

## Parliamentary Joint Committee Corporations & Financial Services Inquiry into Shareholder Engagement and Participation

### Question on Notice – Shareholder Voting Process

AICD's submission to the Inquiry into Shareholder Engagement and Participation addresses a number of matters about the shareholder voting process. These are expanded below, and cross-referenced to other related submissions to the Inquiry. This responds to questions at the public hearing in Sydney on 16 May 2008 from Senator Murray (page 67 of the *Hansard*).

#### 1. Introduction

This response to Senator Murray's question on notice concentrates on the voting process, voting methodologies, the discretion exercised by chairmen over which voting method to employ and how proxies are voted and their outcomes declared to shareholders. It considers whether the voting process facilitates shareholder participation in corporate governance.

Voting occurs within the context of annual general meetings but AICD's response to Senator Murray does not address general issues relating to the AGM and its effectiveness. AICD's main submission covers specific options about the future of the AGM under the term of reference relating to the conduct of annual general meetings. One of the options canvassed looks at whether voting should be decoupled from the information elements of AGMs. AICD refers the Committee to the main submission for further information on this and other options affecting the future of AGMs.

#### 2. Proxy Voting Processing

Proxy voting permits shareholders who do not attend an annual general meeting to participate in the corporate governance of the company. The alternative is to attend in person.

Proxy voting is currently the preferred method of voting for institutional shareholders and their agents.

AICD does not have fundamental concerns about continuing to use a system of proxy voting but supports proposals aimed at improving its administration.

- Problems can arise with processing the proxy votes of institutional shareholders because beneficial ownership is dynamic and complex at an institutional level and administrative systems in the back offices are not keeping pace with the sophistication of the financial markets. For example the

processing chain can move from electronic to paper-based processing and back to electronic, with associated delays and opportunities for error.

- IFSA's submission to the Inquiry provides an excellent analysis of these administrative problems and suggested solutions. AICD contributed to this work as part of an Industry Roundtable and supports its recommendations for electronic processing of proxy votes.
- AICD's supplementary submission to the Inquiry for improving the tracing of beneficial ownership of securities by amending Section 672 A to D of the *Corporations Act 2001* would also assist by making it easier for share custodians to verify that an entitlement to vote exists. This verification is required before a vote can be processed and requires complex matching between beneficial ownership and the proxy holders. Where the entitlement cannot be established before the legal cut-off date for voting in advance of an AGM it can lead to votes being disqualified, sometimes in large quantities. (Votes can be bundled and submitted in bulk by proxy holders rather than being grouped according to the beneficial owner. This gives rise to the potential for all votes in the bundle being discarded when voting rights are not established for a sub-set of that bundle.)
- AICD supports the practice of companies stating their policy for handling cases where voting rights and intentions are not reconciled by the legal cut-off date for proxies before a general meeting.
- IFSA's submission recommends changing the Corporations Act and ASX Listing Rule to extend the legal cut-off date to give more time for verification of voting rights in advance of AGMs. AICD endorses these recommendations.

### **3. Polls and Direct Voting**

It is important for companies to retain the flexibility to choose the voting process that meets their current needs and circumstances.

It is reasonable for chairmen to exercise discretion about which voting method to employ according to the circumstances. In doing so, chairmen have an obligation to ensure that the majority view of the total shareholdings is reflected. Shareholder perceptions of fairness and transparency are important and chairmen need to be mindful of such perceptions with the voting process they select and how they communicate the outcomes to their shareholders.

- Routine and non-controversial matters will typically be settled by a show of hands at the AGM, in the interests of efficiency.
- Controversial matters might be settled by a poll conducted separately from the meeting to reflect the views of all shareholders intending to vote. A poll includes direct votes and proxy votes as well as the votes of shareholders who are present at the AGM (usually retail shareholders).

- Calling a poll is time consuming and may delay notification of voting results until after the meeting. For this reason some chairmen may rely on other approaches provided that the result reflects the majority view: a combination of proxies and direct votes lodged before the meeting, plus a show of hands at the meeting or determination by proxies and direct votes alone if the mood of the meeting departs from the majority view.

Direct Voting, supported by new technologies, could remove the need to appoint a proxy where the shareholder is unable to attend the AGM. It could give absent shareholders the option of completing a voting form lodged by post, fax or electronically. This would mainly assist retail shareholders. Few institutional investors attend the AGM, relying on proxy voting and special briefings to interact with companies and their chairmen.

- AICD supports direct voting as providing another option for shareholders to exercise their voting rights and participate in company affairs. AICD sees direct voting as being complementary to the proxy voting process and part of a suite of opportunities for shareholder engagement.
- The submission by CSA to the Inquiry outlines a comprehensive proposal for direct voting, which AICD supports.
- Direct voting would not, however, remove all vote processing problems that are identified above for the institutions. Verification would still be required for direct voting entitlements. The logistics of electronic processing for a large volume of votes from institutional investors would still be required, whether it be for direct voting technology platforms or proxy voting technology platforms.
- Companies will make individual judgements of the benefits of implementing direct voting depending on their mix of shareholders and the number of retail shareholders. Company constitutions may need to be amended and this will not be a high priority for companies with a predominance of large institutional shareholders.
- Implementing a system of direct voting to assist a relatively small number of retail shareholders is likely to be addressed progressively over time.

#### **4. Shareholder Participation in Voting and Chairmen's Discretion**

Does proxy voting impede shareholder participation in corporate governance?

- Chairmen exercise discretion at AGMs about how the voting will be taken but they have an obligation to ensure that the majority view of the total shareholdings is reflected.

- Shareholders have a right to oblige their proxy to vote (in accordance with agency law) and it is not necessary to impose a legal obligation on all proxy holders to vote.
- Shareholders who direct their proxies to the chairman can be confident that their voting preferences will be exercised by the chairman at the meeting. It is regarded as a good practice for chairmen to exercise their proxies as instructed. If a chairman did not exercise proxies and this inaction improperly influenced the outcome of a vote, then the resolution may be open to challenge in the courts on the grounds that the chairman was in breach of duty.
- AICD is not aware of any systemic problem of ‘cherry picking’ of votes by chairmen. Cherry picking refers to the practice of voting some but not all the shares covered by the proxy.
- Some shareholders choose not to give voting directions to the chairman because they respect the chairman’s judgement and better knowledge and information about the circumstances. Under current legislation the chairman retains discretion as to whether, and how, to vote open-ended proxies that do not give instructions. The chairman must exercise these open-ended proxies in the best interests of the company. If shareholders are unhappy with the outcome they can direct their votes on future occasions and/or vote against the chairman’s re-election to the board.
- AICD supports the practice of companies stating their policy for handling unclear proxy forms, where judgement is exercised in determining the voter’s intentions because the voter has not made their election clear on the form.

## **5. Declaring proxies at AGMs**

The use of proxies raises issues of how voting results should be declared at AGMs.

- AICD recommends that decisions about when to declare the proxy results at an AGM are best left to individual chairmen in the context of each meeting. The mood of the meeting and the matters being resolved will all have a bearing on that judgment and it is not something that is suited to regulation or one-size-fits-all. The pros and cons of different approaches are addressed in AICD’s main submission under the Inquiry’s terms of reference regarding conduct of annual general meetings.
- AICD believes that shareholders who give a proxy should retain the right for their voting intentions to remain private. It is a matter for voters to decide whether or not to reveal their preferences.
- AICD supports the suggestion from IFSA for aggregated voting information to be disclosed, such as the number of votes lodged for/against/abstain for each

resolution at general meetings, including the votes as a proportion of issued capital.

## 6. Advisers, agents and intermediaries

Finally, proxy voting is delegated by institutional shareholders and impedes the dialogue between the company and the beneficial owner.

- Most institutional shareholders, such as superannuation funds, rely on advisers, agents and industry associations to provide advice on proxy voting.
- Companies would like to be offered more opportunities by these intermediaries to discuss their conclusions before that advice is given to institutional investors. This would allow companies to correct misunderstandings about their proposals and to review the resolutions in advance of an AGM if they accept that a problem has been identified.
- As an example it is currently very difficult for a company to offer its institutional shareholders an informed response to an external assessment by these agencies. This has significant implications for the vote on the remuneration report of a company, which has proved to be a contentious matter between companies and intermediaries since the introduction of the non-binding shareholder vote.
- For this reason AICD would not recommend extending the non-binding shareholder vote to cover other matters where decisions are made by company boards.

## 7. Closing Remarks

Any suggestions for improving the voting process need to address both the mechanism for voting and the underlying incentives for shareholder participation. AICD suggests that the starting point is to improve the standard of engagement both at the AGM and by other means.

- Companies are assisted with these objectives by advances in technology.
- AICD's main submission addresses different options in detail under the Inquiry's terms of reference regarding conduct of annual general meetings and the effectiveness of existing communication and feedback mechanisms.

AICD does not see legislative or regulatory change as the main avenue for supporting shareholder engagement and participation.

- However improving the tracing of beneficial ownership of securities by amending Section 672 A to D of the *Corporations Act 2001* would assist

the processing of votes for institutional shareholders by making it easier for share custodians to verify that an entitlement to vote exists.

To conclude, AICD does not have fundamental concerns about continuing to use a system of proxy voting but supports proposals aimed at improving its administration.

It is important for companies to retain the flexibility to choose the voting process that meets their current needs and circumstances.

It is reasonable for chairmen to exercise discretion about which voting method to employ according to the circumstances. They have an obligation to ensure that the majority view for total shareholdings is reflected in the decision.

Shareholder perceptions of fairness and transparency are important and chairmen need to be mindful of such perceptions with the voting process they select and how they communicate the outcomes to their shareholders.