Why work?

Sir James Foots must have been an abysmally poor chief executive. He had no STI, LTI, options, performance rights or publicly-disclosed KPIs. It's a wonder he bothered coming to work.

John Robertson* | 13 Oct 2016 | 9:02 | Opinion

Former MIM Holdings head, Sir James Foots, might be disgusted at the rewards on offer as a small company chief today

Sir James was managing director of Mt Isa Mines and, subsequently, chief executive and chairman of MIM Holdings between 1966 and 1983.

For a brief time during his tenure, MIM Holdings was one of the two most valuable corporate entities, along with BHP, listed on Australia's stock exchange.

At the end of the 1970s, Sir James was described by one newspaper as being the highest-paid chief executive in Australia. To reach this dizzying height, the paper reported, Sir James received an annual salary of A$100,000 (US$110,000).

Since executive remuneration went undisclosed in those days, there are no official records on this point.

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My recollection is consistent with a research paper by Mike Pottenger and Andrew Leigh ('Long Run Trends in Australian Executive Remuneration: BHP 1887-2012'). Pottenger and Leigh concluded that the BHP chief executive at the end of the 1970s earned around six or seven times average Australian earnings. That would imply payments between $85,000 and $100,000 a year.

Inflation adjusted, Sir James' reported salary would be equivalent to $410,000 today. This is still a chunky sum but well short of what the head of a current day large company could command and not much different to the salaries of many modern run-of-the-mill miners.

Thoughts about Sir James resurfaced as I trawled through dozens of annual remuneration reports from Australian mining companies released in the past few weeks.

The reports have grown in size and complexity. Many pages are now needed to explain increasingly complicated multilayered payments and incentive schemes involving cash and different forms of securities.

> *"Reluctant executive needs to be enticed, mollified and continually entreated to stay"*

Recognising the difficulty, some companies offer colourful diagrams to helpfully guide readers through the remuneration maze.

With so much scrutiny, surely everyone is now pulling their weight.

The latest reports show that the annual base salary of executives heading up the mining companies in the ASX small resources share price index averaged slightly over $771,000.

The heads of these 33 second tier companies reporting under the Australian corporations law (excluding a small number of service providers and other non-mining entities included in the index) are getting nearly twice what Australia's most expensive executive received in the late 1970s.

The base amounts only include what today's executives are paid for turning up. These payments do not include the additional benefits 'to better align their activities with the interests of shareholders', to use the now universally adopted corporate catchphrase.

Under Australian law, companies must also identify and report on payments made to their 'KMP' or key management personnel. Average company payments in all forms to directors and senior executives of the small resources companies were $4.6 million.

Companies usually define 'shareholder interest' in terms of higher share prices. In practice, payments bear little resemblance to market capitalisation.

In the cases of both the individual chief executives and the combined executive groups, the correlation between payments and market values is a lowly 9-10%. In other words, for all the effort, there has been no material connection.

The size of the KMP packages varied from a modest $1.2 million to as much as $14.6 million.

The company at the top end of the scale is Pilbara Minerals, where the bulk of the nearly $15 million in value went as vested options without any cost to the recipients and with "no performance conditions prior to the grant or exercise of the options".

Options valued at $6.7 million gifted to directors Neil Biddle and Tony Leibowitz "reflected the significant contribution made by them in raising capital for the company".

The Pilbara accounts show that the company raised $114.6 million through new equity during the year from which $7.021 million was deducted as expenses.

The effective Pilbara funding costs, after the Biddle and Leibowitz reward, jumped to well over 10% of the capital raised.

Euphoria over lithium lubricated this gravy train.

In theory, holding options provides a spur to work a little harder and more innovatively for shareholders. It is often referred to as “skin in the game”.

In this instance, one can be sure the theory will not hold. Leibowitz resigned from the board with effect from 1 July 2016. Biddle ceased being an executive on 19 August.

Another aspect of the Pilbara Minerals arrangements that catches the eye is the board composition.

Typically, a board at this level comprises one or two executives and four or five non-executive directors. The actual average number of executive and non-executive directors among the companies reviewed was 1.45 and 4.48, respectively.

Again, Pilbara Minerals is an outlier.

During the year, Pilbara had two directors (including Leibowitz) designated as non-executive facing three executives. The company’s defiance of corporate governance best practice made it unique among its peers in the small resources index.

Let’s be clear. Without sufficiently enticing rewards for Messrs Biddle and Liebowitz, the as yet undeveloped Pilgangoora lithium mine might have never stood a chance. They would have stayed home. Their flourishing gardens would have bloomed brightly as their shareholders suffered.

The idea of the reluctant executive with better things to do underpins the remuneration paraphernalia now demanded by the law and welcomed so enthusiastically by the lawyers and accountants paid to compose the burgeoning compliance reports.

The reluctant executive needs to be enticed, mollified and continually entreated to stay. Cash and equity options are the tools.

Sir James, on the other hand, believed passionately in the ability of the mining industry to enhance the welfare of all Australians. He saw himself as doing his bit for the country.

He had a strong work ethic. He wanted to build sustainable communities for his workers. He felt an obligation to deliver results for those paying his salary.

Strange fellow! There’s no explaining some people.

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