Grant outcomes for: AFAANZ 2019 Research Fund

Category: Mentoring developing researchers

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Project Title: Nomination Committees in Australia

Project Summary:

Corporate governance guidelines in Australia recommend corporate boards establish 3 committees; an audit, a remuneration and a nomination committee. While prior research has considered the structure and consequence of remuneration and audit committees, we know relatively little of the nomination committee. This study addresses this gap by examining which companies have established nomination committees, how they are structured, and importantly, whether the establishment of a nomination committee leads to the appointment of more qualified and experienced non-executive directors.

This research provides novel information to address outstanding questions regarding the adoption and effectiveness of nomination committees in Australia. First, we provide evidence related to the number of companies in Australia that use a nomination committee as a distinct committee as opposed to a dual-purpose committee, for example, combined with the remuneration committee. Next, we examine whether nomination committees are composed in accordance to ASX guidelines, and where firms have chosen not to establish a nomination committee. We then provide evidence that a powerful CEO can influence a firm to not establish a nomination committee. This gives support to the managerial power perspective (Bebchuck & Fried, 2004) and posits that powerful CEOS are reluctant to relinquish control over the director selection process.

Finally, we examine whether nomination committees meet their objectives set by the ASXCGC, namely, to provide a mechanism for overseeing the selection and appointment of new directors (Hutchinson et al., 2015). Our focus here is on the formal qualifications, backgrounds and industry experience of appointed non-executive directors. We select these attributes by drawing on prior research that has found professional qualifications provide boards with the skills needed to oversee

management (Hambrick et al., 2016) while industry experience enhances the board's ability to identify and prioritise risks and opportunities (Kor & Misangi, 2008).

There has been no variation between the project undertaken and the original application, although the data collected has allowed for the research to adopt a wider scope. As a a consequence we also examine not the diversity of boards – with and without established nomination committees – by focusing on the skill-mix and tenure spread. As anticipated in the original application, the outcomes of this study have widespread implications and benefits to boards and policy makers by providing evidence of the value establishing a nomination committee brings to firms.

Funds Granted $4,000

Expenditure against budget items

Expense item	Actual	Budget
Employee costs	$3,995.05	$4,000

Outcomes

The main outcome of this research has been to compile two related data sets. The first summarises all firms listed on the ASX in 2018, which of these firms have nomination committees, the structure and characteristics of all nomination committees and the governance characteristics of firms with and without nomination committees. A second database details the qualifications, backgrounds, tenure and experience of all non-executive directors serving the firms of listed Australia boards during 2018. From this data two research projects have been made possible with one working paper completed and a second research paper underway. Details of each are below.

Output 1: Nomination committees in Australia and the influence of powerful CEOs

Status: Working paper

Abstract: In this study, we examine the prevalence and characteristics of nomination committees on Australian corporate boards and, given its voluntary context, we question what drives some firms to establish a nomination committee while other firms choose not to. Our analysis suggests that boards utilise nomination committee for efficiencies with dedicated nomination committees most prevalent amounts larger firms. While nomination committees are also adopted by smaller firms, committee membership is more likely to be shared with another board committee, such as the remuneration committee. Meanwhile firms with a powerful CEO are less likely have an active nomination

committee, supporting the managerial power perspective that powerful CEOs can influence board actions.

Future intentions of this project: Journal submission to Accounting & Finance, expected timing December 2020.

<u>Output 2</u>: Nomination Committees and Board Composition

Status: Data collected; analysis underway

Description: This project examines the extent to which firms that establish nomination committees have more diverse and qualified boards. We do this by testing the following three hypotheses:

> *H1: Adoption of the ASX nomination committee recommendations is associated with higher formal qualifications*
>
> *H2: Adoption of the ASX nomination committee recommendations is associated with more diverse boards*
>
> *H3: Adoption of the ASX nomination committee recommendations is associated with a greater spread of tenure amongst directors*

Future Intentions for this project: Conference submission to AFAANZ conference, 2021

Summary of Outcomes and Benefits:

There are three main benefits derived from this research and that are of value to researchers and regulators. First, prior research of nomination committees in limited by its narrow focuses on the largest listed firms. This research extends this knowledge by examining all listed firms.

Second, by showing an association between firms with powerful CEOs and the non-adoption of ASX recommendation to establish a nomination committee, our findings support an argument to mandate nomination committees under the ASX listing rules, as is the case for the audit and remuneration committees.

Finally, the results of our second paper, which is in progress, will be beneficial regardless of whether we show an association between director qualification's, diversity and tenure spread, and the nomination committee. If no association is shown, this provides insight for regulators to reconsider their recommendations of nomination committees. If we show observable director qualifications and experience is associated with nomination committees, this provides evidence to those not using nomination committees to adopt these committees.

References:

Bebchuk, L., & Cohen, A. i J. Fried 2004. *Pay Without Performance: The Unfulfilled Promise of Executive Compensation.*

Hambrick, D. C., Misangyi, V. F., & Park, C. A. (2016). The quad model for identifying a corporate director's potential for effective monitoring: Toward a new theory of board sufficiency. *Academy of Management Review*, 40(3), 323-344.

Hutchinson, M., Mack, J., & Plastow, K. (2015). Who selects the 'right'directors? An examination of the association between board selection, gender diversity and outcomes. *Accounting & Finance*, *55*(4), 1071-1103.

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