



# Identifying lobbying strategies: An analysis of public responses to the Productivity Commission Inquiry into executive remuneration in Australia

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## ABSTRACT

This study investigates lobbying behaviour over the two phases of the 2009 Productivity Commission Inquiry into executive remuneration within Australia. Consistent with expectations, behaviours appeared related to preference for change, the costs of regulatory change relative to those of lobbying, and the need for reputational capital. Industry participants, and those from the Representative and Professional bodies emerge as key opponents. Industry presented in a conciliatory manner during the first phase, revealing a preference for the status quo, but then directly targeted specific recommendations of concern, notably the ‘two strike’ and ‘no vacancy’ rules in the second phase. Respondents from the Representative and Professional Bodies were broadly and consistently supportive of change and the Inquiry’s final recommendations. We also find that these recommendations largely align with the views of the Representative Bodies, but conflict with those expressed by Industry in their second phase submissions. Finally, we find no evidence to suggest the motivation behind Industry lobbying related to poor remuneration practices.

## 1. Introduction

To date, research into lobbying activities surrounding the standard setting process has largely focused on the economic motivation for participation (see Section 3). Further, it has typically involved an analysis of respondents’ inputs in the cross-section, comparing stated positions at a point in time. Against this backdrop, Leuz and Wysocki (2016) highlight the need for research that focuses on the political process by which regulation arises, arguing that ‘understanding the rule-making and standard-setting process is important for the evaluation of regulatory outcomes.’ (p. 601). Equally, Amershi et al. (1982) argue that ‘rational political behaviour appears to be qualitatively different in a single-period than in a multi-period model.’ (p. 20). They propose that in a multi-period context, a setting that most closely describes most standard-setting or regulatory processes, public consultation provides lobbyists with the opportunity to strategically ‘vote’ on critical issues in an attempt to influence the outcome and/or to protect their reputation.

In response to the challenges posed by Leuz and Wysocki (2016) and Amershi et al. (1982), we seek to extend our understanding of strategic lobbying behaviour and its impact on regulators by documenting the activities of respondents during the Australian Productivity Commission Inquiry into executive remuneration regulation (hereafter, the Inquiry). Executive remuneration in

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<sup>1</sup> This work is based on the first study in Stacey Beaumont’s PhD thesis.

Australia has been subject to intensified scrutiny since the Global Financial Crisis (GFC) and several high-profile corporate collapses in the early 2000s. “S[ignificant] community concern about excessive pay practices” (Swan, 2009) and the role of executive remuneration as a possible contributory factor in these market failures prompted the Government to instigate a review of the regulatory arrangements applicable to executive remuneration.

The Inquiry was commissioned in March 2009 and its final report published in January 2010. As conducted, it provided for two distinct phases of public consultation, the first following its commission and the second following the release of its Discussion Draft at the end of September 2009.<sup>2</sup> Public response is well documented, and took the form of written submissions, public hearings, visits, and round table discussions. As an indication of public interest, there were 105 written submissions made during Phase 1 and 65 during Phase 2.

In the end, the Inquiry concluded that boards lacked accountability in reporting their remuneration arrangements. However, rather than a strengthening of disclosure requirements, the Commission instead recommended the introduction of a mechanism designed to force boards to meet shareholders’ expectations around disclosure and accountability. This mechanism, the controversial ‘two strikes’ (‘say on pay’) legislation, was the first of its kind globally and is unique in that relatively low levels of shareholder votes against the remuneration report may result in a full board spill and re-election process. Ultimately, the Commission’s final report precipitated changes to the legislation governing remuneration practices for Australian listed companies, notable among which was the adoption of the two strikes legislation.

We contend that the Inquiry is well suited for an investigation into the nature of lobbying activity surrounding the setting of standards and regulation, and has the potential to offer insights that are broadly applicable. Murphy (1999) argues that the structure and level of executive remuneration is influenced by both public opinion and politics, and Howieson (2011) describes the considerable political pressure that regulators contend with. Further, the two-stage consultation process used during the Inquiry loosely reflects the ‘unknown preferences game’ proposed by Amershi et al. (1982). Finally, Scott (2015) argues that where information is seen as a ‘complex and important commodity’, the determination of appropriate disclosure regulation is an ‘extremely complex issue of social choice’ and necessitates a rigorous ‘due process’ to inform standard setters (p. 26). Here, the Inquiry was conducted based on formal procedures, with its ‘due process’ resulting in the preparation of a comprehensive report based on public consultation. Early evidence from Monem and Ng (2013) indicates that the two strikes rule had an impact on the pay-performance link. Similarly, Grosse et al. (2017) find that firms respond to a strike by decreasing the discretionary bonus component of CEO pay and increasing remuneration disclosure. As such, we argue that examination of the public response to the Inquiry has the potential to provide insights into how various parties attempted to influence outcomes through their implementation of a lobbying strategy and thereby provides a unique setting for an analysis of respondent strategic ‘voting’ behaviour within a political standard or regulation setting context.

As the basis for our analysis, we follow Coombes and Stokes (1985) and Tutticci et al. (1994) and classify respondents into six groups (Industry, Individuals, Representative Bodies, Professional Bodies, Academics, and Government), arguing that the incentives to lobby will differ across the groups. These groups, which are the groups identified by the Australian Accounting Research Foundation (AARF) in the Australian Accounting Standards Board (AASB) Policy Statement 1 are described in Appendix A. To provide context, in Section 4 we develop expectations regarding the likely lobbying behaviour of each group, arguing that their incentives will depend on three key factors: the preference for the status quo relative to change (Chung, 1999); the expected cost of change versus the cost of lobbying (Mathur and Singh, 2011); and the importance of reputational capital (Bamber and McMeeking, 2016).

In terms of design, Leuz and Wysocki (2016) argue that qualitative approaches are an important step in comprehensively evaluating the net benefit of disclosure regulation. Given the difficulties associated with computer-based content analysis techniques highlighted by Loughran and McDonald (2016), we follow Miles and Huberman (1994) and conduct iterative, layered qualitative analysis to identify the characteristics and activities of lobbying behaviour. Specifically, we consider participation, preferred outcome and voting tactics, conducting the study in five stages: (1) documentation of activity across the two phases of the Inquiry; (2) documentation of the views expressed within the written submissions to each phase; (3) comparison of the content and tone of written submissions from respondents who made submissions during both phases; (4) documentation of the alignment between the expressed views of the respondent groups and the Inquiry’s final recommendations; and (5) an analysis of the remuneration practices of firm’s making written submission during both phases.<sup>3</sup>

Consistent with expectations, our analysis reveals differences in lobbying behaviour across the six groups. While most made their initial contact during the first phase, activity during the second phase was greater by respondents from Industry, and the Representative and Professional bodies. The groups also relied on different medium, with Individuals and Academics extensively relying on written communication while respondents from the Professional Bodies also made use of public hearings and the industry group made use of the roundtable forum.

Continuing, the written submissions made during Phase 1 reveal predictable differences in views. For example, Individuals consistently expressed the need for change whereas Industry respondents appeared largely comfortable with the status quo. The submissions made during Phase 2 then reveal that the groups reacted quite differently to the Discussion Draft, with respondents from the Representative and Professional bodies broadly supportive but those from Industry narrowly targeting specific recommendations

<sup>2</sup> The Inquiry was commissioned on 19 March 2009. Submissions during the first phase were due by 29 May 2009, although eight were received after this date. The Inquiry’s Discussion Draft was released on 30 September 2009 and the due date for submissions in response to the draft recommendations was 6 November 2009. The final report was released on 4 January 2010.

<sup>3</sup> We also recognise the caution by Booth and Cocks (1990) and Königgruber (2010) that identifying critical issues and predicting behaviour in what is essentially a political process is challenging due to the unobservable and conflicting interests of respondents.

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