakeholders of a company to protect their interests, whereas those in the other two research categories either deliberately choose to merely comply with South African disclosure

requirements, or do not apply their minds fully to the strategic value full disclosure could offer. Typically, companies in the research category relating to disclosures that exceed what is required, also disclose the underlying reasons and metrics for executive remuneration levels and processes. This accords with the view that a principles based disclosure framework, supported by flexible guidelines on appropriate control measures, is a more progressive solution to corporate governance problems in modern corporations.

Unequal positions of shareholders and managers

There was strong agreement across all interviews that the main reason for the failure of corporate governance control measures related to the unequal positions of shareholders and managers in the modern corporation, where shareholders are often dispersed and absent from real control over the corporation. This view holds that Executives are able to seize the power in corporations from boards, and are therefore able to influence the setting of remuneration levels, policies and performance measures and assessments. In this way, powerful executives are able to ignore or circumvent governance policies and procedures to suit their own needs. This strong following of traditional agency theory considers executives to be conflicted in their fiduciary relationships to the owners of the corporation, which creates opportunities for these executives to further their own interests rather than to pursue the interests of shareholders, as owners of the corporation. This not only materialises in boards being captured by executives, but also in non-executive and independent non-executive directors who are not necessarily as independent as may be required. Although none of the executives interviewed conceded this to

be a major problem, it was however considered to be prevalent by an overwhelming majority of the consultants who formed part of the focus group. In such a scenario it must be clear that the internal corporate governance measures set out in Annexure B are ineffective, and that this impacts negatively on the success of an inclusive corporate governance system in a company.

In considering why there is a need for regulation of executive remuneration disclosure, all interviewees agreed that it is important to note the unequal power positions of owners versus managers of the corporation. Shareholders, as owners, need the assurance that executive remuneration levels and package components are sufficiently competitive in the market so that the required executives may be attracted, motivated and retained, but that those executive remuneration levels are not excessive for this purpose. Although the phrase “attract, motivate and retain high calibre executives” has become almost universal parlance in executive remuneration communications, very few of the companies in the “less than” and “same as” categories demonstrated, both in their Annual Report disclosures and interviews how executive remuneration would be positioned as a tool to achieve such an aim. Companies in the “more than” category on the other hand are able to make such a link.

As a result of executive remuneration disclosures in Annual Reports, shareholders can monitor, to a greater or lesser degree of effectiveness, whether the remuneration packages of executive and non-executive directors provide sufficient incentives, and is aligned with the company’s business strategy and objectives. Potential conflicts of interest between executives and shareholders exist where executives are able to award themselves unjustifiably

and in conflict to the best interests of shareholders. This potential abuse is even more acute where share options are awarded on the basis of future growth of the corporation, and where executives are able to manipulate figures to reflect higher than real growth rates for the corporation. Robust governance controls, including the transparency in full disclosures and resultant activism are therefore considered by companies in the “more than” category to deal with potential conflicts of interest effectively.

Shareholders are ordinarily entitled to insist that executive pay is linked to both individual executive and organisational performance. In this regard, theory holds that executives should not be paid large bonuses or exit packages in poorly performing organisations. It is noteworthy in this regard the active role the South African government, as the sole shareholder in the South African Airways (SAA) has chosen to play in investigating the handsome exit package paid to the former CEO of SAA, Khaya Nqula, in 2009 despite the very poor financial performance of the airline and the circumstances of the departure of its former CEO.

In the same vein, the Attorney General of the State of New York, as representative of USA tax payers, has taken issue with the payment of massive bonuses to the top executives in Merrill Lynch immediately before its collapse in 2009. In a letter to the USA House of Representatives dated 10 February 2009, the USA Attorney General questions the curious timing and lack of justification of massive bonus payments to executives immediately before announcing a \$27 billion annual loss, which bonuses were to be funded by taxpayers (Cuomo, 2009).

It has become clear that executives in South African listed companies still have significant power over shareholders, and that they are able to manipulate governance processes to suit their own interests. In companies that disclosed more than what is required, the potential for such abuses of power reduces significantly as a result of the “shrinking effects” caused by greater transparency and measurability of their performance.

Board and Board Committee members

In many instances there were concerns over the lack of knowledge, participation and qualifications of board and board committee members to fully appreciate their duties and responsibilities in such capacities, or to take these responsibilities seriously enough to make the effort to fully understand the company policies, processes and procedures. This again relates to ineffective internal corporate governance control measures. There is a strong view that many non-executive directors and independent non-executive directors in South African listed companies lack the knowledge or independence to execute their responsibilities towards the shareholders of the corporation effectively, and simply do things “the way it has always been done before”. This phenomenon was especially prevalent amongst companies in the “less than” and “same as” categories. This shortcoming is exacerbated when board members do not at least match the levels of assertiveness shown by executives in making important decisions. In most cases in the “same as” category this leads to a culture of mere “tick-box” compliance at board and board committee level, where these board members are unduly influenced by executives and their representatives, and do not make the effort to critically evaluate the need to

challenge executives and their proposals. In this regard, one of the key principles upon which the King II Report was based, is the “comply or explain” principle, in terms of which corporations have to either comply with the principles outlined in the report, or explain its failure to do so. The majority of South African listed companies still follow this principle in their executive remuneration disclosures. This could be attributed directly to the strong emphasis placed on this principle in the King II Report.

Poor structuring of board committees, or the poor functioning of such committees, has been raised as a serious concern in the effective governance of companies. This is not only related to a lack of structure, role clarity and decision frameworks in these committees, but often to a lack of control, discipline, ethics, and independence by the directors serving on these committees. In especially smaller companies in the “less than” category, the skills and experience of board members relate more to technical skills in the area of the company’s operations, rather than an appropriate mix of skills at board level.

The levels of knowledge by members of remuneration committees and boards of executive remuneration practice and the factors that impact thereon is of critical concern to most South African companies. This is compounded where board members are not totally committed to exercising due diligence in the discharge of their duties to the board and shareholders of the organisation. The result of this is that executive remuneration issues do not receive the proper attention at board and remuneration committee level that is required, and often results in unintended consequences in reward levels. It is common practice in

an overwhelming majority of companies in all three research categories for executive remuneration proposals to be prepared by executives or staff members, who report directly to executives, for presentation to the particular board committees, who are not proactive enough to ask assertively for specific presentations to address the needs of the stakeholders these board members represent. This presents massive opportunities for powerful executives to advance their own interests above those of other stakeholders.

In these circumstances it is therefore not impossible for executives to manipulate their powerful positions to advance their own interests, by, amongst others, presenting data favourably in terms of the content or timing thereof, or securing less than independent appointments to the board or committee. Executives are often also able to manipulate the process of appointment of remuneration consultants to the remuneration committees of companies. In this regard, consultants who are favourably linked to executives by means of informal networks or other more formal assignments for the company, are suggested to the board for appointment. In many instances, consultants who are appointed are neither independent nor qualified to advise the board on executive remuneration issues. In some cases these consultants are perceived to be mouthpieces of the executives, by “just saying what executives want to hear” in order to retain their consultancy appointments. Companies often make use of the same consultancies for multiple tasks, such as, for example remuneration surveys and consultancy advice, which has at least the potential risk that these consultants would give popular advice for as long as they are able to secure further assignments from the company, instead of giving objective, independent, and correct advice. It is noteworthy that, although the

companies in the “more than” category also make use of remuneration surveys provided by South African survey houses, most make use of either different consultants than those from the survey houses, to analyse the survey results and advise the Board thereon, or make use of more than one survey for benchmarking purposes.

The process of setting realistic and measurable performance objectives for executives is particularly open to widespread manipulation by executives. It is common practice to award substantial short and long term incentives to executives on the basis of achievement of pre-determined short term performance objectives. It is however not uncommon for executives to play a leading role in setting those performance targets, and it is often done in such a way as to:

- Enable comfortable achievement thereof without stretching executive effort;
- Disregard market movement effects on the achievement thereof;
- Focusing executive performance only on the achievement of especially short term financial targets rather than on increasing shareholder value over the long term, which creates opportunities for timing abuses by executives;
- Ignore measures of performance relative to industry peers; and
- Protect executives against downside risk.

Remuneration committees have therefore not been very successful in curbing abuse of power by executives.

Lack of capacity

One of the key deficiencies in most corporations in the “less than” and “same as” categories is the absence of a dedicated resource to deal with corporate governance and executive remuneration issues of the company. In most of the companies that disclosed more than what is required, dedicated and strong remuneration specialists provide the board and board committees with high quality executive remuneration proposals. The same assistance was glaringly lacking in almost all companies in the category that relates to disclosures which are less than what is required, and to some extent in companies that disclosed exactly what is required.

One interviewee from the research category relating to executive remuneration disclosures that are less than what is required remarked that *“smaller organisations often feel that they simply don’t have the resources (costs and manpower) to adhere to the practices of good corporate governance”*. She added that *“we do not have a dedicated internal resource to formulate executive remuneration disclosures, and to manage executive remuneration plans, and external advisory services are too costly”*.

In contrast, all of the interviewees from the research category relating to disclosures in excess of what is required, indicated a strong reliance on trained and dedicated remuneration specialists, who ordinarily form part of the Human Resources departments of their companies, and whose role it is to lead Remuneration Committees on all aspects of executive remuneration. These reward specialists understand the underlying reasons for their reward practices,

and are able to link those to performance and rewards. It therefore facilitates a principled approach to remuneration management, and an improved ability to develop tailored control measures to achieve the desired governance state.

Quality of management data

The quality of management data, or lack thereof, have a direct relationship to the success or failure of corporate governance control measures. It is not uncommon for boards and board committees in South Africa to rely on management proposals placed before it by executives and consultants, without necessarily verifying the accuracy thereof. In particular, in companies that disclose less than the minimum requirements, where Remuneration Committee members do not always have the necessary skills or experience to interrogate complex executive remuneration proposals, this problem is exacerbated. This allows self serving executives to manipulate data placed before such boards and committees to serve their own interests above those of the owners of the corporation.

In addition, the quality of consultancy advice to boards and remuneration committees can often be questioned. Besides the inexperience of some consultants and board level advisors, consultants are often not independent enough to advise remuneration committees objectively. It was noteworthy that the consultants used by companies that disclose more than what is required are acknowledged as authoritative and respected in their field, whereas most of the companies in the other two research categories either do not make use of consultants, or base their consultancy appointments on costs factors, which do

not necessary yield the best consultancy services. If a consultant renders or wishes to render additional services to the company, there is always the possibility that such consultant would rather give popular advice which would improve the chance of securing further appointments with the same company. In such a case the value of consultancy advice is highly questionable, and could not lead to informed management decisions.

Conclusion

Although most of the above causes of corporate governance failures could be related to executive remuneration issues, the following aspects thereof were highlighted as the main considerations in this regard:

- Differences in disclosure requirements in governance frameworks;
- Passivity of boards and board members;
- Boards that are captured by self-serving executives;
- Lack of independence of board members and advisors;
- Absence of a clear link between performance and reward; and
- Lack of remuneration committees exercising objective and independent control over the executive pay setting process.

The most common reasons, in order of prevalence, for corporate governance failures advanced by interviewees per research category were as set out in Table 21 below. These present substantiating examples of the broad statements made above.

Table 21 What causes corporate governance failures

Research category	Causes of failures
Disclosures less than what is required	Lack of transparency and trust
	Contradicting practices due to poor KSF's
Disclosures same as what is required	Lack of self-discipline
	Lack of communication
	Independence of Board, Board Committees and advisors
	No or weak link between pay and performance
	Ineffective monitoring structures and processes
	Entrenched executives
	Panic decisions
Disclosures more than what is required	Poor ethics and values
	Excessive concentration of power
	Conflicts of interest (and differing levels of assertiveness)
	Poorly functioning Boards and Board Committees
	Unqualified and inexperienced Board members
	Lack of transparency
	Focus on short term gains instead of long term sustainability
	Weak strategy, targets and measures
	Bad management choices

The ineffectiveness of disclosure of executive remuneration as a corporate governance control measure is therefore not only related to the compliance with or failure to comply with minimum disclosure requirements, but also to the appropriateness of disclosure requirements to achieve its aim of protecting shareholder interests and guarding against self service by powerful executives. The transparency and shrinking effects offered by fuller executive remuneration disclosure seem to contribute to greater levels of alignment and corporate control in companies that disclose more than the minimum requirements.

Both the levels of executive remuneration and the process for determination thereof are symptomatic of the failure of corporate governance control measures.

The following questions from the interview schedule were intended to gather responses which could test the second proposition above:

- If corporate governance control measures are ineffective, what would be the effect, if any, on:
 - levels of executive remuneration?
 - the process for determination of executive remuneration?
- How effective is disclosure in facilitating information symmetry between managers, investors and other stakeholders? What factors determine their effectiveness?

Conflicting interests

If corporate governance control measures are ineffective in regulating how executive remuneration is set, and what the link between performance and reward is, powerful executives may have an opportunity to abuse their powers for own interest by securing remuneration which is not in line with either their individual or with corporate performance. The public perception is commonly that business executives are overpaid, and that corporations fail as a result of executive greed. This places a greater burden on companies to ensure that their disclosures make a strong case for the fact that executives in the particular

company are not in fact overpaid in relation to individual and corporate performance.

A very heated topic in this regard is the widening wage gap between executives and ordinary workers, which debate is not unique to South Africa, as appears from the literature review. Two opposing schools of thought exist in South Africa, namely:

- Those who believe that the wage gap is unjustifiably wide; and
- Those who believe that the wide wage gap is justifiable in relation to the relative contributions to the company's performance.

In practice however, it is not always possible to make such full disclosures where boards have been captured by powerful executives. There is a general view that the executive pay-setting process under a board which has been captured by executives is not always geared towards maximisation of shareholder value, and to the reduction of agency costs.

The managerial power approach is still fairly common amongst South African companies, in that executives enjoy significant power in the pay-setting process, and that board processes are not conducted at arms' length. Managers commonly have the power and the opportunity to disguise excessive salaries in their reports to the board. Conflicts of interest potentially exist between:

- Shareholders and managers;
- Short and long term interests of different stakeholders;
- Costs and benefits of particular disclosure strategies; and

- Sensitivity of information and the need for information symmetry.

It is not always clear whose interests companies should pursue. In a corporation characterised by many dispersed shareholders, it is often the case that those shareholders have conflicting interests. Some investors have short term profit maximisation interests, while others prefer long term sustainability of the company. Shareholders' interests also often conflict with the interests of a broader group of stakeholders of the organisation, of which the employees constitute a critically important stakeholder group. It is important to clarify this issue upfront as part of the remuneration philosophy of the company, and to publish such philosophy prominently to all stakeholders.

A fairly general concern was raised that a full disclosure of a company's executive remuneration details may disclose valuable competitive information to competitors. The literature review disclosed that this is a global concern, and not unique to South Africa. This view holds that, although the remuneration disclosure statement should be both backward- and forward-looking, the company should not be obliged to disclose information of a commercially-sensitive nature which could be detrimental to the company's strategic position. It is therefore considered imperative that companies should evaluate the risks of their disclosures upfront, and has been advanced as a strong rationale for following a disclosure strategy based on mere compliance with minimum requirements. The literature review also concluded that a fine balance between intended and unintended consequences is required (Ablen, 2003).

Ultimately, companies have to therefore carefully balance the benefits of full disclosure with the social and financial costs thereof, before deciding on an appropriate disclosure strategy and level. This is particularly important in view of the sensitivities executives might have regarding having their remuneration packages published publicly, and the general distrust that exists around high executive pay packages in times of poor performance. The aim should be to keep executive remuneration disclosures simple enough for lay persons to understand. It is too often the case that executives design and publish overly complex remuneration schemes, which are often no more than a convenient way of hiding excessive pay in relation to performance. A view similar to that of Slane (1997) was expressed that executives may also follow such an approach to protect their persons and privacy from unwanted attention.

Salary levels

There is a view that when mechanisms to disclose executive remuneration were introduced in South Africa for the first time, it immediately caused substantial ratcheting of executive salary levels. This ultimately had a negative impact on salary negotiations, where executives of one company would merely compare their salary levels to executives of another company, without also considering any differences in performance and results. The good intentions of a disclosure regime in South Africa therefore had immediate negative consequences. The global need for greater levels of transparency in the executive remuneration systems of corporations has now placed a bigger responsibility on boards to be cautious in setting executive remuneration at justifiable levels, and in terms of a due process.

“Improved disclosure of executive compensation is needed in order to eliminate the surprise of hidden payments owed to senior management...”

Christopher Cox, SEC Chairman

The interviews exposed that the failure of corporate governance control measures potentially has the following specific impact on different executive remuneration components:

- Salary: Manipulated survey data; appointment of agreeable consultants;
- Bonuses: Manipulated performance targets, measures and assessments; and
- Incentives: Timing of results; influence over share price by selective disclosure of results.

The manner in which companies from the three research categories complete benchmarking to determine justifiable levels of executive remuneration differ substantially. Almost none of the companies in the category that disclosed less than what is required made use of reputable market surveys to establish common grading rates for remuneration. Although most of the companies in the category that disclosed exactly what is required made use of surveys, these companies often only subscribed to a single survey. This is problematic if the survey participants are not from comparable industries or sectors, and in view of the often vast differences between two similar surveys, as a result of differences in the participant population. The companies in the category that relates to disclosures in excess of what is required all subscribed to multiple local and

international surveys from reputable survey houses. They advised that they did so in order to make realistic comparisons to positions in similar industries, sectors, and company parameters.

Salary determination process

Most interviewees agreed that the process for determination of executive remuneration packages and performance measurement criteria will become highly subjective in the absence of effective corporate governance control measures. Decisions will be based on inaccurate or incomplete data and research, and will consequently not be objectively justifiable. This could result in executive remuneration levels which are either too high or too low in comparison to market rates, and would in all likelihood not be linked to organisational performance. A more robust process to determine executive remuneration is required. There seemed to be significant differences between companies that disclose more than what is required and the other two research categories, in that the “more than” category companies have both the capacity, and actually consider how their executive remuneration practices could lead to more effective control measures.

In the absence of effective corporate governance control measures, companies easily fail to take into account how general market movements impact on performance. Poor performance is consequently often rewarded in periods of general market growth, while excellent performance may not be rewarded in poor market conditions. These unintended consequences could be avoided by the design and implementation of a robust system of effective balance checks

before deciding on the payment of executive remuneration packages and bonuses. Companies with dedicated capacity to do this found themselves in the research category relating to disclosures in excess of the minimum requirements. The link between performance and reward was therefore at least potentially weak in circumstances where such a system and capacity is absent. A more appropriate mechanism would be to award relative-pay-for-relative-performance, which is prevalent in four out of six of the companies in the “more than” category. This implies that individual performance is not only measured against the achievement of personal and corporate performance targets, but also against the performance of peers. This would also eliminate a performance measurement focus which only considers narrow financial measures for convenience sake.

The lack of understanding of the dynamics involved in the setting of executive remuneration policies and levels, in companies in the “less than” category result in incomplete, incomprehensible, misleading or poorly presented executive remuneration disclosures. This is problematic, as full disclosure and transparency allows shareholders to examine relevant facts before making informed decisions. It also allows shareholders to make comparisons and benchmarking decisions for executive remuneration, which are based on inputs from sources which are broader than just the company’s internal mechanisms.

Conclusion

It is clear that ineffective disclosure of executive remuneration, as a corporate governance control measure, could result in many different corporate problems,

which are symptomatic of the failure of disclosure of executive remuneration to achieve its optimal contribution towards effective corporate governance in a company. The two most prevalent such symptoms are:

- Unjustifiable executive remuneration levels; and
- Pay setting processes that are unduly influenced by executives.

The most common impacts of ineffective corporate governance control measures on executive remuneration levels and the executive pay setting process, as identified during the interviews were as set out in Table 22 below. It is interesting to note the degree of correlation amongst the three research categories of the impact of corporate governance failures on executive remuneration.

It could be concluded that, despite a large degree of comparison in relation to the dangers of corporate governance failures, companies follow very different strategies, if at all, to guard against and mitigate these risks. Some of these differences could be related directly to the level of specialisation of a dedicated remuneration capacity to not only design and monitor executive remuneration practices, but also to advise appropriately on disclosure practices. It is one thing to understand the risks, but completely another to have the understanding of what is required to deal with the risks appropriately. A dedicated and specialist corporate governance and executive remuneration staff capacity was mentioned to be a key process in the interviews.

Table 22: Impact of ineffective corporate governance on executive remuneration

Research category	Impact on levels of pay	Impact on pay setting process
Disclosure less than what is required	Unfair increases	Subjective process
	Irrelevant factors used as basis for increases	Process driven by self-service
Disclosure same as what is required	Over- or underpaid executives	Abuse of process
	Pay ratcheting	Self-interest drives process
	No/weak link between pay and performance	Failure to apply mind
		Selective use of surveys
Disclosure more than what is required	Pay for underperformance	Absence of link between pay and performance
	Pay ratcheting	Manipulation of corporate structure to avoid disclosure

11.3.2.3 Third Proposition

Effective disclosure of executive remuneration determination processes and levels, as a corporate governance control measure, contributes to a more effective overall corporate governance system in organisations (i.e. there is a positive correlation between disclosure and good corporate governance).

The following questions from the interview schedule were posed to interviewees to test the third proposition above:

- What factors affect management's disclosure choices?
- Could disclosure of executive remuneration contribute to more effective corporate governance? How?

The literature review revealed that the reasons for disclosure of executive remuneration could either be forward looking in terms of the accuracy enhancement model, or backward looking in terms of the agency cost model (Mahoney, 1995). The accuracy enhancement model postulates that shareholders and other stakeholders in a corporation require access to relevant information in order for them to make informed decisions. The agency cost model on the other hand postulates that information is required to limit agency costs caused by the separation of ownership from control of the corporation, by effectively monitoring the alignment of executive behaviour with shareholder interests.

Disclosure choices

Forward versus backward looking aims of disclosure

The data obtained from the qualitative interviews has shown that there is still a strong following of the traditional agency cost model amongst an overwhelming majority of South African listed companies. Disclosure is strongly viewed as a mechanism to ensure that executives perform their fiduciary duties in companies to the creation of sustainable long term value for the shareholders of the corporation.

One interviewee remarked that “*companies need to determine what is important for its shareholders, and use this to guide its disclosure practices*”. Some of the reasons advanced for this phenomenon is that backward looking disclosures are generally cheaper, less complex to perform, and more consistent in its application over a number of years. It however appeared from the interviews that the most prevalent reason for this preference is an interpretation that the South African disclosure requirements essentially require only information which would satisfy executive monitoring (i.e. backward looking). Forward looking disclosures under the accuracy enhancement model is generally viewed as complex, expensive, and volatile.

A fair number of the companies in the research category that relates to disclosures in excess of what is required and who deliberately also consider the UK disclosure requirements as part of their disclosure strategy, however follow a combination of both forward and backward looking disclosures, although there is still a predominant focus on backward looking disclosures. Most of these cite the more detailed disclosure requirements in jurisdictions such as the UK, where these companies have operations or business interests, as a major factor in their choices of disclosure practices.

Positive versus negative consequences

There are both positive and negative consequences in following a hybrid disclosure strategy. The positive consequences, or arguments in favour of a combined disclosure strategy, have been identified as, amongst others:

- Forward looking and backward looking information are equally important to stakeholders to make informed decisions;
- It controls potential self-dealing by executives by reducing opportunities to conceal their abuses;
- It promotes accountability for corporate performance, in that executives know in advance what their performance will be measured on;
- It is less interventionary than direct legislative intervention (such as the recent legislative upper limits placed on executive remuneration packages in the USA at the beginning of 2009); and
- Access to relevant information creates investor confidence.

The possible negative consequences of, or arguments against, a combined disclosure strategy have been identified as, amongst others:

- It creates additional costs;
- It may lead to ratcheting of salaries without direct relevance to better performance;
- Invasion of privacy of executives;
- Attraction of unwanted and criminal attention to executives; and
- Disclosure of sensitive and competitive information to competitors.

There therefore seems to be a strong appreciation for the fact that disclosure of executive remuneration causes intended and unintended consequences, which requires a fine balance in accordance with the unique circumstances and needs of the company (Ferrarini and Moloney, 2005).

Business philosophy and culture

The business philosophy and culture of the organisation impact heavily on the disclosure strategy employed by the company. Local laws, customs, culture, and historical practices will also play a major role in determining what and how a company will make its executive remuneration disclosures (Ferrarini, *et al.*, 2003).

One interviewee in the research category relating to disclosures in excess of minimum requirements stated that *“a corporate governance framework, which includes disclosure, should be tailored according to the size, nature and objectives of the specific business”*.

Most companies have indicated that they tend to follow what was disclosed by them in the previous year, and that special consideration is only given to major changes that may have occurred in their business practices. In addition, it was suggested that it was too much effort to change the way things were historically done without being forced to do so. This was described as *“old habits that die hard”*, that cause people to do things the way they always used to do it, without thinking about whether such method is still suitable. This accords with the perception that board and board committee members are often too passive, inexperienced, or disengaged to think strategically about these issues. Knowledgeable and experienced board and board committee members, together with a robust training schedule for such members, often enhances more effective corporate governance, as is the case in some of the companies in the “more than” research category.

It appeared from both the analysis of the 2007 Annual Reports of South African companies listed on the JSE, as well as the qualitative interviews, that their remuneration philosophies are almost exclusively stated as being aimed at the attraction, motivation and retention of high calibre executives primarily, but also secondarily to align executive actions to shareholder interests. The distinction between companies in the three research categories lies in the extent to which their statements explain how this will be done. In the category that discloses less than what is required, companies commonly have not applied their minds to this issue, or failed to explain how this will be achieved, whereas companies in the “more than” category have gone to great lengths to explain how and why this will be done.

Regulatory environment

Most companies follow either a legislatively mandated disclosure strategy similar to what is to be found under the Sarbanes Oxley Act in the USA, or a voluntary disclosure strategy informed by a regulatory code or listing requirements of the stock exchange where it is listed, which is more akin to the UK disclosure system. In South Africa there is a strong trend to follow the UK route of voluntary disclosures. This could be ascribed to the major role the King II Code and JSE listing requirements have historically played to establish a culture of voluntary disclosures under a “comply or explain” framework. Most of the companies which fall under the research category that relates to executive remuneration disclosures in excess of what is required, considered the disclosure rules in other jurisdictions than South Africa, which are more detailed and strict. There are essentially two reasons for this:

- Those companies also operate in these jurisdictions where stricter disclosure requirements are made; or
- Those companies are directly linked to either a holding company or subsidiary that operates in a jurisdiction where stricter disclosure requirements are made, and some form of consistency is required in its disclosure practices.

There is a commonality towards compliance with stated disclosure requirements as a result of the explicit focus of King II on the “comply or explain” principle. The interviews confirmed that, across all three research categories, the primary focus of their disclosure practices was to ensure that the company at least complied with minimum standards. Some companies considered this to be enough, while others considered the potential strategic value in increased disclosure.

Sensitivity of information

Boards generally require of the management of a company to ensure that proper executive remuneration structures and benchmarking protocols exist, to form a basis for disclosure. These mechanisms however require a measure of flexibility within a framework that sets out the minimum fixed requirements. As increased disclosure could form a launch pad for increased shareholder and stakeholder activism, as well as labour instability if executive pay increases are higher than that of ordinary staff, there is a strong effort to find a fair balance between what is disclosed and what not. In the same way most companies deemed it necessary to find an equitable balance between the commercial

sensitivity of business related information and the privacy and security of executives. It was remarked that *"executives have as much right to be protected against undue risks as the company is protected"*.

Disclosures which may amount to revenue forecasts are considered to be especially risky. Many companies have made firm decisions not to disclose incentive targets and payouts due to its sensitive nature for both business growth and the retention of key executives. As this information is not required as part of the minimum disclosure requirements, companies will still comply with disclosure requirements despite their failure to also disclose this. Companies in the "more than" category believe that, despite this information not being disclosed publicly, it should nevertheless be disclosed at least to each and every shareholder of the company.

Industry and sector trends

A striking difference in approach was found between the disclosure trends in the banking and mining sectors in South Africa. In the banking sector, industry and sector trends in executive remuneration are considered carefully before a company in this sector decides on its own disclosure strategy. This has had the effect that South African banks' disclosures are generally in excess of what is required. In the mining sector however, it appears that no conscious decisions are made as to the levels of executive remuneration disclosure. A strong minimum compliance mindset is present in mining companies, which is consistent with the analysis done in respect of sectoral disclosure practices in

section 11.2.2 above. There is a similar trend to that of the mining industry, albeit to a lesser extent, in the South African construction industry.

The role of consultants and remuneration specialists

The role of executive remuneration consultants, remuneration and benefits specialists, and board advisors, in the preparation of executive remuneration disclosure statements must not be underestimated. A clear trend emerged from consultations that executive remuneration disclosures tended to be in the category that relates to more than what is required when experienced and well respected consultants and remuneration practitioners were used in the process of preparing disclosure statements. Some of the factors that determine the level of the consultant or practitioner involved in this process are:

- A thorough knowledge of all aspects of executive remuneration;
- A good background knowledge of the company concerned, as well as the industry and sector within which it operates (including disclosure trends and practices); and
- An absence of conflicting or additional appointments with the same company which might impact on the impartiality of advice given.

Companies in the category relating to disclosures of less than what is required, and to a lesser extent companies that disclose exactly what is required, tend to consider the use of remuneration consultants too costly, and therefore mainly rely on internal capacity, which in most cases was outside of a purely remuneration skills set, to prepare executive remuneration packages and

disclosure tables. This explains their disclosure of remuneration levels and tables alone, which information is readily available and not too complex to copy from pay sheets.

Conclusion

Ultimately, it has been suggested that companies should consider, before deciding on a particular executive remuneration disclosure strategy, whether the intended disclosure would enhance executive remuneration and corporate governance issues in the corporation, or whether it would aggravate aspects thereof. In addition hereto, the increased costs of additional disclosures should be considered against the risks of agency costs occurring, as well as the benefits it may hold for the organisation. Developing appropriate control measures therefore involve finding an appropriate balance for the individual organisation.

Disclosed content

Most companies in the categories that relate to disclosures which are either less than or the same as what is required only disclosed details pertaining to the membership of their respective remuneration committees, as well as broadly what the duties and meeting schedule of the committee were. A separate section in the Annual Reports of these same companies, which was not always properly cross-referenced, disclosed levels of executive remuneration for the directors of those companies. Those companies that fall into the research category that relates to disclosures in excess of what is required provided much

more detailed information in this regard, in a single executive remuneration chapter in their Annual Reports.

This glaring difference was explained during the interviews with reference to the staff responsible for compiling the disclosure statements for the Annual Reports. In companies where there is not a dedicated remuneration specialist capacity (all “less than” and some “same as” companies) different but related sections are often compiled by different staff members without necessary reconciliation. In particular, it was suggested that governance aspects relating to the Remuneration Committee is commonly prepared by or on behalf of the Company Secretary, while the remuneration tables for the notes to the financial statements are prepared by Human Resources officers (for remuneration and fees) and Finance officers (for shares and share options). In those companies that disclose more than what is required, and that have dedicated remuneration specialist capacity, executive remuneration disclosures were prepared comprehensively by such staff, and in most cases, as a result thereof, published in a single location chapter of the Annual Report. In some cases however, despite the simplicity and convenience of a single chapter executive remuneration disclosure, the contents contained in such chapter was as confusing as a disclosure across multiple locations in an Annual Report.

Most companies stated in their Annual Reports that directors have full access to any information held by the company. This also applies to non-executive and independent non-executive directors. This however implies that such directors receive what they ask for. The aim of full disclosure however is to provide such information to which executives of the corporation have access, and that the

shareholders do not necessarily know of. The aim is true information symmetry. There is a popular perception that executives would prefer to disclose as little as possible to maintain their own privacy and security. Fuller disclosure consequently implies that executives who support such a strategy put the company's interests above their own.

One of the popular mechanisms to reduce the exposure of executives to public scrutiny of their remuneration arrangements is for companies to only have a Chief Executive Officer and Chief Financial Officer as executives. The remaining members who would ordinarily have executive powers retain those powers, but are not regarded as executives. Their remuneration arrangements therefore do not have to be disclosed in terms of the disclosure requirements in South Africa at the time. In jurisdictions such as the USA this problem is eliminated in that companies are required to not only disclose executive remuneration, but also the remuneration of members of the top three layers of the organisational structure. The King III Code imposed a similar requirement in South Africa from March 2010. There was already such a trend in companies that disclosed more than what is required in their 2007 Annual Reports, for its Remuneration Committees to also consider the remuneration arrangements of senior officials who are not executive directors of a company but who nevertheless have a significant influence over the company's ability to achieve its strategic objectives, and to report thereon to the Board.

Table 23 below indicates some of the most common characteristics of the executive remuneration disclosures that distinguished companies in each of the three research categories from each other.

Table 23: Disclosure characteristics across research categories

Category	Characteristics
Less than required	<ul style="list-style-type: none"> • Remuneration tables in the notes to financial statements generally comply with minimum disclosure requirements, but in some instances the figures are aggregated instead of individualised or broken down into components. • Disclosure items are contained in short, separate paragraphs in either the Directors' Report, Corporate Governance Report, or Sustainability Report. These paragraphs generally set out the mandate, duties, and membership of the remuneration committee, but do not disclose the remuneration policy, performance measures, or what the remuneration was paid for. • Most companies only disclose levels of executive remuneration, but not the process, or performance metrics for the determination thereof. • Benchmarking is done against salary levels of companies in the same or similar SA industries, but not against the relative performance of the company to others. • Disclosure is almost exclusively backward looking (monitoring).
Same as required	<ul style="list-style-type: none"> • Generally, the remuneration philosophy is set out in broad terms, but in different sections of the Annual Report. The aim of executive remuneration is identified as being to attract, motivate and retain high calibre executives primarily, but also to the alignment of executive and shareholder interests, fair reward for contributions to growth and value creation, and benchmarking practices. • Very often these companies include a statement that their disclosures comply with the disclosure requirements in the Companies Act, King II, and the JSE listing requirements, but does not state how it complies. • Remuneration levels are disclosed almost exclusively in tables in the notes to the financial statements. These disclose levels only, and merely comply with the requirements, without giving explanations of how the levels were determined. • In a few cases the disclosures of these companies refer to the use of consultants, but only to the extent that they provide market survey data on market rates. They are not advisors on executive remuneration practice. • Performance metrics are not identified in detail. In some cases there is a statement that both financial and non-financial performance metrics have been used for STI's and LTI's, but no details are given
More than required	<ul style="list-style-type: none"> • Most companies disclose all relevant executive remuneration information in a single and comprehensive chapter (10-14 pages). The chapter typically includes details of remuneration philosophy and its aim, basis for determination of each reward component and its aim, eligibility criteria, detailed performance targets and measurement scales, and the use of consultants for more than just survey data. • Some reports state a commitment to make full disclosures to shareholders regardless of how difficult it might be in periods of poor performance. • The principles that underlie the award of Pay (competitiveness), STI's (reward performance), and LTI's (retention) are distinguished. • Deal with both forward looking and backward looking aspects of disclosure. • Considers listing requirements in other jurisdictions where these companies operate, as well as disclosure practices of holding or subsidiary companies. • Comprehensive details regarding duties of remuneration committee and other board and board committee members, which enables lay assessments. • Companies that comply with UK listing requirements include graphs and diagrams to distinguish between salary components and individual directors. • Indicate company's share price performance relative to the general market, which enables stakeholders to see whether bonuses were paid to executives when the company did not perform well.

Contribution to more effective corporate governance

It is already common cause across the world that effective disclosure of executive remuneration could contribute to more effective corporate governance control measures and corporate governance systems. It seems therefore that disclosure, transparency and corporate governance are concepts which are intrinsically linked to each other. In order to be effective though, an optimal mix of internal and external corporate governance control measures must be found. This not only includes external compliance with regulatory codes, legislation, and disclosure requirements, but also the internal composition and operation of boards and board committees. The interrelatedness of all of the components of an inclusive corporate governance framework as proposed in Annexure B is therefore of critical importance.

Access to information

Competent non-executive directors and independent non-executive directors who have the necessary knowledge, skills, and insight, and who participate actively in the governance of the company, can only do so if they have access to the same information as executives have, and at more or less the same time. Proper and informed business decisions cannot be made without proper information. Stakeholders require that relevant information should therefore be available to them in a timely, cost-effective way, and should, in addition to being published in the company's Annual Report, also be available on their corporate website, the stock exchange where the company is listed, and through direct enquiries to the company itself. This however carries a cost which is considered

too burdensome for smaller companies, that consequently disclose less than what is required.

The OECD Principles suggest that the internet and other information technology tools provide scope for improving information dissemination amongst stakeholders. In countries such as the USA, internet disclosures are already accepted as a legal mode of disclosure, and annual reports are required to state clearly where company information may be found on the internet. The King II Report also emphasizes the need for critical financial information to be made available to shareholders simultaneously, and supports the idea that traditional modes of communication be complemented by such new tools as the internet. Although most South African companies now publish their Annual Reports on their corporate websites, there are nevertheless some that either do not, or who succeed in hiding their reports so that it is difficult to locate them.

The question may be asked why executive remuneration disclosures are commonly fragmented into different parts of the Annual Reports. In doing so, the already complex disclosures are complicated even further to the extent that the average stakeholder would not form a clear and balanced forward- or backward looking view of the remuneration paid to executives in the corporation. One possible reason, which has been confirmed in two interviews with remuneration consultants as well as in the focus group is, such as Hill (2006) suggested, that executives may sometimes deliberately choose to make complex disclosures in order to hide their self-serving practices. In order for information symmetry to be achieved in this regard, it is necessary to group related information together meaningfully in a single location in the annual

report, and to consistently disclose such information in this manner to all stakeholders simultaneously. Some of the reasons advanced for the placement of different aspects of executive remuneration in fragmented paragraphs across Annual Reports are:

- Different staff members of the corporation draft different aspects to be included in the Annual Report, and there is a lack of consolidation of those aspects into meaningful groups;
- Companies fail to consider their disclosures holistically;
- Administrative staff, who do not necessarily understand the connections between different portions of the information, are responsible for compiling the Annual Reports; and
- Remuneration committees take a passive approach towards fulfilling their duties.

The location of corporate governance and executive remuneration disclosures in the Annual Report of a company is not generally prescribed. In practice these disclosures appeared in many different locations in companies' Annual Reports, as appears from Figures 12 and 13 above. Some measure of standardization of the location of corporate governance and executive remuneration disclosures is required to make the disclosed data more accessible and more meaningful. This approach was followed by all of the companies which have been placed in the research category which relates to disclosures in excess of what is required. This approach is also followed in terms of relevant disclosure guidance codes in Hong Kong, India and Switzerland, which not only provide for corporate

governance disclosures to appear in a separate section of the Annual Report, but also in a prescribed format.

Where it is not possible or feasible for corporate governance disclosures to be consolidated into a single chapter of the Annual Report, there should at least be clear and sufficient cross-referencing to the different locations where executive remuneration disclosures have been made. None of the companies in the “less than” category made use of cross-referencing in their Annual Reports, and seem not to have considered any need for such cross-referencing. A majority of companies in the “same as” category were in the same position. This is in sharp contrast to the disclosures in single locations by companies in the “more than” category.

Styan (2009) quotes professor Mervyn King in stating that Annual Reports should be easily understandable since broad communities have a stakeholder interest in companies operating in their areas. He adds a reference to Gill Marcus, who suggested that companies were historically focused on aligning their business with the interests of its shareholders, whereas the modern belief is that companies should have more responsibilities to broader categories of stakeholders. In almost all of the interviews it was stated that shareholder interests should inform executive remuneration policies and practices, and that it was necessary to consider the information needs of shareholders when making disclosures.

“We give them what they ask for” was a recurring theme during the interviews.

Quality of information

The quality of executive remuneration disclosure depends significantly on the robustness of the financial reporting standards used in the preparation of the company's financial statements, but also on the quality of the professional advice rendered to the board and the remuneration committee. Remuneration committees that have the benefit of qualified and independent executive remuneration advisors tend to make more informative disclosures of executive remuneration. Far too often, consultants who are employed to complete multiple general assignments in a specific company advise the remuneration committees of those same companies. This is a risky strategy if the consultant considers the impact on potential further engagements with the company before making its recommendations. Advisors to remuneration committees should be independent, and free of any other commitment with the company which could create even a perception of conflict. This includes those consultants who provide market survey data generated by themselves to those companies while also consulting to the companies on remuneration issues. In most cases they then rely on their own survey data to promote their consultancy solutions.

It is commonly believed to be important to provide shareholders and other stakeholders with the information needed to enable them to hold executives accountable for the remuneration they extract from the company. Companies in the "more than" category also disclosed details regarding the remuneration paid to individual executives in the preceding financial year, to enable stakeholders to consider whether the remuneration is appropriate in comparison with the performance of the company from one year to the next. This practise is already

a requirement under the UK disclosure requirements, and is certainly followed expressly by two companies in the research sample who have business interests in the UK. In the same way it is necessary for shareholders to be informed of packages paid to executives on termination, and especially when companies have performed poorly. A case in point is the huge termination package paid to the former CEO of South African Airways in 2009 after extremely poor financial results posted by the airline, and the dubious circumstances under which he had to vacate his position.

Much more detailed disclosures, which include an explanation of the figures contained in the standard remuneration tables, are provided by companies in the “more than” category. This includes:

- Individualised total rewards tables;
- Narratives explaining the remuneration tables;
- Full details of incentive plans; and
- A clear link between performance and reward.

An interviewee in the “more than” category remarked that *“remuneration tables with figures alone often do not provide clear and relevant information shareholders require. It has to be supplemented by a narrative that links the figures to the remuneration strategy of the company”*. This is indicative of the insight remuneration specialists have to offer in the executive remuneration/corporate governance debate, and strongly supports the case for use of such specialists in modern corporations.

Conclusion

The disclosure of comprehensive, accurate and timely information by companies adds to investor confidence and good corporate governance (McKinsey, 2002). It is therefore important for listed companies to ensure appropriate transparency towards investors to enable them to express their views and to make fully informed decisions on where to invest their funds. Table 24 below sets out the most common factors identified by interviewees that inform companies' executive remuneration disclosure choices, in order of prevalence.

Table 24: Factors influencing companies' disclosure choices

Research category	Disclosure choices
Disclosure less than what is required	Risk aversion (personal and corporate)
	Intended recipients of disclosed information
Disclosure same as what is required	Regulatory requirements
	Shareholder needs
	Historical practices (old habits)
	Shrinking effect of transparency
	Unwanted attention and risks
	Multiple listing requirements
	Strong compliance culture
	Understanding of potential value add
Disclosure more than what is required	Regulatory codes and requirements
	Knowledge and participation rate of Board and Board Committees
	Balance between commercial sensitivity and transparency
	Ethics
	Corporate culture

Shareholders expect companies to provide transparent, succinct and easily understood details of their executive remuneration practices and policies, in order to:

- Ensure alignments between executive actions and shareholder returns;
- Ensure that conflicts of interest are managed appropriately;
- Align executive actions with the achievement of the company's business strategy;
- Reward good performance by the company as well as those individuals who contribute to it;
- Drive desirable behaviour to achieve business objectives; and
- Recruit, motivate and retain high caliber executives.

To be effective, disclosure of executive remuneration ought to be broader and more comprehensive than is currently required in South Africa, must be made timely to allow for information symmetry between shareholders and executives of the corporation, and must be specific in relation to performance criteria and measures. The more comprehensive UK disclosure requirements may be a model to follow in the development of case appropriate and specific governance control measures.

Such disclosures should therefore not only publish information on the levels and composition of executive remuneration packages, but should also identify the principles underlying the design of executive remuneration packages, and the performance criteria for the allocation of incentive rewards. Simplicity in relation to both the content and placement of executive remuneration information in the Annual Report of a company will go a long way to satisfy agency and accuracy

enhancement needs of shareholders, and is a standard practise amongst companies with experienced and dedicated remuneration specialists who are responsible for all aspects of remuneration management in those companies.

11.3.2.4 *Fourth Proposition*

Disclosure of executive remuneration is one of the sub-systems in a larger corporate governance framework, in which different sub-systems interrelate to form an inclusive corporate governance framework.

In order to test the fourth proposition, the following questions from the interview schedule was asked and discussed with each of the interviewees:

- What is the relationship between disclosure, corporate governance, and executive remuneration?
- What role do boards and board committees play in the disclosure process?

Disclosure, corporate governance and executive remuneration

It is generally accepted that the disclosure of executive remuneration levels, the processes to determine it, and the fundamental principles and aims that underlie it, will contribute to entrench the seven characteristics contained in the King I Report into the company's culture. These principles are discipline, transparency, independence, accountability, responsibility, fairness, and social

responsibility. In addition it will also support the three pillars on which the King II Report was built, namely openness, integrity and accountability.

Although there was general consensus amongst interviewees of this philosophy, there were marked differences in their approaches to executing it. Most of the companies that disclose more than what is required have come to realise that, in order to do so, executive remuneration disclosures have to be both forward looking (accuracy enhancement model) and backward looking (agency cost model). They believe that such disclosures will satisfy shareholders, who are dependent on proper information disclosures to make business governance decisions. Proper information in this instance not only relates to comprehensive information which would enable informed decision making, but also timeous disclosure thereof, so that there is information symmetry between executives and shareholders (Mongalo, 2007). In relation to executive remuneration, this includes details regarding all components of executive remuneration packages, the aim of each component, the process for determination thereof, eligibility criteria, as well as the allocation and performance measures which will be applied to it. In both the other two research categories there is still a very strong focus on backward looking disclosures to ensure that shareholders are able to monitor the extent to which executive performance and remuneration is aligned to shareholder interests.

Almost all of the interviewees believe that disclosure in itself is not enough to ensure effective corporate governance in a corporation. It is believed to be most effective when it leads to and facilitates further action. Such action include, amongst others, informed stakeholder decisions, and activism around issues of

concern. This confirms the general view expressed by commentators in the literature review (Ablen, 2003; Mongalo, 2007). Disclosure is therefore seen to be one of the least costly and least invasive corporate governance mechanisms, as it merely presents information to stakeholders, who may or may not act upon it. This is in sharp contrast to the very strict regulations passed in the USA in response to the financial markets crisis of early 2009, when “comply or else” type legislation was passed to place upper limits on the total remuneration levels paid to corporate executives in the USA, which, as a governance measure, is highly invasive.

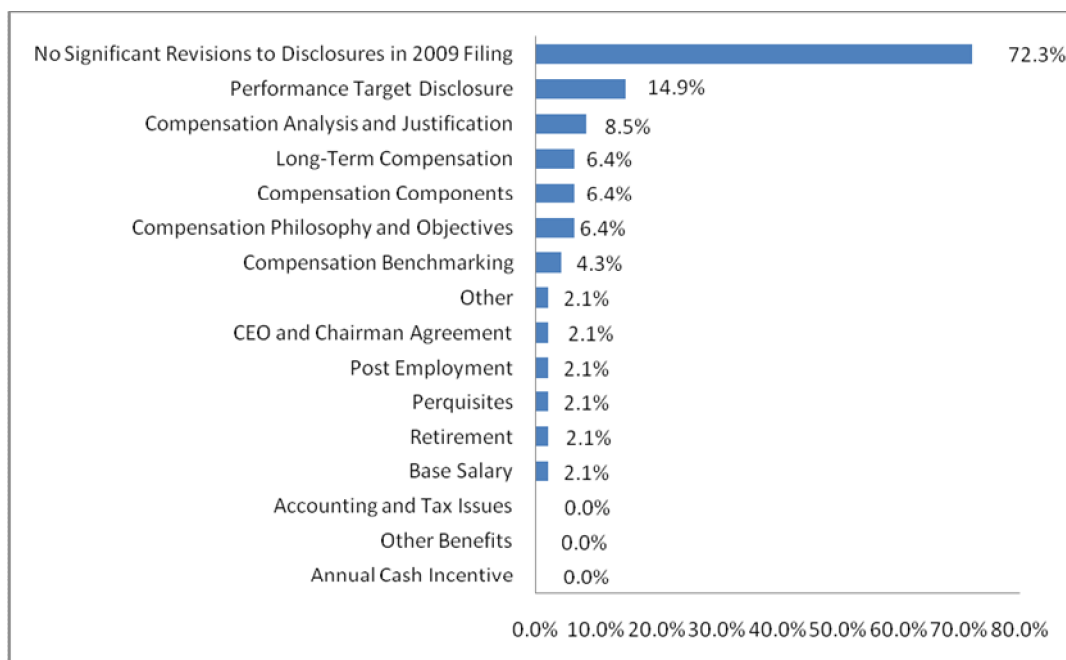
The Corporate Leadership Council (2009c) reports on a study in the USA which investigated how the disclosure practices of 20 USA companies changed after the introduction of the stricter SEC disclosure requirements. The study found that:

- 17% of these companies’ disclosures showed increases in the length of their reports;
- Disclosures became more progressive than incremental; and
- Of those companies revising their disclosure, most are focused on providing greater clarity around performance targets, compensation justification, and long term incentives.

Figure 17 below shows the areas of executive compensation disclosure which have undergone significant revisions as a result of stricter disclosure requirements under the SEC in the USA. It is interesting to note that more than 70 % of companies have not planned any significant revisions of their disclosure practices.

It was interesting to note how few of the interviewees had already considered the potential impact of the draft King III Report on executive remuneration disclosures in the 2009/2010 financial year, despite early indications of significant changes that may be required – especially for those companies that currently disclose less than the minimum requirements.

Figure 17: Areas of compensation disclosure being revised due to SEC requirements



(Corporate Leadership Council, 2009b)

Disclosure of executive remuneration therefore fits comfortably in a corporate governance framework, as an external corporate governance control measure, by facilitating further direct action in response to the information disclosed. There is significant agreement that disclosure of executive remuneration in itself does not eliminate corporate governance failures that could be attributed to the conflict between owners and managers of a corporation, but it does enable

further action. This supports an integrated view of corporate governance, as developed in the model contained in Annexure B hereof. The compounding effect of different and interrelated corporate governance control measures, if implemented effectively, however could have a profound impact on reducing corporate governance failures.

The role of Boards and Board Committees in disclosures

Although executive remuneration levels, processes and policies are ordinarily determined by the remuneration committees of boards, all interviewees agreed that it is ultimately still the responsibility of the board to take accountability for it. This responsibility includes:

- Being fully aware of what is required in terms of disclosures;
- Knowing what all stakeholders of the company need or want to know;
- Knowing industry, sector and market trends in executive remuneration practices;
- Adopting remuneration policies and practices that enhance the ability of the company to create sustainable shareholder value, and are aligned with the business strategy and corporate objectives of the organisation;
- Corroborating any advice received in respect of executive remuneration from independent and trustworthy sources;
- Satisfying itself that performance targets are realistic and relevant, and that performance measurements have been done properly and are verifiable;

- Constantly seeking safeguards for independence and discharge of fiduciary duties; and
- Placing a high value on corporate, executive and board ethics.

Most interviewees believe that Boards should furthermore promote and facilitate a culture of fiduciary self constraint by all directors of the company, and constantly monitor the alignment of executive interests with long term value creation for the shareholders and other stakeholders of the corporation. The constitution of boards comprising of a majority of independent non-executive directors is an effective tool in addressing the conflicted executive pay-setting environment, but is still not believed to be the complete solution. It was suggested that the solution rather lies in an appropriate mix of internal and external corporate governance control measures that balance the interests of shareholders, executives, and other stakeholders to the long term benefit of all concerned. One interviewee aptly remarked that *“Remuneration Committees nowadays need to engage with shareholders and other stakeholders on their information needs in respect of executive remuneration”*.

One of the key features of those companies that fall into the category of executive remuneration disclosures in excess of what is required, is the level of training offered to its board and remuneration committee members. Such training not only includes board process and corporate governance training, but also training on different aspects of executive remuneration practices. In contrast, none of the companies that disclose less than what is required have actively trained its non-executive directors, and especially those serving on their

Remuneration Committees, in different aspects of executive remuneration, other than fairly generic board practice training.

The former President of the USA, George W Bush, summarises the role of the Board of Directors vis-a-vis executive remuneration as follows:

“The main governance for executive compensation ought to be at the Board of Directors level. I am staggered by some of the compensation levels, and I think...compensation packages should be fully transparent in easy-to-understand language...”

George W Bush

Conclusion

Ultimately, internal corporate governance mechanisms (composition of board and board committees, relationships between different categories of directors) and external corporate governance mechanisms (regulatory prescriptions, disclosure) have to be addressed holistically and in a balanced way to be effective. In South Africa, under the King II Report, internal corporate governance mechanisms were still favoured strongly, as is the case in Europe under their relevant governance codes. This has not only entrenched agency theory as the dominant rationale for disclosure in South Africa, but also created a culture of mere compliance with the guidelines contained in King II. It has already been shown that almost 75% of listed companies in South Africa have a policy of ensuring at least compliance with disclosure requirements, in order to

avoid having to provide an explanation for their failure to comply. It is however in the interest of corporate South Africa to find a workable balance between internal and external corporate governance control measures, within a framework which sets out minimum requirements, but nevertheless provides some flexibility. This would not only be in line with the current “comply or explain” principle followed by, amongst others, the King II Report, but would also satisfy the apparent shift to an “apply or explain” principle favoured in the draft King III Report in South Africa.

The most common views on the role of Boards and Board Committees in disclosure of executive remuneration, as identified by the interviewees are as set out in Table 25 below.

Table 25: The role of Boards and Board Committees in disclosures

Research category	Role in executive remuneration disclosure
Disclosure less than what is required	Board Committee should provide a disclosure framework for the Board to approve
Disclosure same as what is required	Board retains accountability despite staff preparing proposals
	Board must still apply its collective mind
	Board must ensure clarity, fairness, understanding and a balance of interests through disclosure practices
	Board must link executive pay to performance targets
Disclosure more than what is required	Ensure compliance with regulations
	Ensure high degree of executive and corporate ethics
	Holistic approach and integration of corporate governance control measures
	Board must set remuneration and disclosure strategies
	Ensure disclosures are understandable to lay persons

11.3.3 Conclusions

Corporate governance systems across the world face the problem that corporate governance control measures appear to be ineffective in preventing corporate failures which could be linked directly to the conflicts of interest between executives and shareholders. Neither strict legislation (such as in the USA), voluntary compliance codes (such as in the UK), or stock exchange listing requirements have impacted with great success on these failures.

The nature of disclosure of executive remuneration can take one or both of two forms, namely informative or monitoring disclosures. Informative disclosures are forward looking in that it provides relevant information to stakeholders to enable them to make informed decisions. Monitoring disclosures are backward looking in that it provides information to shareholders to monitor executive actions and its alignment to the creation of shareholder value (Mahoney, 1995).

Effective disclosure of actual executive remuneration packages, the linkage thereof with specific objectives and philosophies, and the process and factors for determination of executive remuneration packages, have a potentially significant contribution towards an effective and inclusive corporate governance framework, but cannot solve all its problems in isolation. The most appropriate mix between internal and external control measures must be found and implemented to ensure an effective overall corporate governance system, which also allows for stakeholder participation and activism. Disclosure as a mechanism to monitor, control and inform executive remuneration is an

increasing phenomenon worldwide. It is however applied in different ways in companies.

In this research, open-ended information collected from the qualitative interviews and focus group were analysed to provide deeper insights to test the four stated research propositions.

There was strong agreement that the failure of corporate governance control measures could be directly ascribed to the unequal power positions of managers compared to shareholders in the modern corporation. Boards are being captured by conflicted executives who manipulate corporate governance control measures to advance their own interests rather than those of the owners of the corporation. This manipulation includes effectively determining their own rewards and making disclosures which, in terms of timing and content, serve their own interests. Negotiations between boards and executives are often not at arms' length, which means that boards and remuneration committees have not been very successful in curbing abuses of power by executives.

Both internal (board and committee composition, and relationships) and external (regulation and disclosure) corporate governance control measures are not applied to its full potential across all industries, and contribute greatly to corporate scandals and failures, as a result of the inability of stakeholders to not only exercise effective control over executives, but also to make informed investment decisions.

The consequences of the failure of corporate governance control measures, as far as it relates to executive remuneration, materialise in undue ratcheting of executive pay levels and a pay-setting process that is not realistically linked to good performance or the value added by the respective executives. Powerful executives are able to manipulate both the levels of their remuneration packages as well as the process for the determination thereof, to their own benefit.

Effective disclosure of both executive remuneration levels (and the factors that inform those levels) and an objective and independent process for the setting thereof within a corporate strategic framework could contribute significantly towards a more effective corporate governance system. Disclosure however has direct and indirect cost implications which could impact on the extent to which companies can disclose from a cost-benefit perspective. In addition, some social issues must be considered when the extent of disclosure is decided upon by a company.

The McKinsey Report (2002) has already shown that the disclosure of relevant, comprehensive, and timely information adds to investor confidence in the company, and contributes to good corporate governance control measures in these companies. The King II Report refers to this as “shrinking effects”, in that it deters executives from taking advantage of opportunities to serve their own interests above those of the company and its shareholders. It is however necessary for the disclosure requirements to be matched carefully with what is needed by shareholders and other stakeholders for the protection of their interests. This includes backward and forward looking information, which do not

only relate to levels and composition of executive remuneration packages, but importantly also to the underlying reasons for designing those packages, as well as the performance criteria which have to be met by executives before performance incentives are allocated to them.

Mere disclosure of executive remuneration on its own is however not effective unless it enables further action by stakeholders, shareholders or activists, or supports the introduction of sanctions against executives who do not fulfil their fiduciary duties to a required level. The intricate relationships between internal and external corporate governance control measures should therefore be balanced carefully to produce the most effective corporate governance system in each individual company, while remaining within a framework of principles that underlie the desired governance state in the company.

Boards, through their remuneration committees, should therefore pursue at least the following principles in relation to the disclosure of executive remuneration information by the company:

- Performance measures must be aligned with the achievement of business strategy;
- Shareholder views must be obtained before adoption of and publication of executive remuneration packages and strategy;
- Payment of incentive bonuses must be directly linked to relevant performance objectives which are set objectively and upfront;
- Executive remuneration payments must be justified in terms of financial performance of the company;

- There is a need to examine the impact of different remuneration related behavioural drivers to improve future remuneration designs;
- Internal equity and external competitiveness must be balanced carefully; and
- Executives should not be rewarded for poor results.

The Corporate Leadership Council (2009b) proposes that companies should include in their risk assessments an evaluation of executive remuneration and disclosures in terms of the questions below, for which there was found to be strong support in the interviews conducted during this study.

- Is the executive remuneration strategy sufficiently tied to company and individual performance?
- Do the potential executive rewards outweigh the risks senior executives might have to take to pursue the goals set in compensation plans?
- Are all executive perquisites disclosed and explained?
- Is the rationale for executive remuneration levels and packages explained clearly in investor-facing communications?
- Are all performance targets disclosed?
- Are targets set in relation to appropriate peer groups?

The same Council concludes that the quality of executive remuneration disclosure is ultimately determined by:

- the clarity of disclosures and the extent to which the disclosed content and context is understood by ordinary readers thereof;
- the remuneration philosophy of the company and its link to the achievement of corporate objectives; and

- the adoption of objective and realistic performance targets.

(Corporate Leadership Council, 2009a)

It appeared from data collected in both the interviews and the focus group that there is strong support for the proposition that corporate governance failures result from ineffective internal and external corporate governance failures. The reasons for such ineffectiveness however vary significantly from one company to the next. These reasons include a lack of understanding of both the relevant governance and executive remuneration constructs, and the consequences of uninformed executive decisions. This could often be directly attributed to the lack of dedicated and experienced specialists to take care of the highly complex reward and governance activities in an organisation.

There was also strong support for the proposition that a failure of corporate governance control measures could lead to symptoms such as excessive executive remuneration levels and a flawed process for the determination of executive remuneration packages. The research has shown some alarmingly high levels of failures of board members to apply their minds proactively and assertively in the protection of stakeholder interests, to avoid these symptoms from materialising. Unfortunately, it appears that the most popular solution to this problem is to develop more and more control measures to address assumed universal problems instead of addressing the causes of these symptoms principally.

Effective and tailored disclosures of executive remuneration levels, the process for determination thereof, and the underlying reasons for the manner in which

executive remuneration is managed in an organisation is generally agreed to have merit. The limited extent to which most South African listed companies have however applied their minds to this understanding has however had a negative impact on creating effective and integrated governance systems in organisations. Dedicated specialists should be responsible for managing these complex areas in businesses.

Disclosure on its own is however not a sufficient corporate governance control measure. It has to operate within an integrated governance system, where it interacts with and facilitates other control measures, such as the model depicted in Annexure B. In order to create such an integrated governance system, it would be optimal to first identify the principles that are universally applicable to protect stakeholder interests, and thereafter to implement such flexible governance control measures as are most appropriate for the specific company. A delicate balance will have to be found between various conflicting interests in the process. The individual needs of the company and its stakeholders have to inform the choices in this regard.

12. CONCLUSIONS AND RECOMMENDATIONS

In this chapter, conclusions are made in relation to the research problem, research objectives, research propositions, and research findings, where after some recommendations are made.

12.1 Research problem

The ability of traditional corporate governance control measures to adequately cope with the increasing conflicts of interest between shareholders, as assumed owners of modern corporations, and increasingly powerful executives who run these corporations, has increasingly been brought into question of late. The main problem which informed this study was therefore that it seems that corporate governance as a construct has not kept pace with the development of the modern corporation, and to such an extent that corporate governance control measures have become ineffective in many ways. The ineffectiveness of corporate governance control systems in turn causes symptoms that impact on the core rationale for the modern corporation. One of these symptoms is excessive executive remuneration. Another symptom is the inefficient executive remuneration pay-setting process. These symptoms of ineffective corporate governance control measures result from both internal (board composition and effectiveness) and external (disclosure and regulation) deficiencies. Each of these has an individual and collective impact on the total corporate governance system in a firm.

In order to achieve a solution to the research problem, the main purpose of this study was to understand disclosure of executive remuneration, as an external corporate governance control measure, in a corporate governance framework, and to determine whether, and if so, how disclosure of executive remuneration could contribute towards more effective corporate governance in corporations.

An integrated model for corporate governance was developed in Annexure B hereof. This model shows how internal governance control measures (board composition, board committees, auditors), external governance control measures (legislation, regulation, disclosure), and activism (proposals, negotiation, labour action), as sub systems in an overall corporate governance system, interact with one another in an integrated framework.

The research has shown that much of the reform focus to address corporate governance failures have been on developing more and seemingly better governance control measures. A more credible solution would be to develop a solution based on common underlying principles, supported by a flexible framework of guidelines in respect of possible governance control measures which could be tailored to the needs of individual companies.

12.2 Research objectives

Both the literature review and the actual research disclosed that effective disclosure of actual executive remuneration packages, the linkage thereof with specific objectives and philosophies, and the process and factors for determination of executive remuneration packages, have a potentially

significant function in an effective and inclusive corporate governance framework, but cannot solve all its problems in isolation. It is in essence a mechanism to facilitate both monitoring and informed activism by different stakeholders. The most appropriate mix between internal and external corporate governance control measures, and informed activism, must be found and implemented to ensure an effective and inclusive overall corporate governance system, in which a proper balance is found between positive and negative consequences.

Disclosure is one possible mechanism to monitor, control and inform executive remuneration is an increasing phenomenon worldwide. The manner and extent to which it is however used across the world varies significantly. These differences not only relate to societal and legislative influences, but also to the levels of understanding of the underlying aims of disclosure of executive remuneration as a corporate governance control measure. Although disclosure may not always produce intended or positive consequences, it should not be disregarded as a powerful governance control measure in most instances. This research has shown that the level of understanding and optimal application of both forward looking and backward looking disclosures have been fairly poor in South Africa to date. The use of specialists in the fields of corporate governance and executive remuneration has been proposed as a meaningful contribution towards more effective executive remuneration management, disclosure choices, and corporate governance.

The main objective of this study was therefore to understand how an effective system of disclosure of executive remuneration, which is both informative (or

forward looking) and allows for executive monitoring (or backward looking), fits into an inclusive and effective corporate governance system in South African listed companies. This was done by means of both a literature review, which provided the theoretical basis for a broad understanding of disclosure of executive remuneration as a corporate governance control measure, and focused qualitative interviews to source data on practical applications in the field.

The research has shown that there is still a low level of understanding amongst South African listed companies of the full potential of disclosure as a corporate governance control measure. This could be related directly to the level of dedication and experience of specialised skills in the fields of executive remuneration and corporate governance by most South African companies at the time of the research.

12.3 Research propositions

Four research propositions were developed from the literature review, and formed the basis for the analysis of data collected during the quantitative and qualitative phases of the research.

- First Proposition

Corporate governance failures result from ineffective internal and external control measures and systems.

- Second Proposition

Both the levels of executive remuneration and the process for determination thereof are symptomatic of the failure of corporate governance control measures.

- Third Proposition

Effective disclosure of executive remuneration determination processes and levels, as a corporate governance control measure, contributes to a more effective overall corporate governance system in organisations (i.e. there is a positive correlation between disclosure and good corporate governance).

- Fourth Proposition

Disclosure of executive remuneration is one of the sub-systems in a larger corporate governance framework, in which different sub-systems interrelate to form an inclusive corporate governance framework.

12.4 Research analysis and results

The research process after completion of the literature review, and development of the research propositions, was multi phased. In the first phase the actual minimum disclosure requirements for South African listed companies was collated from relevant legislation, the King Codes of Corporate Governance, and the JSE Listing Requirements. This in itself contributed to a better understanding of the requirements by especially inexperienced staff who are often tasked with remuneration and governance compliance requirements that fall outside of their ordinary tasks.

The following conclusions have been made in relation to the literature review, South African executive remuneration disclosure requirements, quantitative analysis of the executive remuneration disclosures in the 2007 Annual Reports of companies listed on the JSE in South Africa, and qualitative analysis through interviews with representatives from a research sample and focus group, as part of the data collection phase of this study.

12.4.1 Literature review

Although constructs such as corporate governance and executive remuneration have been actively debated for decades, its prominence increased dramatically in the last few years as a result of widely published corporate collapses and scandals of the last decade. Even after a global spate of legislative and regulatory interventions after the major corporate collapses over the past twenty years, the collapse of major corporations and financial markets in 2008, and the resultant global economic recession, has shown that those significant interventions have not been effective in preventing failures of corporate governance control measures in even companies which seemingly complied well with the required governance measures.

Both the literature review and the major corporate governance regulations across the world seem to now acknowledge that it is not completely possible to prevent bad ethics from causing corporate governance failures, despite seemingly comprehensive corporate governance regulation. This has also been confirmed in almost all of the interviews conducted during the research.

The most dominant theory used to explain the separation of the ownership for control in modern organisations, and the role of executive remuneration in the process, has historically been agency theory, which considers incentive-based executive remuneration as essential tools in establishing alignment between self-interested executive actions and the interest of shareholders. This research has found overwhelming support of agency theory amongst South African listed companies as far as their disclosures of executive remuneration is concerned.

Stakeholder theory, which was developed to consider the alignment of executive actions with the interest of a wider group of stakeholders, has however become increasingly attractive during the last decade, and especially amongst academic commentators.

The most fundamental issue in the executive remuneration debate, as emanated from both the literature review and interviews, relates to the alignment of conflicts of interest between shareholders and powerful executives, who enjoy opportunities to serve their own interests above those of shareholders. A number of different internal and external corporate governance measures have been developed over time, and imposed through direct legislation, listing requirements and voluntary codes of best practice regulation, but have been described as plasters on an open sore, which will not necessarily heal the underlying cause of the executive remuneration problem, namely the abuse of power by self serving executives.

One of the corporate governance measures developed, and implemented to varying degrees across the world, is the disclosure of executive remuneration.

Most authors on the subject agree that the underlying objective sought to be addressed by such disclosure is to create transparency with regard to executives in an organisation, and thereby to ensure a greater level of alignment between executive actions and shareholder interests in the corporation.

Disclosure of executive remuneration however has both positive (intended) and negative (unintended) consequences. The intended positive consequences of disclosure relate to the executive monitoring informative value and regulatory techniques thereof, while the unintended or negative consequences relate to privacy deprivation and pay ratcheting effects of benchmarking salaries unscientifically and unjustifiably, as well as additional direct and indirect costs that may be caused by disclosures.

The literature review has revealed that disclosure practises around the world could generally be grouped as either full disclosure (Anglo-American) or limited disclosure (continental Europe). Although there are still significant differences in the extent of disclosure amongst different countries, based mainly on economic, political and culture variables, a convergent trend towards a more uniform approach to dealing with executive remuneration and corporate governance is observable. One of the strongest reasons advanced for such convergence is the increase in globalisation and the global market for scarce executive talent.

The research suggested that such convergence could however only be at the level of principles rather than specific control measures, as a result of the deep differences amongst political, social, legal and environmental systems. Where

certain underlying principles of executive remuneration and corporate governance could conceivably be of universal application, the same does not necessarily apply for specific governance control measures. A credible solution would be to allow companies a degree of flexibility in selecting case appropriate control measures in relation to their individual needs, but which are directly linked to the framework of underlying principles promulgated under specific regulation.

There is general consensus amongst commentators that disclosure of executive remuneration policy and packages *per se* would not be sufficient to address the problems with executive pay practices and levels. Disclosure is only a tool that enables further action, of which the most significant would be the ability of shareholders and other activists to exercise more informed oversight over executives, and to make more informed investment and other decisions. This is consistent with the results obtained from the qualitative interviews conducted in this research.

These supportive corporate governance mechanisms can be divided into internal and external measures. Internal measures refer to those mechanisms dealing with the relationship between directors, executives, shareholders, and other stakeholders. In contrast, external measures refer to the legal, regulatory and administrative frameworks for corporate governance in the company (including disclosure and other outside control measures to protect shareholder interests). As will be discussed below, the South African corporate governance regulatory focus, through mainly the King Reports on Corporate Governance, have been primarily on internal corporate governance control measures.

Although a measure of global consistency in respect of a corporate governance framework is required, commentators agree that there should be some flexibility to allow individual companies and countries to operate competitively in their particular environments. An appropriate mix of internal and external corporate governance measures should therefore be applied with a measure of flexibility within a guiding global framework.

12.4.2 Executive remuneration disclosure requirements

Disclosure of executive remuneration in South Africa is regulated mainly in terms of the Companies Act of 1973, the King Codes on Corporate Governance, and the JSE Listing Requirements. Broadly speaking, an analysis of these sources has shown that the remuneration aspects which have to be disclosed in terms thereof must include:

- basic salary or guaranteed pay, broken down into components of basic salary and all other costs of employment;
- benefits;
- short-term incentives (including high level design principles or targets);
- long-term incentives (including high level design principles or valuation methodology, or any interest in share capital); and
- severance arrangements.

In terms of some general, over-arching disclosure principles, remuneration committees of listed companies are required to prepare a remuneration report for the company, which should include a disclosure of the company's

remuneration policy, for approval by the board, and subsequent publication in the Annual Report of the company. Such report should also provide full disclosure of individualised director remuneration, which includes details regarding basic salary, short- and long term incentives, severance payments, loans and other benefits received, and interests in business dealings with the company.

Based on the requirements of the Companies Act of 1973, the King Reports on Corporate Governance in South Africa, and the JSE Listing Requirements, the collated disclosure requirements in respect of publicly listed companies in South Africa have been summarised as set out in the Annual Report Disclosure Compliance Index, which appears as Annexure J hereto. This Index was used to analyse the compliance of companies listed on the JSE in South Africa, in relation to disclosure of executive remuneration in the 2007 Annual Reports of all JSE listed companies (excluding those listed under the AltX and Additional categories). Such analysis formed part of the second and third analysis phases of this study methodology, namely the quantitative and qualitative data collection and analysis phases.

The key requirement and rationale for disclosure of executive remuneration is the effective link of rewards to performance. This has not only been borne out in the literature review and the regulatory codes in South Africa, but was also confirmed in a majority of the interviews conducted. It is specifically for the remuneration committee to establish and monitor such a link, and to align the interests of directors and shareholders in promoting the company's progress towards achieving its strategic objectives and increased stakeholder value. The

long term performance and sustainability of a company must however also be a matter of great concern to the shareholders and other stakeholders of the company, who not only have a right to be informed but also a duty to enforce such right against executives. Three fundamental principles have been identified that underlie stakeholder interests in this area, namely accountability, transparency, and linkage to performance.

Although a fairly general view is held that it is important that companies and their remuneration committees adopt a philosophy of full transparency so that shareholders have access to all the information they may reasonably require to enable them to assess the company's general policy on executive remuneration, both the analysis of disclosures in the 2007 Annual Reports, as well as some interviews, have shown that companies, while they might state this intention, often only pay lip service to it.

In the same way, it is necessary for companies to disclose information to current and potential investors, in order for them to make informed investment decisions, which are based on full and equally available information, and which may lead to informed activism in this area.

12.4.3 Quantitative analysis

The analysis of the content of the 2007 Annual Reports of South African companies listed on the JSE, as far as it relates to disclosure of executive remuneration, showed significant differences in relation to the location of such disclosures in the Annual Reports, the content disclosed, and the extent to

which shareholders and other stakeholders are able to monitor executives' performance of their fiduciary responsibilities.

Companies which disclose more than what is required in terms of the South African Companies Act, the King Reports on Corporate Governance and the JSE listing requirements typically disclosed all aspects of executive remuneration in a single and comprehensive chapter in their Annual Reports, which chapter deals exhaustively with executive remuneration strategy, practices and levels. Such disclosures not only, as was the case with most companies which disclosed less than or equal to the disclosure requirements, disclosed the levels of executive remuneration paid to executives of the company, but also the factors that inform such levels, and the process for transparent determination of executive remuneration packages in those companies. Although no direct or coherent reasons were advanced for these differences, the context of the responses in this regard has shown that on the one hand companies deliberately only comply with the minimum disclosure requirements, and on the other hand do not apply their minds to the need and strategic value that lies beyond historical disclosure practices. In the last instance the interviews revealed that many companies do not even consider fully whether their disclosures are sufficient to satisfy forward- and backward looking stakeholder needs in a changing and global environment.

The general level of understanding of the full potential of disclosure of executive remuneration as a strategic corporate governance control measure seems to be relatively low amongst South African listed companies. Despite the progressiveness of corporate governance codes in South Africa, the specific

executive remuneration contained in those codes still significantly lag the similar disclosure requirements contained in the Combined Code in the UK, which could be regarded as the benchmark in this regard.

In most industries and sectors within those industries, almost 75% of companies tend to make executive remuneration disclosures which were on par with the minimum disclosure requirements for executive remuneration in South Africa at the time of the research. Besides this general trend, there were more companies across these sectors and industries that disclosed more than what is required than there were companies that disclosed less than what is required. Companies in these two research categories were however still fewer than those that disclosed exactly what was required. Companies in the Banking, Media, Household Goods, Oil and Gas, and Mobile Telecommunications sectors tended to disclose more than what is required, whereas companies in the Coal Mining, Travel and Leisure, Oil and Gas, and Development Capital sectors tended to disclose less than what is required.

A chi-square test was done to test whether there was a relationship between the extent of disclosure of executive remuneration and JSE listed industries in South Africa. The results of the chi-square test showed that, based on such disclosures in the 2007 Annual Reports of those companies, there was such a relationship but that, in terms of Cramer's V test, the strength of this association was weak.

It was possible to make some observations and primary conclusions regarding what distinguished between the disclosures of companies in the three different

research categories. In respect of companies that disclosed less than what is required in relation to its executive remuneration, it was found that the levels of executive remuneration were often aggregated as opposed to individualised in respect of each pay component in the total reward packages. In addition, no clear or comprehensive remuneration philosophy followed by these companies had been disclosed, to the extent that it was not possible to evaluate the basis for the levels of remuneration paid to executives in these companies. Details regarding the payment of short term and long term incentives, as well as income (other than remuneration) paid to executives were lacking. These companies tended to focus on “what” and “how much” questions rather than also on “why” and “how”.

Those companies whose executive remuneration disclosures in their 2007 Annual Reports fell into the category of more than required disclosures, generally made such disclosure in a separate chapter that dealt with all required executive remuneration issues comprehensively and in a single location in their Annual Reports. Such chapters not only disclosed the remuneration philosophy followed by these companies, but also disclosed the levels of executive remuneration, the factors taken into account when developing such remuneration packages, the process for determination of executive remuneration packages, and the performance metrics set for payment of both short and long term incentives offered to executives. In these cases both shareholders and other stakeholders were very well informed of not only the levels of executive remuneration paid in these companies, but also the performance measures set for executives to qualify for short and long term bonus payments. In addition to disclosing executive remuneration levels to

stakeholders, therefore, the reasons for and determination process of those remuneration packages were disclosed. “What”, “how much”, “why” and “how” questions were generally addressed in these disclosures. This provided much clearer information to stakeholders to both monitor executive performance, and to make informed investment decisions.

In companies whose executive remuneration disclosures merely complied with the minimum disclosure requirements, different elements of executive remuneration were commonly found in different locations in their Annual Reports, and without proper cross-referencing. The disclosures made in those sections were however weak, and in most instances did not provide stakeholders with sufficient information to eliminate risks associated with information asymmetry between executives and stakeholders of the company. Only limited answers to “why” and “how” questions were provided, if at all.

It should be noted that most companies that fell into either the categories of less than or equal to the requirements for disclosure of executive remuneration focussed almost exclusively on disclosures of the levels of remuneration paid to executives of these companies, rather than to disclose the criteria which informed such remuneration levels. In comparison, companies that fell into the category of disclosures in excess of what is required, disclosed not only the levels of executive remuneration packages, but also the philosophies that underpinned the payment of these levels of remuneration and the performance criteria which had to be achieved by executives to qualify for such payments.

The objective with the qualitative interviews, which were both designed and conducted in accordance with the open ended Interview Schedule contained in Annexure K, was to clarify the reasons for these differences, in order to ultimately create an understanding of disclosure of executive remuneration disclosures as a sub-system in an integrated framework of corporate governance control measures.

12.4.4 Qualitative analysis

The literature review has revealed that disclosure of executive remuneration could take one or both of two forms, namely either informative or monitoring disclosures. Informative disclosures, which are forward looking in nature, seek to address imbalances in information symmetry between executives and other stakeholders, whereas monitoring disclosures, which are backward looking in nature, is intended to enable monitoring of alignment of executive actions with shareholder interests. Figure 6 above depicts a model which views disclosure in this way.

After completion of the quantitative analysis phase of the research, qualitative interviews were conducted with representatives from a sample which represented not only the three research categories, but also the five main industries of JSE listed companies, and the sectors within each. Clear themes and trends, as are summarised below, were identified from these interviews.

Corporate governance failures

There was strong agreement amongst all interviewees that the failure of corporate governance control measures could in most cases be directly ascribed to the unequal power positions of shareholders compared to managers in the modern corporation. There is still a strong perception that Boards are being captured by conflicted executives who manipulate corporate governance control measures to advance their own interests rather than those of the owners of the corporation. This accords with the strong agency based nature of South African disclosure requirements, and with Van Wyk (2009), who believes that the global failure of major banks and other financial institutions in 2008, despite their strict compliance with governance regulations, could be attributed to self service by conflicted executives in these institutions.

Both internal and external corporate governance control measures are not applied effectively by most companies. There is a general view that this could potentially contribute to corporate scandals and failures, but an almost reckless disregard of this potential risk. In addition, the composite minimum executive remuneration disclosure requirements for listed companies in South Africa do not require disclosure of the underlying reasons for particular executive pay practices, or the link between performance and reward, sufficiently to enable real shareholder activism in the field of executive remuneration.

The shift in emphasis in the King III Report from the traditional “comply or explain” principle to one described as “apply or explain” holds the potential to impact positively on this problem. In terms of the “apply or explain” principle

companies will have to explain their failures to apply the principles set out in the King III Report.

Whether the “apply or explain” principle will however go far enough to satisfy this expectation is at least questionable where there is no real effort to establish that these principles have indeed been applied, and in the absence of measures to punish failures to explain why principles have not been applied. A better solution might have been to adopt a “apply and explain” principle, in terms of which companies are required to why, how, and to what extent they have applied the King III principles. This information will undoubtedly be of more value to stakeholders. It would however require a fine balance between intended and unintended consequences of disclosures.

The most prevalent reasons advanced for ineffective corporate governance control measures, and resultant corporate failures, as have been more fully disclosed in Table 21 above, were:

- Differences in disclosure requirements in different governance frameworks;
- Unequal power positions of shareholders and managers;
- Ineffective monitoring and informative structures and processes;
- Passivity, inexperience and lack of independence of boards and board members;
- Lack of dedicated capacity to deal with corporate governance and executive remuneration issues;
- Absence of a clear link between performance and reward;
- Poor self discipline and ethics; and

- Poor or inaccurate management data.

The ineffectiveness of disclosure of executive remuneration as a corporate governance control measure is therefore not only related to the compliance with or failure to comply with minimum disclosure requirements, but also to the appropriateness of disclosure requirements to achieve its aim of protecting shareholder interests and guarding against self service by powerful executives. The transparency and shrinking effects offered by fuller executive remuneration disclosure seem to contribute to greater levels of alignment and corporate control in companies that disclose more than the minimum requirements.

Symptoms of corporate governance failures

The most common view which emanated from the qualitative interviews with regard to the consequences of the failure of corporate governance control measures, as far as it relates to executive remuneration, was that it could materialise in undue ratcheting of executive pay levels and a pay-setting process that is not realistically linked to good performance or the creation of sustainable shareholder value. Effective disclosure of executive remuneration, as one such a corporate governance control measure in an inclusive corporate governance framework as set out in Annexure B, could therefore contribute to limiting the risks of such failures. The King II Report refers to this phenomenon as “shrinking effects”, in that this control measure reduces the opportunity for abuse or manipulation of process by powerful executives. The levels of strict following of the guidelines contained in the King II Report amongst South African listed companies bears testimony to the belief amongst those

companies in its ability to do so. As Van Wyk (2009) however pointed out, strict compliance with regulatory governance codes and legislation has not prevented corporate and corporate governance failures which could be ascribed to self service by executives. Where such compliance is blindly applied in governance, without considering whether the control measures are indeed effective in addressing the underlying principle sought to be achieved, it is not strange that governance failures persist despite the existence of state of the art control measures.

Although there was a general appreciation from almost all interviewees that corporate governance failures could impact on both levels of executive remuneration and the pay-setting process, the ways in which companies have historically guarded against these risks differ significantly – especially in relation to the measure of their pro-activeness. Table 22 above indicates the perceived impact of corporate governance failures on levels of pay and the pay-setting process. It is interesting to note the remarkable similarities amongst the three research categories. The differences amongst those categories were however apparent in the manner in which they dealt with these appreciations, if at all.

Disclosure choices

Almost all interviewees accepted that effective disclosure of both executive remuneration levels (and the factors that inform those levels) and an objective and independent process for the setting thereof within a corporate strategic framework could theoretically contribute significantly towards a more effective corporate governance system. At a practical level though there was a strong

caution for the social and financial cost implications which could impact on the extent to which companies could disclose executive remuneration strategies from a cost-benefit perspective. A delicate balance is required. Table 24 above sets out the disclosure choices identified by the interviewees in each of the research categories. The common choices across the three research categories, in order of prevalence, were:

- Regulatory requirements for disclosure;
- Historical disclosure practices;
- Personal and corporate risk aversion levels; and
- The needs and preferences of the target recipients.

Commentators generally hold the view that mere disclosure of executive remuneration on its own is however not effective unless it enables further action by stakeholders, shareholders or activists, or supports the introduction of sanctions against executives who do not fulfil their fiduciary duties to a required level. The McKinsey survey report (2002) furthermore showed that disclosure of comprehensive, accurate and timely information by companies adds to investor confidence and good corporate governance. Although there was not a high level of appreciation for this view amongst companies who disclosed less than what is required in terms of the minimum executive remuneration disclosure requirements, the opposite is true for companies in the category which disclose more than what is required.

The levels of information symmetry between executives and other stakeholders (and especially shareholders) is an important aspect in the relationship between disclosure of executive remuneration, as a corporate governance control

measure, and other such control measures in an integrated corporate governance framework, as depicted in Annexure B.

Joseph Stiglitz shared the Nobel Memorial Prize in Economics in 2001 for laying the foundations for the theory of markets with asymmetric information with George Akerlof and Michael Spence. Despite well documented economic theory that market failures are at least to some extent caused by information asymmetry, Stiglitz (2002b) proposed that some degree of government intervention is required to address these imbalances. Stiglitz (2002a) emphasizes that modern economic theory has shown that whenever information is imperfect and markets incomplete, governments can improve the outcome by well-chosen interventions. In relation to corporate governance, these interventions have essentially either been through a legislative approach or through voluntary compliance with regulatory codes of compliance. The manner in which different interventions therefore materialised in different jurisdictions across the world, as have been elaborated on in the literature review, differs significantly between “no regulation”, “voluntary codes”, “listing requirements” and “legislation”. Stiglitz (2002b) concludes that the optimal range of government interventions is much larger than what traditional economic theory recognizes. The real challenge is to find the right balance between market forces and government intervention, and between advantages and disadvantages of different interventions.

To be effective, disclosure of executive remuneration ought to be broader and more comprehensive than is currently required in South Africa, must be made timely to allow for information symmetry between shareholders and executives

of the corporation, and must be specific in relation to performance criteria and measures. In view of the strong favour of mere compliance with the minimum disclosure requirements by South African listed companies, it is therefore critically important that the disclosure requirements are both meaningful and comprehensive. A disclosure framework based on specific remuneration and corporate governance principles which are applicable universally, and are supplemented by flexible governance control measure guidelines, seem to be the most appropriate universal solution.

Disclosures should therefore not only publish information on the levels and composition of executive remuneration packages, but should also identify the principles underlying the design of executive remuneration packages, and the performance criteria for the allocation of incentive rewards. Simplicity in relation to both the content and placement of executive remuneration information in the Annual Report of a company will go a long way to satisfy agency and accuracy enhancement needs of shareholders, and is already a standard practise amongst companies with experienced and dedicated remuneration specialists who are responsible for all aspects of remuneration management in those companies.

Inclusive corporate governance framework

For a corporate governance framework to be fully effective and inclusive, both the internal corporate governance mechanisms (composition of board and board committees, relationships between different categories of directors) and the external corporate governance mechanisms (regulatory prescriptions,

disclosure), as well as informed activism, have to be addressed holistically and in a balanced way, as suggested in the inclusive view of a corporate governance framework in Annexure B.

In South Africa, under the King II and King III Reports, internal corporate governance mechanisms are still favoured strongly, as is the case in Europe under the applicable governance codes in operation in each of the countries. It is however in the interest of corporate South Africa to find a workable balance between internal and external corporate governance control measures, within a framework which sets out appropriate minimum requirements, but nevertheless provides some flexibility to companies to apply in accordance with their environments. This would not only be in line with the current “comply or explain” principle followed by, amongst others, the King II Report, but would also satisfy the apparent shift to an “apply or explain” principle favoured in the King III Report in South Africa.

CONCLUSIONS FROM THE QUALITATIVE ANALYSIS

Effective disclosure of actual executive remuneration packages, the linkage thereof with specific objectives and philosophies, and the process and factors for determination of executive remuneration packages, therefore have a potentially significant function in an effective and inclusive corporate governance framework, but cannot solve all its problems in isolation. The most appropriate mix between internal and external control measures must be found and implemented to ensure an effective overall principled corporate governance system, in which informed and positive activism is enabled.

A combination of regulatory tools, which could include legislation, voluntary codes and guidelines, and stringent listing requirements, as well as effective shareholder control is essential for an effective corporate governance system. In the process of selecting appropriate governance control measures however, there are both positive and negative consequences which must be considered and balanced very carefully. The board, and especially the remuneration committee of the board, has to be vigilant, independent, and knowledgeable enough to withstand attempts by executives to capture corporate governance processes. Ultimately, it is still the board which is accountable to the shareholders for protecting their interests and for ensuring the sustainability of the organisation.

Disclosure must be meaningful to shareholders and other stakeholders, to succeed as a corporate governance control measure. Regulatory instruments dealing with minimum disclosure requirements should therefore include all aspects that would make disclosure meaningful to stakeholders of the corporation at a principled level, and allow companies to implement case appropriate control measures to give effect thereto. It must not be a “tick-the-box” compliance exercise, but should be thoroughly considered as an effective corporate governance tool by the board. Currently, the South African executive remuneration disclosure requirements focus strongly on information that only satisfy the “what” and “how much” questions associated with executive remuneration. Very little focus is given to the “why” and “how” questions, and it is left to progressive companies, who disclose more than the minimum disclosure requirements voluntarily. In an effective disclosure framework which is both backward and forward looking, and which therefore allows for both

executive monitoring and information symmetry, it is essential for stakeholders to not only know the extent of executive remuneration packages, but also the key drivers and determinants thereof. Effective executive remuneration disclosure should therefore address all of the above types of questions.

The information needs of shareholders and other stakeholders must be known to the board when the extent of disclosure is decided upon, but, in the same way, the interests of executives should be balanced with it. Such a balance will not only succeed in satisfying shareholders in readily determining the sustainable long term value of their investments, but also in attracting, motivating and retaining business executives of the highest calibre.

12.5 Findings on research propositions

This study has found support for all four stated propositions developed after completion of the literature review, which propositions were substantiated from the literature review, quantitative analysis and the qualitative interviews conducted with representatives from the selected sample companies.

The first proposition stated that corporate governance failures result from ineffective internal and external control measures and systems. The literature review revealed a strong support for corporate governance control measures to be classified as either external or internal in nature (Rahman, 2002). A model for a systems view of corporate governance in an organisation was developed, as depicted in Annexure B. This model shows the interrelatedness of different sub-systems of internal and external corporate governance control measures, and activism, in an inclusive corporate governance framework. Besides support in the literature review for the impact of a failure of one sub-system on the whole (Senge, 2006), the qualitative interviews found strong support for the proposition that ineffective corporate governance control measures have a potentially negative impact on the effectiveness of the total corporate governance system in an organisation, and may lead to a failure of the total such system. The well publicized corporate failures of the past decade, and in particular those of late 2008, bears practical substantiation of this proposition.

The second proposition developed from the literature review postulated that the levels of executive remuneration as well as the process for determination thereof are symptomatic of the failure of corporate governance control

measures. Although much of the public and academic attention in the area of corporate failures have been on the size and composition of executive remuneration packages, the research found support for the proposition that these are merely symptoms of a deeper problem. At least part of this problem relates to ineffective control measures for the remuneration of executives in the organisation. The interviews conducted in this research showed a remarkably similar appreciation amongst the three research categories for the potential impact on executive remuneration due to a failure of corporate governance control measures. There were however significant differences in their respective responses to their appreciations.

The third proposition stated that effective disclosure of executive remuneration, as a potential governance control measure, could contribute to a more effective overall corporate governance system in organisations. The literature review distinguished between backward and forward looking aims of disclosure. These relate to ex post monitoring of executive actions to ensure that these are aligned to the interests of mainly shareholders, and the creation of information symmetry between executives and stakeholders, respectively. Strong support was found for the notion that effective disclosure should be both backward and forward looking, but that a balance was required between intended and unintended consequences of disclosure. An analysis of the executive remuneration disclosure requirements for South African listed companies in comparison to other similar requirements in different jurisdictions (and especially the UK Combined Code which is regarded as a global benchmark in this regard) has shown that the South African disclosure requirements are lacking. The South African disclosure requirements tend to require disclosures

of levels and components of executive remuneration, rather than also requiring the underlying reasons which inform those levels and components, and providing stakeholders with sufficient detail to enable them to make accurate and justifiable links between executive performance and reward. The research found support for the notion that executive remuneration disclosures which provide stakeholders with sufficient information to monitor executives' performance against set performance objectives, and to facilitate informed activism, contribute positively to an effective system of corporate governance in the organisation.

The fourth proposition was that the disclosure of executive remuneration was only one of the sub-systems in an inclusive corporate governance system in which different sub-systems interrelate with each other. The model for a systems view of corporate governance in Annexure B was developed based on the revelations which emanated from the literature review. In terms of this model, disclosure of executive remuneration is viewed as an external corporate governance control measure, together with legislation and regulation. In addition to the interrelatedness of these three external control measures, there is a similar interrelation between external and internal control measures and activism, which comes from outside of the organisation. The balance that is required in this process is to be found at different points of interaction, depending on the different preferences and situations of companies and the societies within which they operate. Global corporate governance failures of the past few years have shown that, despite the existence of strict legislative and regulatory governance mechanisms, there is no single solution to the problem. A practical combination of legislation, regulation, personal ethics, and activism

is required. In addition thereto, a strong measure of self-regulation and internalisation of an ethical corporate culture is required, without which no formal legislative or regulatory governance control would be completely failsafe. The challenge is to ensure that these corporate governance control mechanisms are effective in order to provide stakeholders with the information required to protect their interests, but also to protect the organisation and its executives from any negative or unintended consequences of such disclosures.

This research has therefore found support for all four of the research propositions, in both the literature review and the analysis of the quantitative and qualitative research data collected.

12.6 Recommendations

Although the fact that the exploratory nature of the research lead to recommendations which may appear somewhat reticent, it was nevertheless possible to make some meaningful recommendations.

A combination of regulatory tools, which could include legislation, voluntary codes of guidelines, and stringent listing requirements, as well as effective shareholder control are essential for an effective and inclusive corporate governance system, as envisaged in the model for a systems view of corporate governance depicted in Annexure B. An optimal combination of internal and external corporate governance control measures must be implemented by corporations, and should facilitate informed activism in areas where stakeholder interests have to be protected. In this process however, there are both positive

and negative consequences which must be considered and balanced very carefully.

The board, and especially the remuneration committee of the board, has to be vigilant, independent, and knowledgeable enough to withstand attempts by self-servient executives to capture corporate governance processes. Ultimately, it is still the board which is accountable to the shareholders for the protection of their interests and for ensuring a sustainable organisation which creates long term value for its stakeholders.

Disclosures must be meaningful to shareholders and other stakeholders, to succeed as a corporate governance control measure. Regulatory instruments setting minimum disclosure requirements should therefore rather deal with underlying principles which ought to be applied universally. These principle based frameworks should then include all potential aspects that would make disclosure meaningful to stakeholders of the corporation, as flexible guidelines. Both backward and forward looking aims of disclosure, namely executive monitoring and information symmetry, should be included as specific control measure options therein.

Disclosure must not be a “tick-the-box” compliance exercise, but should be thoroughly considered as one potential governance tool by the board. The information needs of shareholders and other stakeholders must be known to the board when the extent of disclosure is decided upon, but, in the same way, the interests of executives should be balanced with it. Such a balance will not only succeed in satisfying shareholders in readily determining the sustainable long

term value of their investments, but also in attracting, motivating and retaining business executives of the highest calibre.

Those who are responsible for making disclosures of executive remuneration, including board members, executives and dedicated employee specialists, should be trained in remuneration principles and practice, in order for them to understand and act effectively in the highly technical field of executive remuneration. It is necessary for these members to appreciate the underlying rationale for disclosure of executive remuneration, and to focus their disclosures on the achievement of those aims, rather than to prepare disclosures which blindly follow the way in which disclosures were done in the past, or by other organisations or jurisdictions. The environment and needs within which the organisation operates may require annual adjustments to companies' disclosure strategies.

In an environment which is characterised by a strong propensity to merely comply with the minimum disclosure requirements set in terms of regulatory codes, such as is the case amongst South African listed companies, it is essential for those regulatory prescripts to be as comprehensive and compelling as possible to ensure that the ultimate aims of disclosure as a corporate governance control measure is satisfied. In this regard, the South African disclosure requirements fall far short from providing stakeholders with both monitoring information and information symmetry to make informed decisions on their investments in the company. A continued focus on developing more governance control measures which may not be universally applicable will remain less than effective. Instead, addressing the causes of governance

failures rather than symptoms thereof, will improve the overall effectiveness of the governance system. In such a framework, tailored control measures could be implemented to address the specific needs of the company.

Although the shift in focus of King III from a “comply or explain” regime to one of “apply or explain” is a step in the right direction, it is questionable whether this in itself will be sufficient to curb abuses of power by executives. An approach in terms of which companies are required to “apply and explain” the fundamental corporate governance principles set out in the King III Report would have been preferable to an approach based on an “apply or explain” principle, in that an “apply and explain” approach would not only confirm to stakeholders of the organisation that the stated principles have been complied with, but also how and why those principles have been applied in the organisation. This would undoubtedly lead to better informed stakeholders.

12.7 Future research

The fields of executive remuneration and corporate governance are rich in potential future research opportunities, in that both constitute social disciplines that are closer to an art than to a science. Commentators, companies and consultants alike are continuously searching for a better way of doing things. For the same reason the subject continues to provide a rich field for future research on almost any element thereof.

Some of the current topics that could provide both research stimulation and academic value might be:

- Comparing how disclosure practices amongst South African listed companies changes, if at all, as a result of the promulgation of the new Companies Act in 2011, and the implementation of the King III Report in March 2010;
- Linking performance and reward, and especially so in relation to executive remuneration;
- The impact of training in remuneration principles and practice on effective Board and Remuneration Committee members;
- Evaluating how economic cycles impact on executive remuneration, and comparing executive performance to reward during the same cycle periods;
- The link between executive remuneration packages and the tenure of those executives; and
- Comparing disclosures amongst JSE main board listed and AltX listed companies.

REFERENCES

- Ablen, D. 2003. *Remunerating "fairly and responsibly": The "Principles of good corporate governance and best practice recommendations" of the ASX Corporate Governance Council* [online]. Available from: <<http://www.austlii.edu.au/au/journals/SydLRev/2003/25>> [Accessed 16 May 2007]
- Aboody, D. and Kasznik, R. 2000. 'CEO stock option awards and corporate voluntary disclosures', *Journal of Accounting and Economics*, 129: 73.
- Abor, J. and Adjasi, C.K.D. 2007. 'Corporate governance and the small and medium enterprises sector: theory and implications', *Corporate Governance*, 7 (2): 111-122.
- Abowd, J. and Kaplan, D.S. 1999. 'Executive compensation: Six questions that need answering', *Journal of Economics Perspective*, 13 (4): 145-168.
- Aggarwal, R. and Samwick, A. 1999. 'Executive compensation, strategic competition and relative performance evaluation: Theory and evidence', *Journal of Finance*, 54.
- Allcock, D. and Pass, C. 2006. 'Executive incentive pay strategies in entrepreneurial UK initial public offering companies: an empirical study', *Corporate Governance*, 6 (2): 148-161.
- Allens Arthur Robinson. 2007. *Remuneration* [online]. Available from <<http://www.aar.com.au/corpgov.iss/rem/htm>> [Accessed 16 May 2007]
- Allio, R.J. 2003. 'Russell L Ackoff, iconoclastic management authority, advocates a "systemic" approach to innovation', *Strategy and leadership*, 31(3): 19-26.
- Australian Council of Trade Unions. 2003. *Corporate governance background paper* [online]. Available from <<http://www.actu.asn.au/Archive/ACTUCongress/Papers/CorporateGovernance>> [Accessed 16 May 2007]
- Banker, R.D., Potter, G. and Srinivasan, D. 2000. 'An empirical investigation of an incentive plan that includes non financial performance measures', *The Accounting Review*, 75 (1): 65-92.
- Barris, L. 1992. 'The over compensation problem: A collective approach to controlling executive pay', *Indiana Law Journal*, 68: 59.
- Bebchuk, L. and Friend, J. 2004. *Pay without performance: The unfulfilled promise of executive compensation*. Harvard: Harvard University Press
- Bebchuk, L.A., Friend, J.M. & Walker, D.I. 2002. 'Managerial power and rent extraction in the design of executive compensation', *University of Chicago Law Review*, 751.

- Becht, M., Bolton, P. & Röell, A. 2002. 'Corporate governance and control', *ECGI Finance Working Paper*, 2: 46.
- Bender, R. and Porter, B. 2001. 'A theoretical framework to explain directors' remuneration', British Accounting Association Annual Conference 26-28 March, Nottingham, 1-36.
- Bender, R. and Porter, B. 2001. *A new theoretical framework to understand executive directors remuneration*, British Academy of Management Conference, Cardiff, 5-7 September. 2001.
- Berglof, E. and Pajuste, A. 2005. 'What do firms disclose and why? Enforcing corporate governance and transparency in Central and Eastern Europe', *Oxford Review of Economic Policy*, 121 (2): 155-163.
- Berle, A.A. and Means, G.C. 1932. *The Modern Corporation and Private Property*. New York: Commerce Clearing House.
- Bertrand, M. and Mullainathan, S. 2000. 'Agents with and without principals', *American Economics Review*, 203.
- Bertrand, M. and Mullainathan, S. 2000. 'Do CEO's set their own pay? The ones without principals do', *NBER Working Paper*, 7604: 9.
- Bhasa, M.P. 2004. 'Global corporate governance: debates and challenges', *Corporate Governance*, 4 (2): 5-17.
- Black, B.S. 1992. 'Agents watching agents: the promise of institutional investor voice', *UCLA Law Review*, 39: 811-94.
- Black, B.S. 1998. 'Shareholder activism and corporate governance in the United States'. In: Newman, P. ed. *The New Palgrave Dictionary of Economics and the Law*. London: Macmillan.
- Black, B. and Coffee, J. 1994. 'Hail Britannia? Institutional investor behaviour under limited regulation', *Michigan Law Review*, 92: 1999-2088.
- Blair, M. 1992. 'Australia's continuous disclosure regime: Proposals for change', *Australian Journal of Corporate Law*, 2: 54.
- Blair, M.M. 1995. 'Ownership and Control: Rethinking corporate governance for the 21st century', *Corporate Governance*, 12.
- Blair, M. and Ramsay, I.M. 1998. 'Mandatory corporate disclosure rules and securities regulation'. In: Gordon, J. and Walker, A. eds. 1998. *Securities Regulation in Australia and New Zealand*. Auckland: OUP.
- Bradley, M., Schipani, C., Sundaram, A. & Walsh, J. 1999. 'The purposes and accountability of the corporation in contemporary society: Corporate governance at a crossroads', *L & CP*, 62: 9.

- Brenner, S. and Cochran, P. 1991. *The stakeholder theory of the firm: implications for business and social theory and research*. IABS Proceedings, 449.
- Brooks, A., Chalmers, K., Oliver, J., & Veljanovski, A. 1999. 'Issues associated with Chief Executive Officer remuneration: Shareholder perspectives', *Company and Securities Law Journal*, 17: 360.
- Bryman, A. 2004. 'Qualitative research on leadership: A critical but appreciative review', *The Leadership Quarterly*, 15: 729 – 769.
- Bujaki, M. and McConomy, B. 2002. 'Corporate governance: factors influencing disclosure by publicly traded Canadian firms', *Canadian Accounting Perspectives*, 1 (2): 105-39.
- Bury, S. and Leblanc, R. 2007. 'Corporate governance research on the free web: a selected annotated guide', *Reference Service Review*, 35 (3): 497-514.
- Bushman, R.M., Indejejian, R.J. & Smith, A. 1996. 'CEO compensation: the role of individual performance evaluation', *Journal of Accounting and Economics*, 21: 161-193.
- Bussin, M. 2007. *Remuneration committee dilemmas* [online]. Available from <<http://www.21century.co.za/docs/remuneration>> [Accessed 25 September 2007]
- Bussin, M. and Fletcher, S. 2007. *How to set CEO and Executive pay* [online]. Available from <<http://www.21century.co.za/docs/CEO-pay.doc>> [Accessed 25 September 2007]
- Byrne, J.A. 2002. 'How to fix corporate governance', *Business Week*. 6 May. 68.
- Canyon, M., Gregg, P. & Machin, S. 1995. 'Taking care of business: Executive compensation in the United Kingdom', *The Economic Journal*, 105: 704.
- Cadbury Committee. 1992. *Report of the Committee on the Financial Aspects of Corporate governance*. London: Professional Publishing Limited.
- Canyon, M. and Murphy, K. 2000. 'The prince and the pauper: CEO pay in the United States and the United Kingdom', *Economic Journal*, 110: 640.
- Caroati, G. and Rad, A.T. 2000. 'Convergence of corporate governance systems', *Managerial Finance*, 26 (10): 66- 83.
- Chambers, A. 2005. 'Insights from practice: A teddy bear's picnic or the lion's den? Do non-executive directors add value?', *Measuring Business Excellence*, 9 (1): 23-34.
- Cheffins, B. 2003. 'Will executive pay globalise along American lines', *Corporate Governance*, 11: 8.

- Chidambaran, N.K. and Woitke, T. 1999. 'The role of negotiations in corporate governance: evidence from withdrawn shareholder-initiated proposals', *Working paper No CLB-99-012*, New York: New York University Center for Law and Business.
- Chingos, P.T. 2004. *Responsible Executive Compensation for a New Era of Accountability*. Hoboken NJ: Wiley.
- Chong, Y.Y. 2007. 'Corporate governance: risk management starts at the top', *Balance Sheet*, 12 (5): 42-47.
- Chow, C.W. and Wong-Boren, A. 1987. 'Voluntary financial disclosure by Mexican corporations', *Accounting Review*, 62 (3): 533-541.
- Clyne, S. 2002. 'Modern Corporate Governance', *AJCL*, 11: 276.
- Coffee, J. 1986. 'Shareholders versus managers: The strain in the corporate web', *Michigan Law Reports*, 85: 1.
- Coffee, J. 2001. 'The rise of dispersed ownership: The roles of Law and the State in the separation of ownership and control', *YLT*, 1: 111.
- Collier, J. 2004. 'Measuring and evaluating board performance', *Measuring Business Excellence*, 8 (3): 12-17.
- Conyon, M. and Leech, D. 1994. 'Top pay, company performance and corporate governance', *Oxford Bulletin of Economics and Statistics*, 56: 229.
- Cooper, D.R. and Schindler, P.S. 2003. *Business Research Methods*. 8th ed. New York: McGraw-Hill.
- Core, J., Holthausen, R. & Larcker, D. 1999. 'Corporate governance, chief executive officer compensation and firm performance', *Journal of Finance and Economics*, 51: 371.
- Corporate Leadership Council. 2009. *Shareholder perspectives on the new SEC executive compensation requirements* [online]. Available at <<http://www.executiveboard.com>>. [Accessed 23 April 2009].
- Corporate Leadership Council. 2009. *Executive compensation: Chief Human Resources Officers' questions and early responses for 2009* [online]. Available at <<http://www.executiveboard.com>>. [Accessed 23 April 2009].
- Corporate Leadership Council. 2009. *The SEC's proposed executive compensation disclosure requirements – early filing trends* [online]. Available at <<http://www.executiveboard.com>>. [Accessed 23 April 2009].
- Corporate Leadership Council. 2009. *The SEC's executive compensation disclosure proposals: Much is changing and some are already taking steps (big and small) towards the SEC's objective* [online]. Available at <<http://www.executiveboard.com>>. [Accessed 23 April 2009].

- Creswell, J. 1994. *Research design: Quantitative and qualitative approaches*. Thousand Oaks: Sage.
- Crotty, A. and Bonorchis, R. 2006. *Executive pay in South Africa: Who gets what and why?* Cape Town: Double Storey Books.
- Cuomo, AM. 2009. *Attorney General of the State of New York letter to the USA House of Representatives*. 10 February.
- Cyert, R.M and Hedrick, C.L. 1972. 'Theory of the firm: Past, present and future: An interpretation', *Journal of Economic Literature*, 10 (2): 398 -412.
- De Beer, B. 2005. *Remuneration governance? Do we need an upgrade?*[online] Available from <<http://www.21century.co.za>> [Accessed 25 September 2007]
- De Mott, D.A. 2000. 'Shareholder challenges to executive remuneration', *Australian Law Journal*, 74: 576.
- De Vos, A.S. 2002. *Research at grass roots for social sciences and human services professions*. Pretoria: Van Schaik.
- Donaldson, T. and Dunfee, T. 1994. 'Towards a unified conception of business ethics: integrative social contract theory', *Academy of Management Review*, 19 (2): 252
- Donham, W.B. 1922. 'Essential groundwork for a broad executive theory', *Harvard Business Review*, 1 (1): 1-10.
- Drucker, P.F. 1985. 'Entrepreneurial strategies', *California Management Review*, 27 (2): 9-25.
- Drucker, P.F. 1987. 'Management: The problems of success', *Academy of Management Executive*, 1 (1): 13-19.
- Durie, J. 2002. 'Disclosure: Business risks together rules', *Australia and Financial Review*, 8 March. 8.
- Elson, C. 1995. 'The duty of care, compensation and stock compensation', *University of Cincinnati Law Review*, 63: 649.
- Epstein, M.J and Roy, M.J. 2005. 'Evaluating and monitoring CEO performance: evidence from US compensation committee reports', *Corporate Governance*, 5 (4): 75-87.
- Fama, E.F. 1980. 'Agency problems and the theory of the firm', *Journal of Political Economy*, 88 (8): 288-307.
- Fama, E.F. and Jensen, M. 1983. 'Separation of ownership and control', *Journal of Law and Economics*, 26: 327-349.

- Ferrarini, G and Moloney, N. 2004. 'Executive remuneration and corporate governance in the EU: Convergence, divergence and reform perspectives', *ECFR*, 1: 251 – 339.
- Ferrarini, G and Moloney, N. 2005. 'Executive remuneration in the EU: The context for reform'. *Oxford Review of Economic Policy*, 121 (2): 304-323.
- Ferrarini, G., Moloney, N. & Vespro, C. 2003. *Executive remuneration in the EU: Comparative Law and practice* [online]. Available from <<http://www.ssrn.com>> [Accessed 26 May 2007]
- Finch, N. 2006. *The practice of director and executive remuneration disclosure by Australian firms* [online]. Available from <<http://www.ssrn.com>> [Accessed 16 May 2007]
- Fox, M. 2000. 'Required disclosure and corporate governance', *L & CP*, 62: 113.
- Gadfly, A. and Smacker, P. 2010. *Tincture: Passing the buck and bucking the system*. Groenkloof: Tincture Publications.
- Garen, J.E. 1994. 'Executive compensation and principal-agent theory', *Journal of Political Economy*, 102: 1175 – 1199.
- Gibson, J.W., Hodgetts, R.M. & Herrera, J.M. 1999. 'Management history gurus of the 1990's: Their lives, their contributions', *Journal of Management History*, 5 (6): 380-397.
- Gill, J. and Johnson, P. 1997. *Research methods for managers*. London: Paul Chapman.
- Gillan, S.L. and Starks, L.T. 1998. 'A survey of shareholder activism: motivation and empirical evidence', *Contemporary Finance Digest*, 2 (3): 10-34.
- Gordon, J. 2002. 'What Enron means for the management and control of the modern business corporation: Some initial reflections', *Columbia Law School, Centre and Economics*, Working Paper No 203.
- Goold, M. 1996. 'Design, learning and planning: A further observation on the design school debate', *California Management Review*, 38 (4): 94-95.
- Grant, G. 2003. 'The evolution of corporate governance and its impact on modern corporate America', *Management Decision*, 41 (9): 923-934.
- Gregoriou, G.N. and Rouah, F. 2003. 'An examination of CEO compensation of US banks and thrifts using non-traditional performance measures: 1997-2001', *Journal of Financial Services Marketing*, 7 (3): 246-257.
- Greiner, L.E. 1998. 'Evolution and revolution as organisations grow', *Harvard Business Review*, 76 (3): 55-67.

- Grint, K. 1997. *Fuzzy Management: Contemporary ideas and practices at work*. Oxford: Oxford University Press.
- Gugler, K., Mueller, D.C. & Burcin, Y.B. 2003. 'The impact of corporate governance on investment returns in developed and developing countries', *Economic Journal*, 113 (491): 511-539.
- Handy, C. 2002. 'What's a business for?', *Harvard Business Review*, 80 (12): 49-55.
- Harwood, T.G. & Garry, T. 2003: 'An overview of Content Analysis', *The Marketing Review*, 3: 479 – 498.
- Hawley, J.P. and Williams, A.T. 2000. *The rise of Fiduciary Capitalism: How Institutional Investors Can Make Corporate America More Democratic*. Philadelphia: University of Pennsylvania Press.
- Healy, P.M. and Palepu, M. 2001. 'Information asymmetry, corporate disclosure and the capital markets: A review of the empirical disclosure literature', *Journal of Accounting and Economics*, 31: 1.
- Herawaty, M and Hoque, Z. 2007. 'Disclosure in the annual reports of Australian government departments', *Journal of Accounting and Organizational Change*, 13 (2): 147-168.
- Hewitt & Associates. 2003. *Survey findings: Corporate and executive remuneration: A European perspective*. Lincolnshire, IL.
- Hill, J. 1996. 'What reward have ye? Disclosure of director and executive remuneration in Australia', *Australian Investment Managers' Association*, Research Paper No. 1:96.
- Hill, J. 1996. 'Remuneration disclosure in Australia', *Australia Investment Managers' Association*, Research paper No.1/1996.
- Hill, J. 2000. 'Public beginnings, private ends – should corporate law privilege the interests of shareholders?'. In: Macmillan, M. *International Corporate Law Annual*, 1: 17
- Hill, J. and Yablon, C . 2000. 'Corporate governance and executive remuneration: Rediscovering managerial positional conflict', *New South Wales Law Review*, 25: 294.
- Hill, J. and Yablon, C.M. 2002. 'Corporate governance and executive remuneration: Rediscovering managerial positional conflict', *University of New South Wales Law Journal*, 25: 294 – 334.
- Hoinville, G. and Jowell, R. 1985. *Survey Research Practice*. Aldershot: Gower Publishing Limited.

- Holburn, E. 2007. *Executive pay – the “stock” or “share” option* [online]. Available from <<http://www.classalinfo.com.au/knowledge/executivePay.htm>> [Accessed 16 May 2007]
- Holstrom, B. 1974. 'Moral hazard and observability', *Bell Journal of Economics*, 10: 74.
- Holstrom, B. and Kaplan, S. 2002. 'The state of US Corporate Governance: What's right and what's wrong', *NBER Working Paper*, No. 9613.
- Huczynski, A.A. 1992. 'Management guru ideas and the 12 secrets of their success', *Leadership and Organisation Development Journal*, 13 (5): 15-20.
- Illbury, C. And Sunter, C. 2001. *The mind of a Fox*. Cape Town: Human & Rousseau/Tafelberg.
- Illbury, C. And Sunter, C. 2007. *Socrates and the Fox*. Cape Town: Human & Rousseau/Tafelberg.
- International Corporate Governance Network. 1999. *Statement on global corporate governance principles* [online]. Available from <<http://www.ecgi.org/codes/documents/icgn-principles.pdf>> [Accessed 07 August 2007]
- International Corporate Governance Network. 2003. *Summary of the report on Executive Remuneration: Best Practises for Executive and Director Remuneration* [online]. Available from <http://www.icgn.org/documents/best_practice_bullets> [Accessed 07 August 2007]
- International Corporate Governance Network Sub-Committee on Executive Remuneration. 2002. *Executive Remuneration-The Caucus Race* [online]. Available from <<http://www.icgn.org.documents/ICGNExecRem.pdf>> [Accessed 07 August 2007]
- Institute of Directors. 2005. *The Handbook of International Corporate Governance: A definitive guide*. London: Kogan Page.
- Institutional Shareholders Committee. 2002. *The Responsibilities of Institutional Investors – A Statement of Best Practice*. London: ABI.
- Ittner, C.D. and Larcker, D.F. 1998. 'Innovations in performance measurement: trends and research implication', *Journal of Management Accounting Research*, 10: 205-238.
- Jensen, M.C. and Meckling, W.H. 1976. 'Theory of the firm: capital managerial behaviour, agency costs and ownership structure', *Journal of Financial Economics*, 3 (4): 305-360.
- Jensen, M.C. and Murphy, K.J. 1990. 'CEO incentives – Its not how much you pay, but how', *Harvard Business Review*, 138.

- Jensen, M.C. and Murphy, K.J. 2004. 'Remuneration: Where we've been, How we got there, what are the problems, and how to fix them', *European Corporate Governance Institute*. Working Paper No. 44/2004.
- Judin, M. 2007. 'New King needed for SA's journey', *Business Day*. 29 January. 9.
- Kakabadse, N.K, Kakabadse, A. and Kouzmin, A. 2004. 'Director's remuneration: The need for a geo-political perspective', *Personnel Review*, 33 (5): 561-582.
- Kaplan, R.S. and Norton, D.P. 1996. *The Balanced Scorecard*. Cambridge: Harvard Business School Press.
- Karpoff, J. 2001. 'The impact of shareholder activism on target companies: a survey of empirical findings', *University of Washington*. Working Paper No. 1.
- Karpoff, J.M., Malatesta, P.H. & Walking, R.A. 1996. 'Corporate governance and shareholder initiatives: empirical evidence', *Journal of Financial Economics*, 42 (3): 365-395.
- Keller, G. and Warrack, B. 1997. *Statistics for management and economics*. Pacific Grove: Brookes/Cole.
- Kim, D.H. and Senge, P.M. 1994. 'Putting systems thinking into practice', *System dynamics review*, 10 (2/3): 277-290.
- King Committee on Corporate Governance. 1994. *The King Report on Corporate Governance*. Johannesburg: Institute of Directors of Southern Africa.
- King Committee on Corporate Governance. 2002. *The King Report on Corporate Governance for South Africa*. Johannesburg: Institute of Directors of Southern Africa.
- King Committee on Corporate Governance. 2009. *Draft Code of Governance: Principles for South Africa*. Johannesburg: Institute of Directors of Southern Africa.
- King Committee on Corporate Governance. 2009. *Code of Governance for South Africa*. Johannesburg: Institute of Directors of Southern Africa.
- Kolbe, R.H. & Burnett, M.S. 1991. 'Content-Analysis Research: An Examination of Applications with Directives for Improving Research Reliability and Objectivity', *Journal of Consumer Research*, 18: 243 – 250.
- Koeck, W.J. 1995. 'Continuous disclosure', *C+SLJ*, 13: 485.
- Kraakman, R. 2004. 'Disclosure and Corporate Governance: An overview essay'. In: Ferrarini, G., Hapt, K., Winter, J. & Wyneersch, E. eds. *Reforming Company and take over law in Europe*. Oxford: Oxford University Press.

- Krugman, P. 2006. *The great wealth transfer* [online]. Available from <<http://www.rollingstone.com/politics/story/12699486>> [Accessed 16 May 2007]
- La Porta, R., Lopez-de-Silanes, E. & Shleifer, A 1999. 'Corporate ownership around the world', *Journal of Finance*, 54 (2): 471-517.
- Lazonick, W. and O' Sullivan, M. 2000. 'Maximizing shareholder value:" A new ideology for corporate governance', *Economy and Society*, 29 (1): 13-35.
- Little, J. 1991. 'The policy underlying financial disclosure by corporations and its effect upon legal liability', *Australian Journal of Corporate Law*, 1: 97.
- Loewenstein, M. 1996. 'Reflections of executive compensation and a modest proposal for further reform', *Southern Methodist University Law Review*, 50: 201.
- Loewenstein, M. 2000. 'The conundrum of executive compensation', *Wake Forest Law Review*, 35: 1.
- Mahoney, P. 1995. 'Mandatory disclosure as a solution to agency problems', *University of Chicago Law Review*, 62: 1047.
- Main, B. and Johnston, J. 2006. Remuneration committees and corporate governance. *Accounting and Business Research*, 23: 351.
- Mardjono, A. 2005. 'A tale of corporate governance: lessons why firms fail', *Managerial Auditing Journal*, 20 (3): 272-283.
- Martin, R. and Nisar, T.M. 2007. 'Activist investment: institutional investor monitoring of portfolio companies', *Management Decision*, 45 (5): 827-840.
- McConvill, J. 2005. *Money can't buy you ... performance* [online]. Available from <<http://www.pay-without-performance.com/TheAgeAU>> [Accessed 16 May 2007]
- Mc Kinsey and Company. 2002. *Global investor opinion survey on corporate governance: key findings* [online]. Available from <www.mckinsey.com/governance> [Accessed 17 January 2008]
- McKnight, P.J. and Tomkins, C. 1999. 'Top executive pay in the United Kingdom: a corporate governance dilemma', *International Journal of Economics of Business*, 6(2): 223-243.
- Mc Taggart, J., Kontes, P.W. & Mankins, M. 1994. *The value imperative: Managing for superior shareholder returns*. New York: Free Press.
- Mechran, H. 1995. 'Executive compensation structure, ownership and firm performance', *Journal of Finance and Economics*, 38: 163.

- Meek, G.K., Roberts, C.B. & Gray, S.J. 1995. 'Factors influencing voluntary annual report disclosures by US, UK, and Continental European multinational corporations', *Journal of International Business Studies*, 26(3): 555-572.
- Miller, T.R. and Vaughan, B.J. 2001. 'Messages from the management past: Classic writers and contemporary problems', *SAM Advanced Management Journal*, 66 (1): 4-11.
- Mintzberg, H. 2001. 'Decision making: It's not what you think', *MIT Sloan Management Review*, 42 (3): 89-93.
- Mintzberg, H. 2004. 'Enough leadership', *Harvard Business Review*, 82 (11): 22.
- Mongalo, T. 2007. *The managerial employee: Implications of principles of corporate governance* [online]. Available from <<http://lexisnexis.co.za/presentations/17th/TshepoMongalo.doc>> [Accessed 16 May 2007]
- Moxey, P. 2004. 'Corporate Governance and wealth creation', *The Association of Chartered Certified Accountants*. ACCA Occasional Research Paper No. 37.
- Murphy, K. 1995. 'Politics, economics and executives pay', *University of Cincinnati Law Review*, 63: 713.
- Musson, G. 1998: 'Life Histories'. In: Symon, G. and Cassell, C. *Qualitative methods and analysis in organisational research: A practical guide*. California: Sage Publications.
- Ney, D. 2007. *Corporate governance* [online]. Available from < [http://www.willis.com/services/Corporate Governance.aspx](http://www.willis.com/services/Corporate%20Governance.aspx) > [Accessed 16 May 2007]
- Oldert, N. ed. 2008. *Profile's Stock Exchange Handbook: February – May 2008*. Pietermaritzburg: Profile Media.
- O'Reilly, C.A., Main, B.G.M. & Crystal, G.S. 1988. 'CEO salaries as tournaments and special comparisons: a tale of two theories', *Administrative Science Quarterly*, 33(3): 257-274.
- Parker, S., Peter, G.F. and Turetshy, H.F. 2002. 'Corporate governance and corporate failure: a survival analysis', *Corporate Governance*, 2(4): 12.
- Pepper, S. 2005. 'Corporate governance and executive remuneration – what is the connection?', *Euromoney*.
- Pepper, S. 2006. *Senior Executive Reward: Key models and practices*. Hampshire: Gower Publishing Limited.
- Porter, M.E., Lorsch, J.W. & Nohria, N. 2004. 'Seven surprises for new CEO's', *Harvard Business Review*, (82) (10): 62-72.

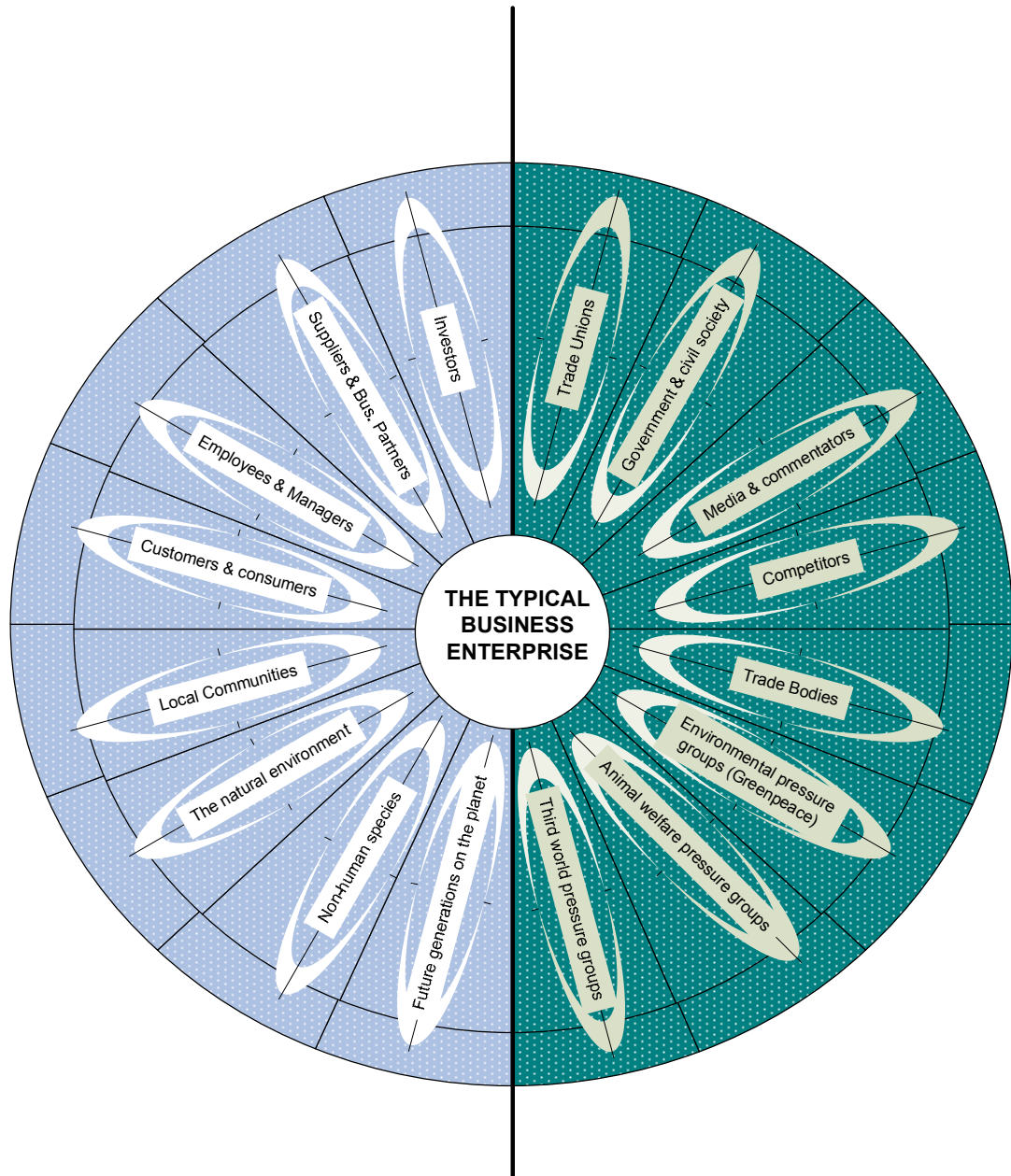
- Price Waterhouse Cooper. 2009. *Executive Directors Best Practice Report* [online]. Available at <<http://www.pwc.com/sa>> [Accessed 24 July 2009].
- Quin, P. 1999. 'The unchangeables – Director and Executive remuneration disclosure in Australia', *Australian Journal of Corporate Law*, 10: 89.
- Rahman, A.R. 2002. *Incomplete financial contracting, disclosure, corporate governance and firm value –with evidence from a moderate market for corporate control environment* [online]. Available at <<http://ssrn.com/abstract>> [Accessed 17 January 2008].
- Raimond, P. 1993. *Management Projects: Design, Research and Presentation*. London: Chapman and Hall.
- Rajgopal, S. and Shevlin, T. 2002. 'Empirical evidence on the relation between stock option compensation and risk taking', *Journal of Accounting and Economics*, 33: 1.
- Rappaport, A. 1999. 'New thinking in how to link executive pay to performance', *Harvard Business Review*, 99: 91 -101.
- Reed, D. 2002. 'Corporate governance in developing countries', *Journal of Business Ethics*, 37(3): 223-247.
- Re Australian Newsprint Mills Ltd (1988) 6 ACLC 1205
- Remenyi, D., Williams, B., Money, A. & Swartz, E. 1998. *Doing research in business and management: An introduction to process and method*. London: Sage.
- Rezaee, Z., Olibe, K.O. & Minnier, G. 2003. 'Improving corporate governance the role of audit committee disclosures', *Managerial Auditing Journal*, 18(6/7): 530 -537.
- Roberts, V., Ceron, M., Fourage, B., & Knieriem, A. 2007. *Executive compensation disclosure in Europe* [online]. Available at <<http://www.mercer.com/excremeurope>> [Accessed 17 December 2008]
- Robins, F. 2006. 'Corporate governance after Sarbanes-Oxley: an Australian perspective', *Corporate Governance*, 6 (1): 34-48.
- Roe, M. 1993. 'Some differences in corporate structure in Germany, Japan and the United States', *YLLJ*, 102: 1979.
- Roe, J.M. 2002. 'Political foundations for separating ownership from corporate control', *Columbia Law School, The Centre for Law and Economic Studies*. Working Paper No. 155.
- Rogers, W. and Gago, S. 2003. 'A model capturing ethnics and executive compensation', *Journal of Business Ethics*, 48: 189 -202.

- Romano, R. 1993. 'A cautionary note on drawing lessons from comparative corporate law', *YLT*, 102: 2021.
- Romano, R. 2001. 'Less is more: Making institutional investor activism a valuable mechanism of corporate governance', *Yale Journal of Regulation*, 18: 174.
- Romano, R. 2002. 'Less is more: making institutional investor activism a valuable mechanism of corporate governance'. In: McCahery, J. and Renneboog, L. eds. *Convergence and Diversity in Corporate Governance Regimes and Capital Markets*. Oxford: Oxford University Press.
- Romano, R. 2005. 'The Sarbanes-Oxley Act and the making of quack corporate governance', *Yale Law Review*, 114: 7.
- Ryan, R. 2009. *Preparing executive compensation disclosure* [online]. Available at <<http://www.executiveboard.com>> [Accessed 23 April 2009].
- Salamon, G.L. and Smith, E.D. 1979. 'Corporate control and managerial misrepresentation of firm performance', *Bell Journal of Economics*, 319.
- Saunders, M., Lewis, P., & Thornhill, A. 2003. *Research Methods for Business Students*. Harlow: Prentice Hall.
- Schadewitz, H.J. and Blevins, D.R. 1998. 'Major developments of interim disclosures in an emerging market', *American Business Review*, 16: 710-721.
- Senge, P.M. 2006. 'Systems Citizenship: The Leadership Mandate for this Millennium', *Reflections*, 7(3): 1-8.
- Senge, P.M. 2006. *The Fifth Discipline: The art and practice of the learning organisation*. London: Random House.
- Sethi, S.P and Emelianova, O. 2006. 'A failed strategy of using voluntary codes of conduct by the global mining industry', *Corporate governance*, 6 (3): 226-238.
- Sheffield Accord. 2007. *Disclosure of executive pay. No place to hide?* [online]. Available from <<http://www.sheffieldaccord.com/articles/mervyn.html>> [Accessed 16 May 2007]
- Shim, D.S. 2006. 'Governance in the markets: Malaysian perspective', *Journal of Financial Crime*, 13 (3): 300-322.
- Shleifer, A. and Vishny, R. 1997. 'A survey of corporate governance', *Journal of Finance*, 52(2): 737-783.
- Shorten, R.L. 1992. 'An overview of the revolt against executive compensation', *Rutgers Law Review*, 45: 121.

- Siciliano, J.I. 2002. 'Governance and strategy implementation: expanding the board's involvement', *Business Horizons*, November/December: 33-37.
- Slane, B.H. 1997. 'Mandatory disclosure of executive remuneration'. Report by the Privacy Commissioner to the Minister of Justice (New Zealand). Unpublished.
- Smith, A. 2000. *The theory of moral sentiments*. New York: Prometheus Books.
- Sonnenfeld, J.A. 2004. 'Good governance and the misleading myths of bad metrics', *The Academy of Management Executive*, 18(1): 108-113.
- Spanos, L.J. 2005. 'Corporate governance in Greece: developments and policy implications', *Corporate Governance*, 5 (1): 15-30.
- Stabile, S. 2000. 'Viewing corporate executive compensation through a partnership lens: A tool to focus reform', *Wake Forest Law Review*, 35: 153.
- Styan, J.B. 2009. 'King III lui nuwe era in vir maatskappye', *SakeBeeld*. 6 June. 13.
- Sutton, R.I. 2004. 'Prospecting for valuable evidence: why scholarly research can be goldmine for managers', *Strategy and Leadership*, 32 (1): 27-33.
- Szondy, G. 2003. 'Executive remuneration and disclosure: The hot issues ... and the corporate impact', *Briefings*, 2.
- Stiglitz, J.E. 2002. *Globalization and Its Discontents*. New York: W.W. Norton & Company.
- Stiglitz, J.E. 2002. 'There is no invisible hand', *The Guardian Comment*. 20 December.
- Stiglitz, J.E. 2006. *Making Globalization Work*. New York: Penguin Books.
- Stiglitz, J.E. 2008. *The fruit of hypocrisy* [online]. Available from <http://guardian.co.uk/commentsisfree/2008/sep/16/economics/wallstreet> [Accessed 14 October 2009]
- Taylor, D.W. 2000. 'Facts, myths and monsters: understanding the principles of good governance', *The International Journal of Public Sector Management*, 13(2): 108 – 124.
- Thomas, R.S. and Martin, K.J. 2001. 'Litigating challenges to executive pay: An exercise in futility', *Washington University Law Quarterly*, 1(79): 569-580.
- Treanor, J. 2007. *Summit on corporate governance standards for LSE's foreign firms* [online]. Available from <<http://business.guardian.co.uk>> [Accessed 16 May 2007]
- Tricker, R.I. 1984. *Corporate governance*. Aldershot: Gower Publishing

- Tsamenyi, M., Enninful-Adu, E. & Onumah, J. 2007. 'Disclosure and corporate governance in developing countries: evidence from Ghana', *Managerial Auditing Journal*, 22 (3): 319-334.
- Turnbull, S. 1997. 'Corporate governance: its scope, concerns and theories', *Corporate Governance: Scholarly Research and Theories Papers*, 5(4): 180.
- Uren, D. 2003. *The transparent corporation: Managing demands for disclosure*. Sydney: Allen and Unwin.
- Van Wyk, A.H. 2009. 'Sal King III 'n invloed hê op jou lewe?', *SakeBeeld*. 8 September.
- Vinten, G. 2002. 'The corporate governance lessons of Enron', *Corporate Governance*, 2(4): 4-9.
- Visser, A. 2009. 'King III 'n streng dieet vir sakegesondheid', *SakeBeeld*. 27 February. 24.
- Wheatley, M.J. 2010. *Leadership and the new science: Discovering order in a chaotic world*. San Fransisco: Berrett-Koehler Publishers.
- Weiss, E. 1979. 'Disclosure and corporate accountability', *Business Law*, 34: 575.
- Wheeler, D. and Sillanpaa, M. 1997. *The stakeholder corporation*. London: Pitman.
- WorldatWork. 2007. *The WorldatWork Handbook of Compensation, Benefits and Total Rewards*. New York: John Wiley & Sons.
- Yablon, C.M. 1992. 'Overcompensation: The corporate lawyer and executive pay', *Columbia Law Review*, 92: 1867.
- Yablon, C.M. and Hill, J. 2000. 'Timing Corporate disclosures to maximise performance – based remuneration: A case of misaligned incentives?', *Wake Forest Law Review*, 35: 83.
- Yeoh, P. 2007. 'Corporate governance models: Is there a right one for transition economics in Central and Eastern Europe?', *Managerial Law*, 49 (3): 57-75.

ANNEXURE A: STAKEHOLDER FRAMEWORK



(Source: Wheeler & Silanpaa, 1997)

ANNEXURE C: CORPORATE GOVERNANCE REPORTS OF DIFFERENT COUNTRIES

Report	Country	Description	Nature
Treadway Commission, 1987	USA	Importance of audit committee mentioned. Designed best practices for audit committees. Emphasized that audit committees are primarily meant to check corporate frauds.	Compulsory formation of ACs necessary to be listed on NYSE, AMEX and NASDAQ exchanges.
Cadbury Committee, 1992	UK	Role of board in governance system emphasized. Best practises for board composition and functioning developed. Audit committee, remuneration committee and nomination committee to be formed by corporations.	Voluntary adoption by LSE.
Hilmer Report, 1993	Australia	Best practises code for the composition and functioning of boards prepared.	Voluntary compliance.
Dey Report, 1994	Canada	Board responsibility and board composition were the primary thrust, a total of 14 principles prepared by the Toronto Stock Exchange Committee on Corporate Governance.	Voluntary compliance.
Vienot Report, 1995	France	Focus on board responsibilities, formation of audit, nominating and compensation committees.	Voluntary compliance.
Greenbury Report, 1995	UK	Director compensation standards set and disclosure of remuneration emphasized.	Voluntary compliance.
Peters Report, 1997	Netherlands	Code prepared by the Amsterdam Stock Exchange on the composition and functioning of two-tier boards	Voluntary compliance.
Hampel Report, 1998	UK	Disclosure and quality of board governance stressed upon.	Comply or explain.
Bajaj Committee Report, 1999	India	Prepared by the committee set up Confederation of Indian Industries. Board structure addressed and accountability to investors emphasized.	Voluntary compliance.
Birla Committee Report, 2000	India	Prepared by the committee set up by SEBI. Clearly influenced by Cadbury report and is a rehash of all the above reports.	Mandatory for listing on BSE.
King II Report, 2002	South Africa	Focus on inclusive governance approach, and importance of non-financial reporting.	Voluntary compliance.
King III Report, 2002	South Africa	Build on inclusive approach to governance by outlining principles of good governance that ought to be applied	Voluntary compliance.

(Adapted from Bhasa, 2004)

ANNEXURE D: GLOBAL REPORTING INITIATIVE GUIDELINES

Main category	Sub-Category	Issues
Economic	Direct economic impacts	Customers, Suppliers, Employees, Providers of capital, Public sector
Social	Labour practices and decent work	Employment, Labour/management relations, Health and safety, Training and education, Diversity and opportunity
	Human rights	Strategy and management, Non-discrimination, Freedom of association and collective bargaining, Child labour, Forced and compulsory labour, Disciplinary practices, Security practices, Indigenous rights.
	Society	Community, Bribery and corruption, Political contributions, Competition and pricing
	Product responsibility	Customer health and safety, Products and services, Advertising, Respect for privacy
Environmental	Environmental	Material, Energy, Water, biodiversity, Emissions, Effluents and waste, Suppliers, Products and services, Compliance, Transport, Overall

Source: Meek, Roberts, Gray, 1995)

ANNEXURE E: EXECUTIVE REMUNERATION THEORIES

No.	Theory	Proponent	Explanation
1	Agency theory	Berle and Means 1932	Separation of ownership and control causes agency costs
2	Class hegemony theory	Gornez-Mejia 1994	Fellow CEO's as board members follow own interests
3	Efficiency wage theory	Prendergast, 1999	Premiums paid to CEO's to incentivize extra efforts
4	Figurehead theory	Ungston and Steers 1984	CEO's paid as leaders and figureheads rather for results.
5	Human capital theory	Agarwal 1981	Executive remuneration based knowledge and skills
6	Managerialism theory	Gornez-Mejia 1994	Managers have absolute power and control to pursue own interests
7	Marginal productivity theory	Gornez-Mejia 1994	CEO should receive compensation based on value added
8	Prospect theory	Wiseman and Gornez Mejia 1998	CEO's paid for risk aversion
9	Social comparison theory	O'Reilly, Main and Crystal, 1998	Board members' pay informs exec pay
10	Tournament theory	Lazear and Rosen 1981	Executive remuneration sets incentives for direct subordinates

ANNEXURE F: VOLUNTARY DISCLOSURE CHECKLIST

Strategic information

1. General Corporate Information
 1. Brief history of company
 2. Organizational structure
2. Corporate Strategy
 - 3 Statement of strategy and objectives - general
 - 4 Statement of strategy and objectives - financial
 - 5 Statement of strategy and objectives - marketing
 - 6 Statement of strategy and objectives - social
 - 7 Impact of strategy on current results
 - 8 Impact of strategy on future results
3. Acquisitions and Disposals
 - 9 Reasons for the acquisitions
 - 10 Reasons for the disposals
4. Research and Development
 - 11 Corporate policy on research and development
 - 12 Location of research and development activities
 - 13 Number employed in research and development
5. Future Prospects
 - 14 Qualitative forecast of sales
 - 15 Quantitative forecast of sales
 - 16 Qualitative forecast of profits
 - 17 Quantitative forecast of profits
 - 18 Qualitative forecast of cash flows
 - 19 Quantitative forecast of cash flows
 - 20 Assumptions underlying the forecasts
 - 21 Current period trading results - qualitative
 - 22 Current period trading results - quantitative
 - 23 Order book or backlog information

Nonfinancial information

6. Information about Directors
 - 24 Age of the directors
 - 25 Educational qualifications (academic and professional)
 - 26 Commercial experience of the executive directors
 - 27 Other directorships held by executive directors
7. Employee Information
 - 28 Geographical distribution of employees
 - 29 Line-of-business distribution of employees
 - 30 Categories of employees by gender
 - 31 Identification of senior management and their functions
 - 32 Number of employees for two or more years
 - 33 Reasons for changes in employee numbers or categories
 - 34 Amount spent on training
 - 35 Nature of training
 - 36 Categories of employees trained
 - 37 Number of employees trained
 - 38 Data on accidents
 - 40 Redundancy information (general)
 - 41 Equal opportunity policy statement

- 42 Recruitment problems and related policy
8. Social Policy and Value Added Information
- 43 Safety of products (general)
 - 44 Environmental protection programs - quantitative
 - 45 Charitable donations (amount)
 - 46 Community programs (general)
 - 47 Value added statement
 - 48 Value added data
 - 49 Value added ratios
 - 50 Qualitative value added information
- Financial information**
9. Segmental Information
- 51 Geographical capital expenditure - quantitative
 - 52 Geographical production - quantitative
 - 53 Line-of-business production - quantitative
 - 54 Competitor analysis - qualitative
 - 55 Competitor analysis - quantitative
 - 56 Market share analysis - qualitative
 - 57 Market share analysis – quantitative
10. Financial Review
- 58 Profitability ratios
 - 59 Cash flow ratios
 - 60 Liquidity ratios
 - 61 Gearing ratios
 - 62 Disclosure of intangible valuations (except goodwill and brands)
 - 63 Dividend payout policy
 - 64 Financial history or summary - six or more years
 - 65 Restatement of financial information to non-U.S/U.K. GAAP
 - 66 Off balance sheet financing information
 - 67 Advertising information - qualitative
 - 68 Advertising expenditure - quantitative
 - 69 Effects of inflation on future operations - qualitative
 - 70 Effects of inflation on results – qualitative
 - 71 Effects of inflation on results - quantitative
 - 72 Effects of inflation on assets - qualitative
 - 73 Effects of inflation on assets - quantitative
 - 74 Effects of interest rates on results
 - 75 Effects of interest rates on future operations
11. Foreign Currency Information
- 76 Effects of foreign currency fluctuations on future operations – qualitative
 - 77 Effects of foreign currency fluctuations on current results – qualitative
 - 78 Major exchange rates used in the accounts
 - 79 Long-term debt by currency
 - 80 Short-term debt by currency
 - 81 Foreign currency exposure management description
12. Stock Price Information
- 82 Market capitalization at year end
 - 83 Market capitalization trend
 - 84 Size of shareholdings
 - 85 Type of shareholder

ANNEXURE G: CURRENT DISCLOSURE PRACTICES ACROSS EUROPE

	Denmark	Finland	France	Germany	Ireland	Italy	Netherlands	Norway	Portugal	Spain	Sweden	Switzerland	UK
Executive compensation disclosed in the annual reports	√	√	√	√	√	√	√	√	√	√	√	√	√
Executive directors covered	All directors	All directors	Board members	Board members	Board members	Board members	Board members	Board members	Board members	Board members	Board members	Board members	All directors
Executive remuneration only provided as an aggregate amount	√	√							√	√	√	√	
Individualised executive compensation provided for each executive	CEO only	CEO only	√	√	√	√	√	√			CEO only	Highest paid executives	√
Elements of compensation disclosed in tabular format													
Salary			√	√	√	√	√	√		√	√	√	√
Fees			√	√	√	√	√	√		√	√	√	√
Bonus			√	√	√	√	√	√		√	√	√	√
Benefits			√		√	√	√	√		√	√	√	√
Pension			√	√	√		√	√		√	√		√
Long term incentives (LTI)			√	√	√	√	√	√		√	√	√	√
Other	Total		Severance		Severance		Severance	Severance, LT costs		Severance, small perks		Change of control	Performance graph
Detailed description of compensation element included													
Executive compensation philosophy		√	√	(Y)	√	√	√			(Y)	√	√	√
Overview of bonus		√	√	(Y)	√	√	√	√		(Y)	√	√	√
Overview of LTI plans		√	√	(Y)	√	√	√	√		(Y)	√	√	√
Description of pension		√	√	(Y)	√			√		(Y)	√	√	√
Any payouts to departing executives			√	(Y)	√		√	√			√	√	√
Any peer groups used			√		√								√
Disclosure of performance required								√	√		√		√
Shareholders vote on the remuneration report	√			√					√	√	√		√

(Roberts, et al, 2007)

(Y) – Typically not provided for in annual reports

Note 1: Disclosure rules in each country typically apply to companies listed on the country's stock market. There are less onerous disclosure requirements for private companies.

Note 2: Typically the shareholders' vote on the remuneration report is only advisory. There is usually a vote required for changes to equity-based compensation.

ANNEXURE H: COMPARATIVE GOVERNANCE MEASURES IN EU COUNTRIES

	France	Germany	Switzerland	UK	USA
Is individual disclosure of directors' remuneration required?	Yes	Recommended	Highest-paid director and aggregate of all directors' remuneration only	Yes	Yes
Are shareholders entitled to vote on directors' remuneration?	Yes, in respect of the aggregate amount only	Yes, for the supervisory board and in respect of the aggregate amount only	No	Yes, but the effect of the vote is advisory only	No
Is shareholders' approval required for stock-based incentive plans?	Yes	No, approval is required for the issuing of shares generally, not specific plans	No, approval is required for the issuing of shares generally, not specific plans	Yes	Yes
Must a remuneration committee comprised of independent directors approve executive remuneration proposals?	Recommended	Supervisory board can delegate responsibilities to a compensation committee	Recommended	Recommended-comply or explain	Recommended
Is it normal to have single or two-tier board?	Single-tier, occasionally two-tier	Two-tier, required by law	Two-tier boards required by Swiss banking law for all banks. Many other Swiss companies have a board of directors and separate executive board. The CEO is often a member of both.	Single-tier	Single-tier
Is separation of roles between the Chairperson and CEO required?	No	Yes	Required for banks. Otherwise not required, but increasingly common in practice	Recommended-comply or explain	No, though lead non-executive directors are increasingly common
What is the recommended maximum length of directors' contracts?	4 years recommended; 6 year limit required by law	Appointments to supervisory board are for a maximum of 5 years	4 years recommended	1 year recommended	None, though the terms and conditions of the employment of the top five named executives must be disclosed annually.

(Source: Pepper, 2006)

ANNEXURE I: PRELIMINARY RESEARCH SAMPLE

No	Industry	Sector	Total	
			Sector	Industry
1	Oil and gas			2
		Oil and gas	2	
2	Raw materials			86
		General mining	17	
		Forestry and paper	4	
		Chemicals	5	
		Diamonds and semi precious stones	23	
		Gold mining	15	
		Industry metals	9	
		Platinum	10	
		Coal	3	
3	Industrial			56
		General industrial	10	
		Electric and electronic	12	
		Industrial engineering	7	
		Industrial transport	7	
		Construction and materials	20	
		Support services	16	
4	Consumer goods			32
		Liquor	4	
		Household goods	1	
		Cars and parts	4	
		Leisure goods	2	
		Personal goods	5	
		Food processing	16	
5	Health care			4
		Pharmaceutical	2	
		Health services	2	
6	Consumer services			44
		General retail	19	
		Media	8	
		Travel and leisure	13	
		Food and medicine retail	4	
7	Telecommunications			4
		Mobile	3	
		Fixed line	1	
8	Financial			69
		General financial	24	
		Banks	8	
		Investment	13	
		Property	34	
		Life assurance	6	
		Insurance	4	
9	Technology			18
		Software	16	
		Hardware	2	
10	Development capital			6
		General	6	
11	Risk capital			9
		General	9	
	Totals		330	330

(Adapted from Oldert, 2008)

ANNEXURE J: ANNUAL REPORT DISCLOSURE COMPLIANCE INDEX

Minimum disclosure requirements		Points	Total
General	Annual Report published	1	
	Distinguish between Executive and Non-Executive Directors	1	
	Disclosure of aggregate and individualized emoluments paid to directors	1	
Specific disclosures	Fees for services as a director	1	
	Other fees paid for direct and indirect services rendered	1	
	Basic salary	1	
	Bonuses and performance-related payments	1	
	Sums paid by way of expense allowance	1	
	Any other material benefits received	1	
	Contributions paid under any pension scheme	1	
	Any commission, gain or profit-sharing arrangements	1	
	Share options	Opening balance	1
		Number of share options awarded and their strike prices	1
		Strike dates	1
		Number of share options exercised	1
		Closing balance of share options	1
	Shares issued and allotted	Number issued	1
		Price of issue	1
		Release periods applicable	1
	Fees paid or accrued as payable to a third party in lieu of directors' fees		1
Compliance with minimum disclosure requirements		20	
Additional disclosure items			
1	Annual report on website		
2	Performance / reward criteria published		
3	Remuneration policy published		
4	Aggregate director's interest in share capital published		
5	Separate chapter containing all executive remuneration disclosures		

KEY

Category	Description	Points
A	Disclose less than minimum requirements	< 20
B	Disclose minimum requirements	20
C	Disclose more than minimum requirements	20 + some additional items

ANNEXURE K: INTERVIEW SCHEDULE

1. ADMINISTRATIVE DATA (Collected and completed before the interview)

Company	Industry	Sector	Disclosure group		
			Less	Same	More

2. GENERAL QUESTIONS

- Is there a mandated remuneration committee at your company?
- Does your company have a specified policy on disclosure of executive remuneration?
- What is the role of a company remuneration manager and/or consultant in the drafting of your company's disclosure statement?

3. TARGET QUESTIONS

- What causes corporate governance failures?
- Which of these causes are related to executive remuneration?
- Why is there a need for regulation of disclosure of executive remuneration?
- What types of disclosure should be regulated and what should not?
- If corporate governance control measures are ineffective, what would be the effect, if any, on:
 - levels of executive remuneration?
 - the process for determination of executive remuneration?
- How effective is disclosure in facilitating information symmetry between managers, investors and other stakeholders? What factors determine their effectiveness?
- What factors affect management's disclosure choices?
- Could disclosure of executive remuneration contribute to more effective corporate governance? How?
- What is the relation between disclosure, corporate governance, and executive remuneration? What role do boards and board committees play in the disclosure process?

ANNEXURE L: SAMPLE INTERVIEW SCHEDULE

Topic	Questions
Regulation of disclosure.	<ul style="list-style-type: none"> ▪ Why is there a need for regulation of disclosure in capital markets? What types of disclosures should be regulated and which should not? ▪ How effective are accounting standards in facilitating credible communication between managers and outside investors? What factors determine their effectiveness? ▪ Which mandated disclosures should be recognized directly in the financial statements and which should be included as supplemental disclosures?
Auditors/intermediaries and disclosure	<ul style="list-style-type: none"> ▪ How effective are auditors in enhancing the credibility of financial statements? What factors influence auditors' effectiveness? ▪ How effective are financial analysts as information intermediaries? What factors influence their effectiveness? ▪ How does corporate disclosure affect analyst coverage of firms?
Disclosure decisions of managers	<ul style="list-style-type: none"> ▪ What factors affect management's disclosure choices? ▪ What is the relation between disclosure, corporate governance, and management incentives? What role do boards and audit committees play in the disclosure process?
Capital market consequences of disclosure	<ul style="list-style-type: none"> ▪ How do investors respond to corporate disclosures? Are firm disclosures made outside the financial statements credible? ▪ Do investors evaluate disclosures that are included directly in the financial statements differently from those that are included as supplemental disclosures? ▪ What factors influence investors' perception of the quality of capital market disclosures across economies? ▪ How does disclosure affect resource allocation in the economy?

(Source: Healy & Palepu, 2000)

ANNEXURE M: KING II GUIDELINES FOR COMPONENTS OF REMUNERATION

As part of achieving and maintaining reasonable, acceptable levels of remuneration, the Committee is encouraged to consider the following guidelines:

- **Base fees**
 - the general level of hourly or daily rates of fees earned by directors in their professional capacities (e.g. as lawyers, accountants, executives, management consultants);
 - the hours spent in travel and preparation for meetings, as well as actual attendance;
 - whilst indirect cost pertinent to the role of directors are separately reimbursed, a fair and reasonable allowance for any direct costs should, however, be made in the base fee;
 - in the case of companies of usual size or complexity, a comparison can be made, and a relativity established with the level of the chief executive officer's remuneration disregarding any incentive package;
 - company performance (i.e. profit, dividend and share price) is not considered to be of special significant for the purpose of setting a base fee;
 - the fee must be fair.
- **Forms of payment**
 - cash;
 - shares or share options – this can have the advantage of aligning remuneration with the interest of the shareowners by increasing the focus of directors on company performance and share value. Where share options are to be offered to non-executive directors, shareowners must approve this offer in a general meeting prior to the allocation being implemented.
- **Reviews**

The dates for review would be an appropriate time also to undertake evaluations of the performances of individual directors.

- **Equal sharing**

In line with the principle of collective responsibility, base fees should, whenever possible be shared equally except in the case of additional responsibility or workload such as the chairperson and deputy

chairperson. The level will depend on the extent of their involvement with the company.

- **Supplementary fees**

Supplementary work resulting from the membership of board committees (e.g. audit, remuneration, etc.) should be spread as evenly as possible among board members and recognised in the level of the base fee. If supplementary fees are charged separately, they may be calculated as an hourly or daily rate rather than annually and should be subject to review in the same manner as base fees.

- **Reimbursement of expenses**

- Directors should ensure that they are reimbursed for all direct and indirect expenses reasonably and properly incurred (e.g. office, secretarial, accommodation, travelling expenses).
- Accommodation and travelling expenses should include those incurred in attending all meetings of director and board committee's, shareowners' meetings or otherwise in connection with company business.
- Where a director uses personal transport, travelling expenses should include realistic kilometre allowances.
- Expenses applicable to multi-directorships should be apportioned on a fair and reasonable basis, having regard to the time spent on each directorship including travelling costs.
- Directors should ensure that the company's articles of association do not restrict the reimbursement of expenses.

- **Directors' and Officers' liability insurance**

- Directors should, wherever practical, arrange for such insurance to be taken out, and for such insurance to be paid by the company.
- The cover provided by the insurance should be as extensive as permitted by law, including all risks relating to legal costs.
- Directors should ensure that the payment of insurance cover is authorised by the company's articles of association

- **Payment on termination**

- The payment of retirement benefits to executive directors is an accepted practice among companies and should be determined on the company's particular circumstances. Alternatively, a termination payment can be negotiated as part of their overall remuneration package.
- If retirement benefits are paid it is recommended that, unless authorised otherwise by shareowners, the lump sum amount to the

base for the pension should both exceed the total remuneration of the director in his or her capacity as a director in any three years chosen by the Committee.

- The Committee should ensure that the payments or benefits of any nature on termination are not restricted by the company's articles of association but are fair to the company and can be adequately justified to shareowners if called on to do so.

- **Flexibility**

- All the component of remuneration are, in the normal course, a matter of negotiated commercial contract and, accordingly, should be sufficiently flexible to suit each individual circumstance.

ANNEXURE N: PROPOSED ANNUAL REPORT DISCLOSURE TABLES

TABLE 1 Total remuneration excluding incentives								
Base pay/Cash	Retirement + Risk contributions (ER)	Other contributions	Allowances	Sub Total Guaranteed Pay (CTC)	Other Material benefits	Severance/Loss of benefits	Directors emoluments & consulting fees	TOTAL REM EXCLUDING INCENTIVES

TABLE 2 Variable Pay/Remuneration			
STI		LTI	
Short Term Incentive payments	Deferred STI	LTI - awarded	LTI - gains
		Rand value of awarded amount	Gross Rand Value of shares sold/options exercised+ sold
			Shares, options, phantom/SARS/loan deferred pay arrangements

TABLE 3 Variable Remuneration accrued /less what has been reported in Table 2 as paid out in Financial Year			
STI	DSTI	RETENTION	LTI
			Total not annual

TABLE 4 Long term incentives								
Total holding at start of FY	Total # granted	Strike Price	Total # exercised	Price exercised at	Total # vested	Total No cancelled/lapsed	Total # unvested at year-end	Total holding at year end
vested/unvested								

TABLE 5 No of share options /SARS		
Strike price per grant	vesting period per grant	Valid or not at end of financial year end
Expiry date per grant		

ANNEXURE O: GUIDELINES FOR THE DISCLOSURE AND DETERMINATION OF REMUNERATION FOR NON-EXECUTIVE AND EXECUTIVE DIRECTORS

Considerations

- (a) In determining an appropriate and fair base fee structure, the following should be considered:
- The general level of hourly or daily rates of fees earned by directors in their professional capacities (for instance, as lawyers, accountants, executives or management consultants);
 - The hours spent in travel and preparation for meetings, as well as actual attendance;
 - Although the indirect costs pertinent to the role of directors are separately reimbursed, a fair and reasonable allowance for any direct costs should be made in the base fee;
 - In the case of companies of the usual size or complexity, a comparison can be made, and a relativity established with the level of the chief executive officer's remuneration disregarding any incentive package;
 - Company performance (profit, dividend and share price) is not considered to be of special significance for the purpose of setting a base fee;
 - The fee must be fair.
- (b) Companies must agree to a base fee for all non-executive directors in terms of their directorships with a listed company. This base fee will be supplemented by attendance fees for their attendance at the respective committees of which they are members. The supplementary attendance fees must take into consideration the amount of time required to prepare for the committee meeting, as well as the duration of the actual meeting.
- (c) All directors' fees must be payable in arrears and not in advance.

- (d) Shareholder approval must be obtained for any increases in remuneration fees or the remuneration structure of directors. No changes in fees should be implemented without the approval of shareholders at an annual general meeting or special meeting.
- (e) Different remuneration structures may be agreed by the board for chairpersons or deputy chairpersons of committees, senior directors and any other additional responsibilities allocated to members of the board.
- (f) All the components of remuneration are normally a matter of negotiated commercial contract and therefore should be sufficiently flexible to suit each individual circumstance.
- (g) Directors should, wherever practical, arrange for personal liability insurance to be taken out, and for such insurance to be paid by the company. The cover provided by the insurance should be as extensive as permitted by law, including all risks relating to legal costs. Directors should ensure that the payment of insurance cover is authorised by the company's articles of association.
- (h) The dates for review would be an appropriate time also to undertake evaluations of the performances of individual directors.

Forms of payment

- (a) Payment to non-executive directors may take the following forms:
 - Fees;
 - Supplementary fees; and
 - Reimbursement of expenses.

- (b) Supplementary work resulting from the membership of board committees should be spread as evenly as possible among board members and recognised in the level of the base fee. If supplementary fees are charged separately, they may be calculated as an hourly or daily rate rather than annually, and should be subject to review in the same manner as base fees.
- (c) Directors should ensure that they are reimbursed for all direct and indirect expenses reasonably and properly incurred (such as office, secretarial, accommodation or travelling expenses). Accommodation and travelling expenses should include those incurred in attending all meetings of director and board committees, shareholders' meetings or otherwise in connection with company business. Where a director uses personal transport, travelling expenses should include realistic kilometric allowances. Expenses applicable to multi-directorships should be apportioned on a fair and reasonable basis, having regard to the time spent on each directorship, including travelling costs. Directors should ensure that the company's articles of association do not restrict the reimbursement of expenses.
- (d) The Remuneration Committee should ensure that the payments or benefits of any nature on termination are not restricted by the company's articles of association but are fair to the company and can be adequately justified to shareholders if the committee is called on to do so.
- (e) Granting shares or share options to non-executive directors should be avoided because of the impact of such grants on their independent decision making. Shares or share options granted under approved black economic empowerment schemes may be allowed in exceptional circumstances.

Procedural guidelines

Shareholder acceptance

- (a) Every effort should be made to promote acceptance of the benefits paid to non-executive directors, for a realistic alignment of director remuneration with corporate strategy.
- (b) Requirements to disclose remuneration in the annual report must be seen as a constructive opportunity to communicate with shareholders on all aspects of remuneration.
- (c) The information disclosed should, in relation to each director, include such matters as a breakdown of remuneration into its individual components, the remuneration package as a total cost to the company, the number of meetings attended and, if practicable, the number of hours worked.
- (d) The adoption by organisations of formal remuneration policies, encompassing such matters as the philosophy behind remuneration assessments, the criteria for remuneration setting, the remuneration components, and the composition and role of the committee, as well as the disclosure of such policies, indicates a responsible approach to remuneration issues to the public.

Remuneration

- (e) Members of a committee may be paid special remuneration in respect of their appointment, fixed by the board, with regard to the functions that the members of a committee perform in addition to their functions as directors in relation to the activities of the organisation. This must be done according to the specific power conferred on the board by the articles of

association of the organisation. This special remuneration must be in addition to the annual fees payable to directors.

- (f) Directors' fees are a combination of an annual retainer and meeting attendance fees, which should be formulated for this purpose.
- (g) Incentives may be used and can take the form of:
 - management performance incentives;
 - commission on deals concluded; or
 - share based incentives.
- (h) Incentives and their awarding must be governed. This should be done in such a way that there is clarity as to who may approve what.

ANNEXURE P: PHASE 2 RESULTS

JSE LISTED COMPANIES (EXCL ALTX AND ADDITIONAL)			Phase 2 results			Other
FirstOfInstrumentLongName	Industry	Sector	Less	Same	More	Country
AECI Ltd	Raw Materials	Chemicals			X	
African Oxygen Ltd				X		
Freeworld Coatings Ltd				X		
Omnia Holdings Ltd				X		
Spanjaard Ltd				X		
Hwange Colliery Company Ltd		Coal	X			x
South African Coal Mining Holdings Ltd			X			
Diamondcore Ltd		Diamonds and gemstones		X		
Diamondcorp Plc				X		
Rockwell Diamonds Inc				X		x
Tawana Resources NL					X	x
Thabex Ltd				X		
Trans Hex Group Ltd				X		
Mondi Ltd		Forrestry and paper			X	
Sappi Ltd				X		
York Timber Organisation Ltd		General mining		X		
African Rainbow Minerals Ltd					X	x
Anglo American Plc				X		
Assore Ltd				X		
Bhp Billiton Plc				X		
Exxaro Resources Ltd					X	
GVM Metals Ltd				X		x
Kumba Iron Ore Ltd					X	
Matodzi Resources Ltd				X		
Merafe Resources Ltd			X			
Metorex Ltd				X		
Miranda Mineral Hldgs Ltd				X		
Mvelaphanda Resources Ltd				X		
Petmin Ltd				X		
Sallies Ltd				X		
Sentula Mining Ltd				X		
Uranium One Inc			X			
Aflease Gold Ltd		Gold mining		X		
Anglogold Ashanti Ltd				X		
Central Rand Gold Ltd				X		x
Drdgold Ltd				X		
Gold Fields Ltd				X		
Great Basin Gold Ltd			X			x
Halogen Holdings Societe Anonyme				X		x
Harmony Gold Mining Company Ltd				X		
Pamodzi Gold Ltd			X			
Simmer And Jack Mines Ltd			X			
Village Main Reef Gold Mining Company Ltd			X			
Witwatersrand Consolidated Gold Resources Ltd				X		
ArcelorMittal SA Ltd		Industrial metals			X	
First Uranium Corporation Ltd			X			
Hiveld Steel And Vanadium Corporation Ltd					X	
Hulamin Ltd					X	
Metmar Ltd				X		
Palabora Mining Company Ltd				X		
Teal Exploration and Mining Inc			X			
Zambia Copper Investments Ltd			X			x
Anglo Platinum Ltd		Platinum and precious metals			X	
Anoorag Resources Corporation			X			
Aquarius Platinum Ltd				X		x
Eastern Platinum Ltd				X		x
Impala Platinum Hlgs Ltd					X	
Jubilee Platinum Plc			X			x
Lonmin P L C					X	
Northam Platinum Ltd				X		
Wesizwe Platinum Ltd				X		

JSE LISTED COMPANIES (EXCL ALT X AND ADDITIONAL)

FirstOfInstrumentLongName	Industry	Sector	Phase 2 results			Other Country
			Less	Same	More	
Afrimat Ltd	Industrial	Construction and minerals		X		
Ag Industries Ltd					X	
Aveng Ltd				X		
Basil Read Hldgs Ltd				X		
Buildmax Ltd				X		
Ceramic Industries Ltd				X		
Distribution and warehousing network Ltd				X		
Elb Group Ltd				X		
Group Five Ltd				X		
Kaydav Group Ltd				NEW		
Kwikspace Modular Buildings Ltd				X		
Masonite Africa Ltd				X		
Murray And Roberts Holdings Ltd				X		
Pretoria Portland Cement Company Ltd				X		
Protech Khuthele Holdings Ltd				X		
Raubex Group Ltd				X		
Sea Kay Holdings Ltd				X		
TWP Holdings Ltd				X		
Wilson Bayly Holmes-Ovcon Ltd				X		
Stefanutti & Bressan Ltd				X		
Allied Electronics Corporation Ltd		Electric and electronic equipment			X	
Amalgamated Electronic Corporation Ltd			X			
ARB Holdings Ltd				X		
Bicc Cafca Ltd			X			x
Control Instruments Group Ltd				X		
Delta Electrical Industries Ltd				X		
Digicore Holdings Ltd				X		
Jasco Electronics Holdings Ltd				X		
Reunert Ltd					X	
Setpoint Technology Holdings Ltd				X		
South Ocean Holdings Ltd				X		
Argent Industrial Ltd		General industrial		X		
Astrapak Ltd Pref					X	
Barloworld Ltd					X	
Bowler Metcalf Ltd				X		
Kap International Holdings Ltd				X		
Nampak Ltd					X	
Remgro Ltd				X		
Sekunjalo Investments Ltd				X		
Transpaco Ltd				X		
Bell Equipment Ltd		Industrial engineering		X		
Howden Africa Holdings Ltd				X		
Hudaco Industries Ltd					X	
Invicta Holdings Ltd				X		
Kairos Industrial Holdings Ltd				X		
Venter Leisure and Commercial Trailers Ltd				X		
Cargo Carriers Ltd		Industrial transportation		X		
Grindrod Ltd					X	
Imperial Holdings Ltd					X	
Mobile Industries Ltd			X			
Super Group Ltd				X		x
Trencor Ltd				X		
Value Group Ltd				X		
Adcorp Hldgs Ltd		Support services		X		
Austro Group Ltd				X		
The Bidvest Group Ltd				X		
Command Holdings Ltd				X		
Enviroserv Holdings Ltd				X		
Excellerate Hldgs Ltd				X		
Iliad Africa Ltd				X		
Kelly Group Ltd				X		
Marshall Monteagle Holdings Societe Anonyme			X			
Metrofile Holdings Ltd				X		
Micromega Holdings Ltd			X			
Mvelaphanda Group Ltd				X		
Primeserv Group Ltd				X		
Telimatrix Ltd				X		
Universal Industries Corporation Ltd				X		
Winhold Ltd				X		

JSE LISTED COMPANIES (EXCL ALTX AND ADDITIONAL)

FirstOfInstrumentLongName	Industry	Sector	Phase 2 results			Other Country
			Less	Same	More	
Absa Group Limited	Financial	Banks			X	
Capitec Bank Hldgs Ltd				X		
Firststrand Ltd					X	
Mercantile Bank Hldgs Ltd				X		
Nedbank Group Ltd					X	
Rmb Holdings Ltd				X		
Standard Bank Group Ltd					X	
Brimstone Investmnt Corp		Equity investment instruments			X	
Cape Empowerment Trust Ltd				X		
Eureka Industrial Ltd				X		
Hosken Cons Invest Ltd				X		
Makalani Holdings Ltd			X			
Purple Capital Ltd			X			
Real Africa Hldgs Ltd				X		
Sabvest Ltd				X		
Trematon Capital Inv Ltd			X			
African Bank Investments Ltd		General financial			X	x
Afrocentric Inv Corp Ltd			X			
Anbeeco Investment Holdings Ltd			X			
Barnard Jacobs Mellet Holdings Ltd				X		
Brait SA					X	
Cadiz Holdings Ltd				X		
Conduit Capital Ltd			X			
Coronation Fund Managers Ltd				X		
Decillion Ltd				X		
Enterprise Risk Management Ltd				X		
Investec Ltd					X	
Jse Ltd				X		
London Finance and Investment Group Plc				X		
M Cubed Holdings Ltd				X		
New Corpcapital Ltd			X			
Peregrine Holdings Ltd				X		
PSG Financial Services				X		
Sasfin Holdings Ltd				X		
Wooltru Ltd				X		
Zeder Investments Ltd				X		
Clientele Life Assurance Company Ltd		Life insurance		X		
Discovery Holdings Ltd				X		
Liberty Group Ltd					X	
Liberty Holdings Ltd			X			
Metropolitan Hldgs Ltd				X		
Old Mutual Plc					X	
Sanlam Ltd					X	x
Glenrand M.i.b. Ltd		Non-life insurance		X		
Mutual And Federal Insurance Company Ltd				X		
Sanlam Ltd				X		
Zurich Insurance Company of SA Ltd				X		
Acucap Properties Ltd		Real estate		X		
Ambit Properties Ltd				X		
Apexhi Properties Ltd			X			
Bonatla Property HoLdings Ltd				X		
Capital Property Fund Ltd			X			
Colliers SA Holdings Ltd				X		
Diversified Property Fund Ltd				X		
Emira Property Fund			X			
Fairvest Property Holdings Ltd			X			
Fountainhead Property Trust			X			
Growthpoint Properties Ltd			X			
Hospitality Property Fund Ltd			X			
Hyprop Investments Ltd			X			
Johnnic Holdings Ltd				X		
Liberty International Plc				X		
Madison Property Fund Managers Holdings Ltd				X		
Merchant & Industrial Properties Ltd			X			
Monyetla Property Fund Ltd			X			
Octodec Investments Ltd				X		
Orion Real Estate Ltd			X			
Pangbourne Properties Ltd				X		
Premium Properties Ltd				X		
Putprop Ltd			X			
Redefine Income Fund Ltd			X			
Resilient Property Income Fund Ltd			X			
SA Corporate Real Estate Fund			X			
SA Reit Ltd				X		
Sable Hldgs Ltd			X			
Sycum Property Fund			X			
Vukile Property Fund Ltd				X		

JSE LISTED COMPANIES (EXCL ALTX AND ADDITIONAL)

FirstOfInstrumentLongName	Industry	Sector	Phase 2 results			Other Country
			Less	Same	More	
Pik N Pay Holdings Ltd	Consumer services	Food and drug retailers			X	
Shoprite Hldgs Ltd			X			
The Spar Group Ltd				X		
Advtech Ltd		General retailers	X			
African And Overseas Enterprises Ltd				X		
Cashbuild Ltd				X		
Combined Motor Holdings Ltd				X		
Ellerine Holdings Ltd				X		
Foschini Ltd					X	
Italtile Ltd				X		
Jd Group Ltd					X	
Lewis Group Ltd				X		
Massmart Holdings Ltd					X	
Mr Price Group Ltd					X	
New Clicks Hldgs Ltd					X	
Nictus Ltd			X			x
Rex Trueform Clothing Company Ltd				X		
Tradehold Ltd			X			
Truworths International Ltd				X		
Verimark Holdings Ltd			X			
Woolworths Holdings Ltd					X	
African Media Entertainment		Media	X			
Avusa Ltd					X	
Caxton and Ctp Publishers and Printers Ltd				X		
Kagiso Media Ltd					X	
Naspers Ltd					X	
City Lodge Htl's Ltd		Travel and leisure		X		
Comair Ltd				X		
Cullinan Holdings Ltd			X			
The Don Group Ltd			X			
Famous Brands Ltd			X			
Gold Reef Resorts Ltd				X		
Ideco Group Ltd				X		
Ifa Hotels And Resorts			X			x
King Consolidated Holdings Ltd			X			
Phumelela Gaming and Leisure Ltd			X			
Spur Corporation Ltd			X			
Sun International Ltd					X	
Tourism Investment Corporation Ltd				X		
Dorbyl Ltd	Consumer goods	Automobiles and parts	X			
Metair Investments Ltd				X		
Tiger Automotive Ltd				X		
Wesco Investments Ltd				X		
Awethu Breweries Ltd		Beverages	X			
Distell Group Ltd				X		
KWV Investments Ltd				X		
SabMiller Plc					X	
Afgri Ltd		Food producers			X	
Astral Foods Ltd				X		
Avi Ltd					X	
Conafex Holdings Societe Anonyme			X			
Country Bird Holdings Ltd			X			
Crookes Bros Ltd			X			
Illovo Sugar Ltd				X		
Intertrading Ltd				X		
Oceana Group Ltd					X	
Rainbow Chicken Ltd					X	
Sovereign Food Investments Ltd				X		
Tiger Brands Ltd				X		
Tongaat Hulett Ltd				X		
Steinhoff International Holdings Ltd		Household goods			X	
Amalgamated Appl Hld Ltd		Leisure goods		X		
Nu-world Holdings Ltd			X			
Emergent Properties Ltd		Personal goods		X		
The House of Busby Ltd				X		
Pals Holdings Ltd			X			
Richemont Securities AG					X	x
Seardel Invest Corp Ltd				X		

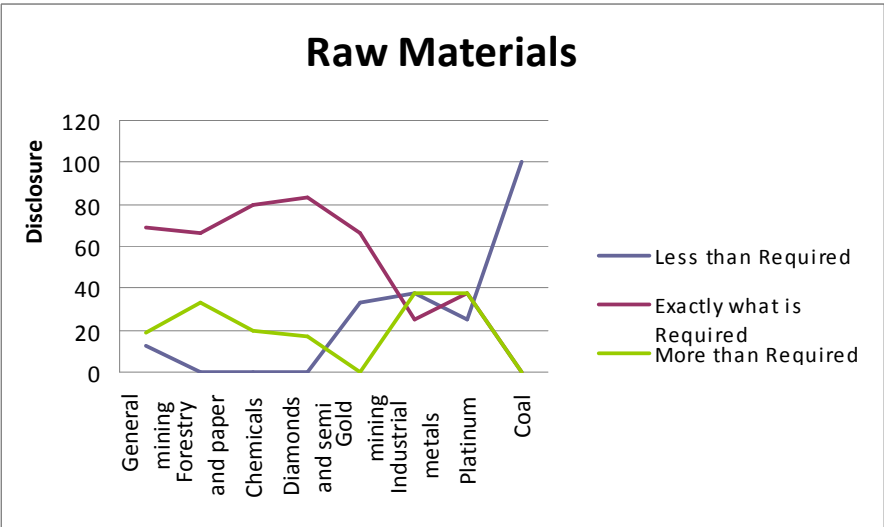
JSE LISTED COMPANIES (EXCL ALTX AND ADDITIONAL)

FirstOfInstrumentLongName	Industry	Sector	Phase 2 results			Other Country
			Less	Same	More	
Mustek Ltd	Technology	Hardware			X	
Pinnacle Technology Hldgs Ltd				X		
Bytes Technology Group		Software			X	
Business Connexion Group Ltd				X		
Compu Clearing Outsourcing Ltd				X		
Convergenet Holdings Ltd				X		
Datacentrix Holdings Ltd			X			
Datatec Ltd					X	
Dimension Data Hldgs Plc					X	
Eoh Holdings Ltd				X		
Faritec Holdings Ltd			X			
Gijima Ast Group Ltd				X		
InfoWave Holdings Ltd				X		
Paracon Holdings Ltd			X			
Securedata Holdings Ltd				X		
Spescom Ltd				X		
Square One Solutions Group Ltd			X			
Ucs Group Ltd				X		
Absolute Holdings Ltd	Venture Capital	General	X			
Beget Holdings Ltd					X	
Cenmag Holdings Ltd			X			
Industrial Credit Company Africa Holdings Ltd			X			x
John Daniel Holdings Ltd				X		
Labat Africa Ltd				X		
Lonrho Plc				X		x
SA Mineral Resources Corporation Ltd				X		
Southern Electricity Company Ltd			X			
Cenmag Holdings Ltd	Development Capital	General	X			
Dynamic Cables Rsa Ltd			X			
Independent Financial Services Ltd			X			
Indequity Group Ltd				X		
S and J Land Holdings Ltd			X			
Stella Vista Technologies Ltd					X	
Telkom Sa Ltd	Telecommunications	Fixed line		X		
Allied Technologies Ltd		Mobile			X	
Blue Label Telecoms Ltd			X			
Mtn Group Ltd					X	
Medi-clinic Corp Ltd	Health care	Health care services		X		
Network Healthcare Holdings Ltd			X			
Aspen Pharmacare Holdings Ltd		Pharmaceutical		X		
Enaleni Pharmaceuticals Ltd				X		
Oando Plc	Oil and gas	Oil and gas	X			x
Sasol Ltd					X	

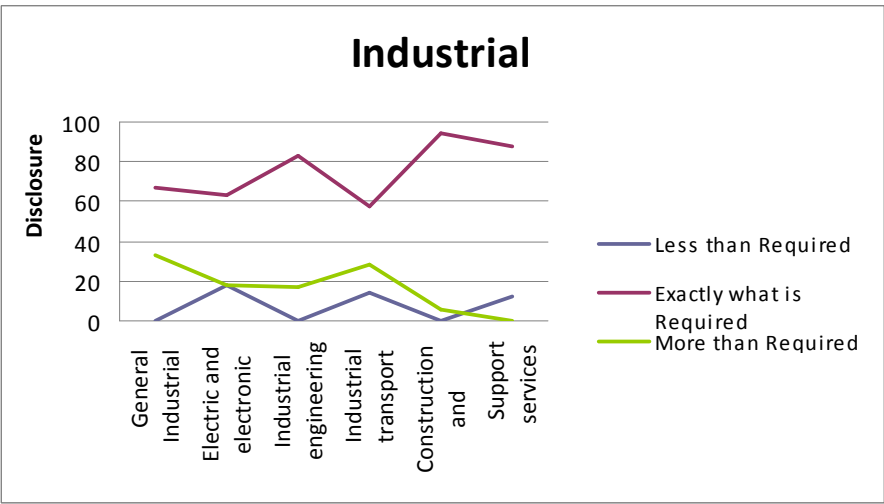
ANNEXURE Q: LOCATIONS OF EXECUTIVE REMUNERATION DISCLOSURES

Industry	Sector	Location of executive remuneration disclosure in 2007 Annual Report																				
		Separate chapter			Corporate Governance Report			Directors' Report			Sustainability Report			Notes to Financial Statements			No disclosure			Multiple locations		
		Less	Same	More	Less	Same	More	Less	Same	More	Less	Same	More	Less	Same	More	Less	Same	More	Less	Same	More
Raw materials	General mining			3		1			4				1	6						1		
	Forestry and paper			1										2								
	Chemicals			1					1					2							1	
	Diamonds and semi precious stones		1	1										4								
	Gold mining								2					2						1	4	
	Industrial metals			3										2	2		1					
	Platinum			3				1						1	1						2	
	Coal													2								
Sub total		0	1	12	0	1	0	1	7	0	0	0	0	19	0	1	0	0	2	7	0	
Industrial	General industrial			3					1					4							2	
	Electric and electronic				1		1			1				3							3	1
	Industrial engineering													3							2	1
	Industrial transport			1		2								2		1						1
	Construction and materials			1		2								7							9	
	Support services					2								2	2						10	
	Sub total	0	0	5	1	6	1	0	1	0	0	0	0	3	21	0	1	0	0	0	26	3
Financial	General financial			3	3	3			1				1	5							4	
	Banks			3					1												2	1
	Equity investment instruments			1	1									4							1	
	Property		1		2	4		1	1					4		4					3	3
	Life assurance			2	1	1	1							1							1	
	Non-life insurance								1					1							2	
	Sub total	0	1	9	7	8	1	1	4	0	0	0	0	9	15	0	4	0	0	4	13	1
Consumer services	General retail		1	3		2	1				1			3							2	2
	Media			2										1							1	1
	Travel and leisure			3	1	2	1	1	1					3	3		2				1	
	Food and medicine retail																			1	1	1
	Sub total	0	1	8	1	4	2	1	1	0	1	0	0	8	6	0	2	0	0	2	4	4
Consumer goods	Beverages			1										1							2	
	Household goods					1									2							1
	Automobiles and parts							1													1	
	Leisure goods							1														
	Personal goods				1									1	2							
	Food producers			3		2	1	1	1					1	3						1	1
	Sub total	0	0	4	1	3	1	3	1	0	0	0	0	3	7	0	0	0	0	1	3	2
Technology	Software			3										2	4						2	2
	Hardware									1					1							
	Sub total	0	0	3	0	0	0	0	0	1	0	0	0	2	5	0	0	0	0	2	2	0
Venture capital	General				1	1		1	1					2	1						1	1
	Sub total	0	0	0	1	1	0	1	1	0	0	0	0	2	1	0	0	0	0	0	1	1
Development capital	General						1							4	1							
	Sub total	0	0	0	0	0	1	0	0	0	0	0	0	4	1	0	0	0	0	0	0	0
Telecommunications	Mobile			1						1					1							
	Fixed line													1								
	Sub total	0	0	1	0	0	0	0	0	1	0	0	0	1	1	0	0	0	0	0	0	0
Health care	Pharmaceutical													1	1							
	Health services																				2	
	Sub total	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0	0	0	0	0	2	0
Oil and gas	General			1													1					
	Sub total	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0

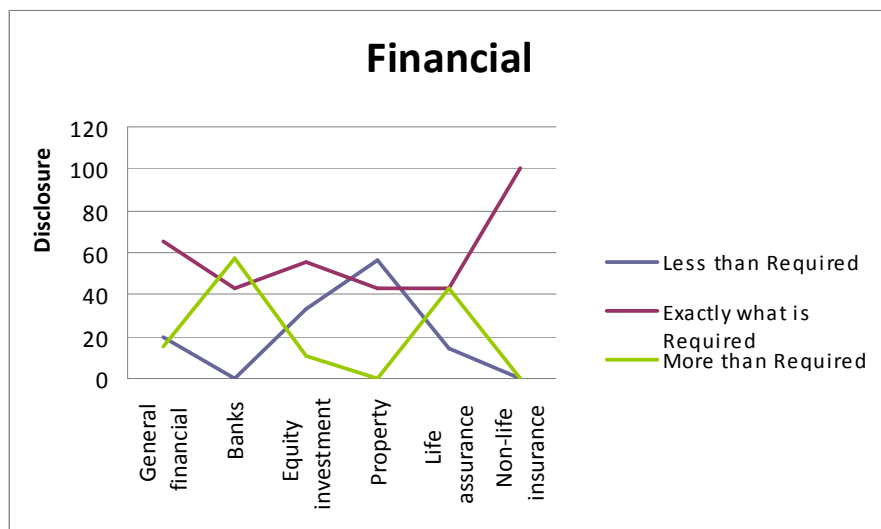
ANNEXURE R: ANNUAL REPORT DISCLOSURE ANALYSIS



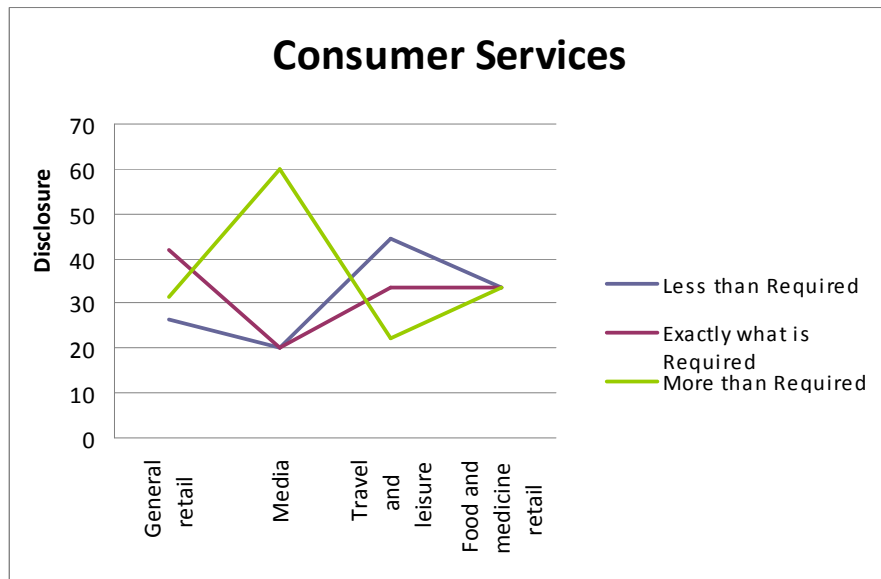
In the Raw Materials industry there was a strong trend to disclose exactly what is required in terms of executive remuneration disclosures. In the smaller sectors in this industry, the trend favoured disclosures which did not meet the minimum disclosure requirements in South Africa.



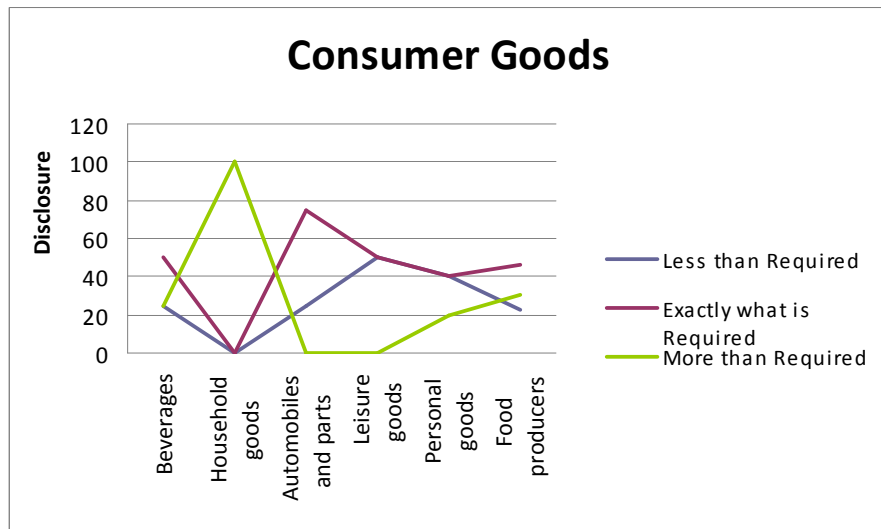
In the Industrial category there was a very strong trend towards making executive remuneration disclosures which merely comply with the minimum disclosure requirements, across all sectors in the industry. There were generally more companies that disclose in excess of what is required than those which did not meet minimum disclosure requirements in this category.



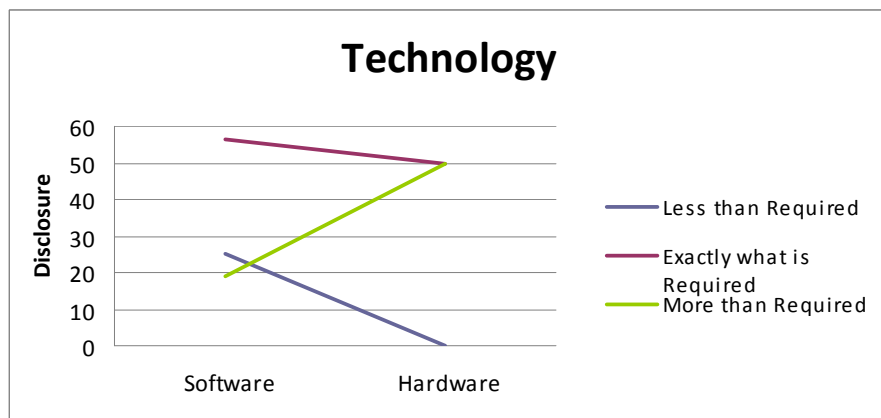
In the Financial industry there was also a trend towards executive remuneration disclosures that merely comply with the relevant disclosure requirements. In the Banking sector there was a trend towards executive remuneration disclosures which are more than what is required, whereas in the Property sector there was a trend towards disclosing less than what is required.



In the Consumer Services industry there was no clear general disclosure trend. In each of the four sectors in the industry there was a different trend. The Media sector however stood out in that a significantly higher percentage of companies in this sector made executive remuneration disclosures in excess of requirements than those in other sectors of the same industry. Apart from this deviation, the distributions across other sectors were fairly equal.

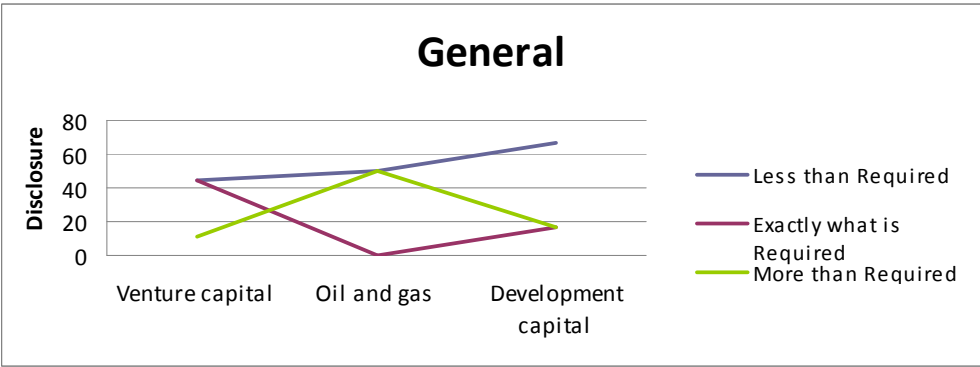


In the Consumer Goods industry there was a fairly general trend across all sectors to make executive remuneration disclosures which are on par with what is required. In the Household Goods sector a significant percentage of companies disclosed more than what is required.

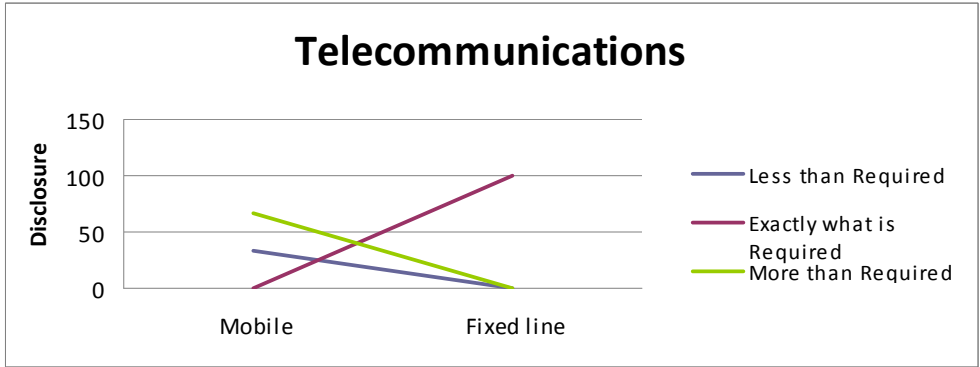


In the Technology industry there was a strong trend across both sectors to disclose more than what is required, while disclosures in the Hardware sector

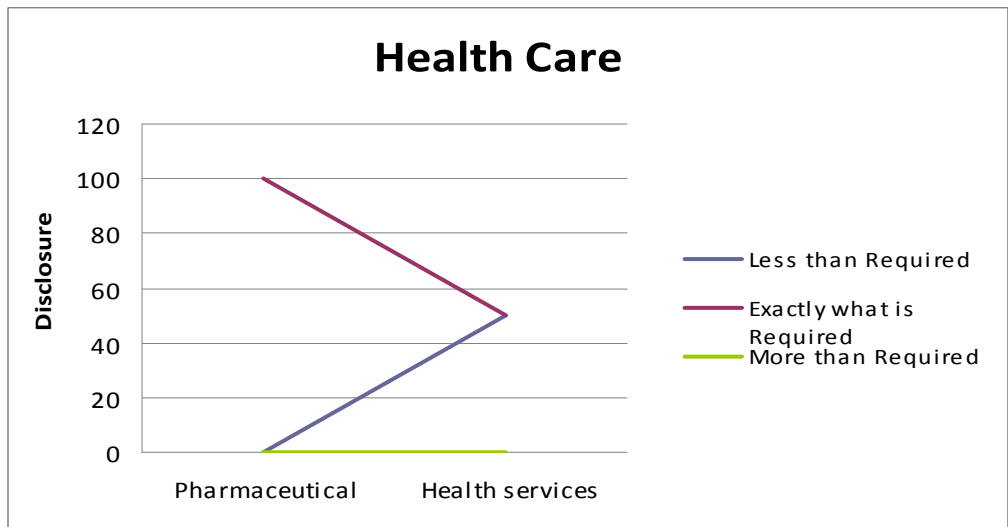
were split equally between disclosures which are either on par with or in excess of what is required.



The data for the Venture and Development Capital, as well as for the Oil and Gas sectors have been combined in Figure 21 above due to the small sizes of these sectors. In each of these sectors however there was a clear trend that most of the companies in each sector tend to make executive remuneration disclosures which did not meet minimum disclosure requirements.



In the Telecommunications industry, executive remuneration disclosures of all companies in the Fixed Line sector were on par with disclosure requirements, whereas two thirds of the companies in the Mobile sector disclosed more than what is required.



In the Health Care industry there was also a clear trend that companies in both sectors tend to make executive remuneration disclosures which merely comply with what is required. All companies listed in the Pharmaceutical sector disclosed exactly what is required, while half of the companies in the Health Services sector made similar executive remuneration disclosures. It is interesting to note that there were no companies in either sector in this industry that disclosed more than what is required.

ANNEXURE S: CRITICAL VALUES OF THE CHI SQUARE DISTRIBUTION

d.f.	Probability under H^0 that $\chi^2 \geq \text{Chi Square}$				
	.10	.05	.02	.01	.001
1	2.71	3.84	5.41	6.64	10.83
2	4.60	5.99	7.82	9.21	13.82
3	6.25	7.82	9.84	11.34	16.27
4	7.78	9.49	11.67	13.28	18.46
5	9.24	11.07	13.39	15.09	20.52
6	10.64	12.59	15.03	16.81	22.46
7	12.02	14.07	16.62	18.48	24.32
8	13.36	15.51	18.17	20.09	26.12
9	14.68	16.92	19.68	21.67	27.88
10	15.99	18.31	21.16	23.21	29.59
11	17.28	19.68	22.62	24.72	31.26
12	18.55	21.03	24.05	26.22	32.91
13	19.81	22.36	25.47	27.69	34.53
14	21.06	23.68	26.87	29.14	36.12
15	22.31	25.00	28.26	30.58	37.70
16	23.54	26.30	29.63	32.00	39.29
17	24.77	27.59	31.00	33.41	40.75
18	25.99	28.87	32.35	34.80	42.31
19	27.20	30.14	33.69	36.19	43.82
20	28.41	31.41	35.02	37.57	45.32
21	29.62	32.67	36.34	38.93	46.80
22	30.81	33.92	37.66	40.29	48.27
23	32.01	35.17	38.97	41.64	49.73
24	33.20	36.42	40.27	42.98	51.18
25	34.38	37.65	41.57	44.31	52.62
26	35.56	38.88	42.86	45.64	54.05
27	36.74	40.11	44.14	46.96	55.48
28	37.92	41.34	45.42	48.28	56.89
29	39.09	42.56	46.69	49.59	58.30
30	40.26	43.77	47.96	50.89	59.70

(Cooper and Schindler, 2003: 821)

ANNEXURE T: UK DIRECTORS' REMUNERATION REPORT REGULATIONS UNDER THE COMPANIES ACT, 1985

SCHEDULE 8

QUOTED COMPANIES: DIRECTORS' REMUNERATION REPORT

PART 1

INTRODUCTORY

- 1.6** (1) In the directors' remuneration report for a financial year (the relevant financial year) there must be shown the information specified in Parts 2 and 3.
- (2) Information required to be shown in the report for or in respect of a particular person must be shown in the report in a manner that links the information to that person identified by name.

PART 2

INFORMATION NOT SUBJECT TO AUDIT

Consideration by the directors of matters relating to directors' remuneration

- 2.6** (1) If a committee of the company's directors has considered matters relating to the directors' remuneration for the relevant financial year, the directors' remuneration report must—
- (a) name each director who was a member of the committee at any time when the committee was considering any such matter;
 - (b) name any person who provided to the committee advice, or services, that materially assisted the committee in their consideration of any such matter;
 - (c) in the case of any person named under paragraph (b), who is not a director of the company, state—
 - (i) the nature of any other services that that person has provided to the company during the relevant financial year; and
 - (ii) whether that person was appointed by the committee.
- (2) In sub-paragraph (1)(b) "person" includes (in particular) any director of the company who does not fall within sub-paragraph (1)(a).

Statement of company's policy on directors' remuneration

- 3.6** (1) The directors' remuneration report must contain a statement of the company's policy on directors' remuneration for the following financial year and for financial years subsequent to that.
- (2) The policy statement must include—
- (a) for each director, a detailed summary of any performance conditions to which any entitlement of the director—
 - (i) to share options, or
 - (ii) under a long term incentive scheme,is subject;
 - (b) an explanation as to why any such performance conditions were chosen;
 - (c) a summary of the methods to be used in assessing whether any such performance conditions are met and an explanation as to why those methods were chosen;
 - (d) if any such performance condition involves any comparison with factors external to the company—
 - (i) a summary of the factors to be used in making each such comparison, and
 - (ii) if any of the factors relates to the performance of another company, of two or more other companies or of an index on which the securities of a company or

- companies are listed, the identity of that company, of each of those companies or of the index;
 - (e) a description of, and an explanation for, any significant amendment proposed to be made to the terms and conditions of any entitlement of a director to share options or under a long term incentive scheme; and
 - (f) if any entitlement of a director to share options, or under a long term incentive scheme, is not subject to performance conditions, an explanation as to why that is the case.
- (3) The policy statement must, in respect of each director's terms and conditions relating to remuneration, explain the relative importance of those elements which are, and those which are not, related to performance.
- (4) The policy statement must summarise, and explain, the company's policy on
- (a) the duration of contracts with directors, and
 - (b) notice periods, and termination payments, under such contracts.
- (5) In sub-paragraphs (2) and (3), references to a director are to any person who serves as a director of the company at any time in the period beginning with the end of the relevant financial year and ending with the date on which the directors' remuneration report is laid before the company in general meeting.

Statement of consideration of conditions elsewhere in company and group

4. The directors' remuneration report must contain a statement of how pay and employment conditions of employees of the company and of other undertakings within the same group as the company were taken into account when determining directors' remuneration for the relevant financial year.

Performance graph

5. (1) The directors' remuneration report must
- (a) contain a line graph that shows for each
 - (i) a holding of shares of that class of the company's equity share capital whose listing, or admission to dealing, has resulted in the company falling within the definition of "quoted company", and
 - (ii) a hypothetical holding of shares made up of shares of the same kinds and number as those by reference to which a broad equity market index is calculated, a line drawn by joining up points plotted to represent, for each of the financial years in the relevant period, the total shareholder return on that holding; and
 - (b) state the name of the index selected for the purposes of the graph and set out the reasons for selecting that index.
- (2) For the purposes of sub-paragraphs (1) and (4), "relevant period" means the five financial years of which the last is the relevant financial year.
- (3) Where the relevant financial year
- (a) is the company's second, third or fourth financial year, sub-paragraph (2) has effect with the substitution of "two", "three" or "four" (as the case may be) for "five"; and
 - (b) is the company's first financial year, "relevant period", for the purposes of sub-paragraphs (1) and (4), means the relevant financial year.
- (4) For the purposes of sub-paragraph (1), the "total shareholder return" for a relevant period on a holding of shares must be calculated using a fair method that
- (a) takes as its starting point the percentage change over the period in the market price of the holding;
 - (b) involves making
 - (i) the assumptions specified in sub-paragraph (5) as to reinvestment of income, and
 - (ii) the assumption specified in sub-paragraph (7) as to the funding of liabilities, and
 - (c) makes provision for any replacement of shares in the holding by shares of a different description;

and the same method must be used for each of the holdings mentioned in sub-paragraph (1).

(5) The assumptions as to reinvestment of income are

(a) that any benefit in the form of shares of the same kind as those in the holding is added to the holding at the time the benefit becomes receivable; and

(b) that any benefit in cash, and an amount equal to the value of any benefit not in cash and not falling within paragraph (a), is applied at the time the benefit becomes receivable in the purchase at their market price of shares of the same kind as those in the holding and that the shares purchased are added to the holding at that time.

(6) In sub-paragraph (5) "benefit" means any benefit (including, in particular, any dividend) receivable in respect of any shares in the holding by the holder from the company of whose share capital the shares form part.

(7) The assumption as to the funding of liabilities is that, where the holder has a liability to the company of whose capital the shares in the holding form part, shares are sold from the holding

(a) immediately before the time by which the liability is due to be satisfied, and

(b) in such numbers that, at the time of the sale, the market price of the shares sold equals the amount of the liability in respect of the shares in the holding that are not being sold.

(8) In sub-paragraph (7) "liability" means a liability arising in respect of any shares in the holding or from the exercise of a right attached to any of those shares.

Service contracts

6.6 (1) The directors' remuneration report must contain, in respect of the contract of service or contract for services of each person who has served as a director of the company at any time during the relevant financial year, the following information

(a) the date of the contract, the unexpired term and the details of any notice periods;

(b) any provision for compensation payable upon early termination of the contract; and

(c) such details of other provisions in the contract as are necessary to enable members of the company to estimate the liability of the company in the event of early termination of the contract.

(2) The directors' remuneration report must contain an explanation for any significant award made to a person in the circumstances described in paragraph 15.

PART 3

INFORMATION SUBJECT TO AUDIT

Amount of each director's emoluments and compensation in the relevant financial year

7.6 (1) The directors' remuneration report must for the relevant financial year show, for each person who has served as a director of the company at any time during that year, each of the following

(a) the total amount of salary and fees paid to or receivable by the person in respect of qualifying services;

(b) the total amount of bonuses so paid or receivable;

(c) the total amount of sums paid by way of expenses allowance that are

(i) chargeable to United Kingdom income tax (or would be if the person were an individual), and

(ii) paid to or receivable by the person in respect of qualifying services;

(d) the total amount of

(i) any compensation for loss of office paid to or receivable by the person, and

(ii) any other payments paid to or receivable by the person in connection with the termination of qualifying services;

(e) the total estimated value of any benefits received by the person otherwise than in cash that

(i) do not fall within any of paragraphs (a) to (d) or paragraphs 8 to 12,

- (ii) are emoluments of the person, and
 - (iii) are received by the person in respect of qualifying services; and
 - (f) the amount that is the total of the sums mentioned in paragraphs (a) to (e).
- (2) The directors' remuneration report must show, for each person who has served as a director of the company at any time during the relevant financial year, the amount that for the financial year preceding the relevant financial year is the total of the sums mentioned in paragraphs (a) to (e) of sub-paragraph (1).
- (3) The directors' remuneration report must also state the nature of any element of a remuneration package which is not cash.
- (4) The information required by sub-paragraphs (1) and (2) must be presented in tabular form.

Share options

8.6 (1) The directors' remuneration report must contain, in respect of each person who has served as a director of the company at any time in the relevant financial year, the information specified in paragraph 9.

(2) Sub-paragraph (1) is subject to paragraph 10 (aggregation of information to avoid excessively lengthy reports).

(3) The information specified in sub-paragraphs (a) to (c) of paragraph 9 must be presented in tabular form in the report.

(4) In paragraph 9 'share option', in relation to a person, means a share option granted in respect of qualifying services of the person.

9. The information required by sub-paragraph (1) of paragraph 8 in respect of such a person as is mentioned in that sub-paragraph is

- (a) the number of shares that are subject to a share option
 - (i) at the beginning of the relevant financial year or, if later, on the date of the appointment of the person as a director of the company, and
 - (ii) at the end of the relevant financial year or, if earlier, on the cessation of the person's appointment as a director of the company,
 in each case differentiating between share options having different terms and conditions;
- (b) information identifying those share options that have been awarded in the relevant financial year, those that have been exercised in that year, those that in that year have expired unexercised and those whose terms and conditions have been varied in that year;
- (c) for each share option that is unexpired at any time in the relevant financial year
 - (i) the price paid, if any, for its award,
 - (ii) the exercise price,
 - (iii) the date from which the option may be exercised, and
 - (iv) the date on which the option expires;
- (d) a description of any variation made in the relevant financial year in the terms and conditions of a share option;
- (e) a summary of any performance criteria upon which the award or exercise of a share option is conditional, including a description of any variation made in such performance criteria during the relevant financial year;
- (f) for each share option that has been exercised during the relevant financial year, the market price of the shares, in relation to which it is exercised, at the time of exercise; and
- (g) for each share option that is unexpired at the end of the relevant financial year
 - (i) the market price at the end of that year, and
 - (ii) the highest and lowest market prices during that year, of each share that is subject to the option.

10.6 (1) If, in the opinion of the directors of the company, disclosure in accordance with paragraphs 8 and 9 would result in a disclosure of excessive length then, (subject to subparagraphs (2) and (3))

- (a) information disclosed for a person under paragraph 9(a) need not differentiate between share options having different terms and conditions;

- (b) for the purposes of disclosure in respect of a person under paragraph 9(c)(i) and (ii) and (g), share options may be aggregated and (instead of disclosing prices for each share option) disclosure may be made of weighted average prices of aggregations of share options;
 - (c) for the purposes of disclosure in respect of a person under paragraph 9(c)(iii) and (iv), share options may be aggregated and (instead of disclosing dates for each share option) disclosure may be made of ranges of dates for aggregation of share options.
- (2) Sub-paragraph (1)(b) and (c) does not permit the aggregation of
- (a) share options in respect of shares whose market price at the end of the relevant financial year is below the option exercise price, with
 - (b) share options in respect of shares whose market price at the end of the relevant financial year is equal to, or exceeds, the option exercise price.
- (3) Sub-paragraph (1) does not apply (and accordingly, full disclosure must be made in accordance with paragraphs 8 and 9) in respect of share options that during the relevant financial year have been awarded or exercised or had their terms and conditions varied.

Long term incentive schemes

- 11.6** (1) The directors' remuneration report must contain, in respect of each person who has served as a director of the company at any time in the relevant financial year, the information specified in paragraph 12.
- (2) Sub-paragraph (1) does not require the report to contain share option details that are contained in the report in compliance with paragraphs 8 to 10.
- (3) The information specified in paragraph 12 must be presented in tabular form in the report.
- (4) For the purposes of paragraph 12
- (a) 'scheme interest', in relation to a person, means an interest under a long term incentive scheme that is an interest in respect of which assets may become receivable under the scheme in respect of qualifying services of the person; and
 - (b) such an interest vests at the earliest time when
 - (i) it has been ascertained that the qualifying conditions have been fulfilled, and
 - (ii) the nature and quantity of the assets receivable under the scheme in respect of the interest have been ascertained.
- (5) In this Schedule 'long term incentive scheme' means any agreement or arrangement under which money or other assets may become receivable by a person and which includes one or more qualifying conditions with respect to service or performance that cannot be fulfilled within a single financial year, and for this purpose the following must be disregarded, namely
- (a) any bonus the amount of which falls to be determined by reference to service or performance within a single financial year;
 - (b) compensation in respect of loss of office, payments for breach of contract and other termination payments; and
 - (c) retirement benefits.

- 12.6** (1) The information required by sub-paragraph (1) of paragraph 11 in respect of such a person as is mentioned in that sub-paragraph is
- (a) details of the scheme interests that the person has at the beginning of the relevant financial year or if later on the date of the appointment of the person as a director of the company;
 - (b) details of the scheme interests awarded to the person during the relevant financial year;
 - (c) details of the scheme interests that the person has at the end of the relevant financial year or if earlier on the cessation of the person's appointment as a director of the company;
 - (d) for each scheme interest within paragraphs (a) to (c)
 - (i) the end of the period over which the qualifying conditions for that interest have to be fulfilled (or if there are different periods for different conditions, the end of whichever of those periods ends last); and
 - (ii) a description of any variation made in the terms and conditions of the scheme interests during the relevant financial year; and

- (e) for each scheme interest that has vested in the relevant financial year
 - (i) the relevant details (see sub-paragraph (3)) of any shares,
 - (ii) the amount of any money, and
 - (iii) the value of any other assets,
 that have become receivable in respect of the interest.
- (2) The details that sub-paragraph (1)(b) requires of a scheme interest awarded during the relevant financial year include, if shares may become receivable in respect of the interest, the following
 - (a) the number of those shares;
 - (b) the market price of each of those shares when the scheme interest was awarded; and
 - (c) details of qualifying conditions that are conditions with respect to performance.
- (3) In sub-paragraph (1)(e)(i) the relevant details, in relation to any shares that have become receivable in respect of a scheme interest, means
 - (a) the number of those shares;
 - (b) the date on which the scheme interest was awarded;
 - (c) the market price of each of those shares when the scheme interest was awarded;
 - (d) the market price of each of those shares when the scheme interest vested; and
 - (e) details of qualifying conditions that were conditions with respect to performance.

Pensions

13.6 (1) The directors' remuneration report must, for each person who has served as a director of the company at any time during the relevant financial year, contain the information in respect of pensions that is specified in sub-paragraphs (2) and (3).

(2) Where the person has rights under a pension scheme that is a defined benefit scheme in relation to the person and any of those rights are rights to which he has become entitled in respect of qualifying services of his

- (a) details
 - (i) of any changes during the relevant financial year in the person's accrued benefits under the scheme, and
 - (ii) of the person's accrued benefits under the scheme as at the end of that year;
- (b) the transfer value, calculated in a manner consistent with "Retirement Benefit Schemes: Transfer Values (GN 11)" published by the Institute of Actuaries and the Faculty of Actuaries and dated 6th April 2001, of the person's accrued benefits under the scheme at the end of the relevant financial year;
- (c) the transfer value of the person's accrued benefits under the scheme that in compliance with paragraph (b) was contained in the directors' remuneration report for the previous financial year or, if there was no such report or no such value was contained in that report, the transfer value, calculated in such a manner as is mentioned in paragraph (b), of the person's accrued benefits under the scheme at the beginning of the relevant financial year;
- (d) the amount obtained by subtracting
 - (i) the transfer value of the person's accrued benefits under the scheme that is required to be contained in the report by paragraph (c), from
 - (ii) the transfer value of those benefits that is required to be contained in the report by paragraph (b),

and then subtracting from the result of that calculation the amount of any contributions made to the scheme by the person in the relevant financial year.

(3) Where

- (a) the person has rights under a pension scheme that is a money purchase scheme in relation to the person, and
- (b) any of those rights are rights to which he has become entitled in respect of qualifying services of his,

details of any contribution to the scheme in respect of the person that is paid or payable by the company for the relevant financial year or paid by the company in that year for another financial year.

Excess retirement benefits of directors and past directors

14.6 (1) Subject to sub-paragraph (3), the directors' remuneration report must show in respect of each person who has served as a director of the company

(a) at any time during the relevant financial year, or

(b) at any time before the beginning of that year,

the amount of so much of retirement benefits paid to or receivable by the person under pension schemes as is in excess of the retirement benefits to which he was entitled on the date on which the benefits first became payable or 31st March 1997, whichever is the later.

(2) In subsection (1) "retirement benefits" means retirement benefits to which the person became entitled in respect of qualifying services of his.

(3) Amounts paid or receivable under a pension scheme need not be included in an amount required to be shown under sub-paragraph (1) if

(a) the funding of the scheme was such that the amounts were or, as the case may be, could have been paid without recourse to additional contributions; and

(b) amounts were paid to or receivable by all pensioner members of the scheme on the same basis;

and in this sub-paragraph "pensioner member", in relation to a pension scheme, means any person who is entitled to the present payment of retirement benefits under the scheme.

(4) In this paragraph

(a) references to retirement benefits include benefits otherwise than in cash; and

(b) in relation to so much of retirement benefits as consists of a benefit otherwise than in cash, references to their amount are to the estimated money value of the benefit,

and the nature of any such benefit must also be shown in the report.

Compensation for past directors

15. The directors' remuneration report must contain details of any significant award made in the relevant financial year to any person who was not a director of the company at the time the award was made but had previously been a director of the company, including (in particular) compensation in respect of loss of office and pensions but excluding any sums which have already been shown in the report under paragraph 7(1)(d).

Sums paid to third parties in respect of a director's services

16.6 (1) The directors' remuneration report must show, in respect of each person who served as a director of the company at any time during the relevant financial year, the aggregate amount of any consideration paid to or receivable by third parties for making available the services of the person

(a) as a director of the company, or

(b) while director of the company

(i) as director of any of its subsidiary undertakings, or

(ii) as director of any other undertaking of which he was (while director of the company)

a director by virtue of the company's nomination (direct or indirect), or

(iii) otherwise in connection with the management of the affairs of the company or any such other undertaking.

(2) The reference to consideration includes benefits otherwise than in cash; and in relation to such consideration the reference to its amount is to the estimated money value of the benefit.

The nature of any such consideration must be shown in the report.

(3) The reference to third parties is to persons other than

(a) the person himself or a person connected with him or a body corporate controlled by him, and

(b) the company or any such other undertaking as is mentioned in sub-paragraph (1)(b)(ii).

PART 4

INTERPRETATION AND SUPPLEMENTARY

17. (1) In this Schedule

“amount”, in relation to a gain made on the exercise of a share option, means the difference between

- (a) the market price of the shares on the day on which the option was exercised; and
- (b) the price actually paid for the shares;

“company contributions”, in relation to a pension scheme and a person, means any payments (including insurance premiums) made, or treated as made, to the scheme in respect of the person by anyone other than the person;

“defined benefit scheme”, in relation to a person, means a pension scheme which is not a money purchase scheme in relation to the person;

“moluments” of a person

- (a) includes salary, fees and bonuses, sums paid by way of expenses allowance (so far as they are chargeable to United Kingdom income tax or would be if the person were an individual), but
- (b) does not include any of the following, namely
 - (i) the value of any share options granted to him or the amount of any gains made on the exercise of any such options;
 - (ii) any company contributions paid, or treated as paid, in respect of him under any pension scheme or any benefits to which he is entitled under any such scheme; or
 - (iii) any money or other assets paid to or received or receivable by him under any long term incentive scheme;

“long term incentive scheme” has the meaning given by paragraph 11(5);

“money purchase benefits”, in relation to a person, means retirement benefits the rate or amount of which is calculated by reference to payments made, or treated as made, by the person or by any other person in respect of that person and which are not average salary benefits;

“money purchase scheme”, in relation to a person, means a pension scheme under which all of the benefits that may become payable to or in respect of the person are money purchase benefits in relation to the person;

“pension scheme” means a retirement benefits scheme within the meaning given by section 611 of the Income and Corporation Taxes Act 1988;

“qualifying services”, in relation to any person, means his services as a director of the company, and his services at any time while he is a director of the company

- (a) as a director of an undertaking that is a subsidiary undertaking of the company at that time;
- (b) as a director of any other undertaking of which he is a director by virtue of the company’s nomination (direct or indirect); or
- (c) otherwise in connection with the management of the affairs of the company or any such subsidiary undertaking or any such other undertaking;

“retirement benefits” means relevant benefits within the meaning given by section 612(1) of the Income and Corporation Taxes Act 1988;

“shares” means shares (whether allotted or not) in the company, or any undertaking which is a group undertaking in relation to the company, and includes a share warrant as defined by section 779(1) of the 2006 Act;

“share option” means a right to acquire shares;

“value”, in relation to shares received or receivable on any day by a person who is or has been a director of the company, means the market price of the shares on that day.

(2) In this Schedule “compensation in respect of loss of office” includes compensation received or receivable by a person for

- (a) loss of office as director of the company, or

- (b) loss, while director of the company or on or in connection with his ceasing to be a director of it, of
 - (i) any other office in connection with the management of the company's affairs, or
 - (ii) any office as director or otherwise in connection with the management of the affairs of any undertaking that, immediately before the loss, is a subsidiary undertaking of the company or an undertaking of which he is a director by virtue of the company's nomination (direct or indirect);
- (c) compensation in consideration for, or in connection with, a person's retirement from office; and
- (d) where such a retirement is occasioned by a breach of the person's contract with the company or with an undertaking that, immediately before the breach, is a subsidiary undertaking of the company or an undertaking of which he is a director by virtue of the company's nomination (direct or indirect)
 - (i) payments made by way of damages for the breach; or
 - (ii) payments made by way of settlement or compromise of any claim in respect of the breach.

(3) References in this Schedule to compensation include benefits otherwise than in cash; and in relation to such compensation references in this Schedule to its amounts are to the estimated money value of the benefit.

(4) References in this Schedule to a person being "connected" with a director, and to a director "controlling" a body corporate, are to be construed in accordance with sections 252 to 255 of the 2006 Act.

18.6 (1) For the purposes of this Schedule emoluments paid or receivable or share options granted in respect of a person's accepting office as a director are to be treated as emoluments paid or receivable or share options granted in respect of his services as a director.

(2) Where a pension scheme provides for any benefits that may become payable to or in respect of a person to be whichever are the greater of

- (a) such benefits determined by or under the scheme as are money purchase benefits in relation to the person; and
- (b) such retirement benefits determined by or under the scheme to be payable to or in respect of the person as are not money purchase benefits in relation to the person,

the company may assume for the purposes of this Schedule that those benefits will be money purchase benefits in relation to the person, or not, according to whichever appears more likely at the end of the relevant financial year.

(3) In determining for the purposes of this Schedule whether a pension scheme is a money purchase scheme in relation to a person or a defined benefit scheme in relation to a person, any death in service benefits provided for by the scheme are to be disregarded.

19.6 (1) The following applies with respect to the amounts to be shown under this Schedule.

(2) The amount in each case includes all relevant sums paid by or receivable from

- (a) the company; and
- (b) the company's subsidiary undertakings; and
- (c) any other person,

except sums to be accounted for to the company or any of its subsidiary undertakings or any other undertaking of which any person has been a director while director of the company, by virtue of section 219 of the 2006 Act (payment in connection with share transfer: requirement of members' approval), to past or present members of the company or any of its subsidiaries or any class of those members.

(3) Reference to amounts paid to or receivable by a person include amounts paid to or receivable by a person connected with him or a body corporate controlled by him (but not so as to require an amount to be counted twice).

20. (1) The amounts to be shown for any financial year under Part 3 of this Schedule are the sums receivable in respect of that year (whenever paid) or, in the case of sums not receivable in respect of a period, the sums paid during that year.

(2) But where

(a) any sums are not shown in the directors' remuneration report for the relevant financial year on the ground that the person receiving them is liable to account for them as mentioned in paragraph 19(2), but the liability is thereafter wholly or partly released or is not enforced within a period of 2 years; or

(b) any sums paid by way of expenses allowance are charged to United Kingdom income tax after the end of the relevant financial year or, in the case of any such sums paid otherwise than to an individual, it does not become clear until the end of the relevant financial year that those sums would be charged to such tax were the person an individual, those sums must, to the extent to which the liability is released or not enforced or they are charged as mentioned above (as the case may be), be shown in the first directors' remuneration report in which it is practicable to show them and must be distinguished from the amounts to be shown apart from this provision.

21. Where it is necessary to do so for the purpose of making any distinction required by the preceding paragraphs in an amount to be shown in compliance with this Part of this Schedule, the directors may apportion any payments between the matters in respect of which these have been paid or are receivable in such manner as they think appropriate.

22. The Schedule requires information to be given only so far as it is contained in the company's books and papers, available to members of the public or the company has the right to obtain it.