OWNERSHIP MATTERS

Suite 4, Level 5, 167 Queen St, Melbourne VIC 3000 **T** +61 3 9602 4548 **www.ownershipmatters.com.au**

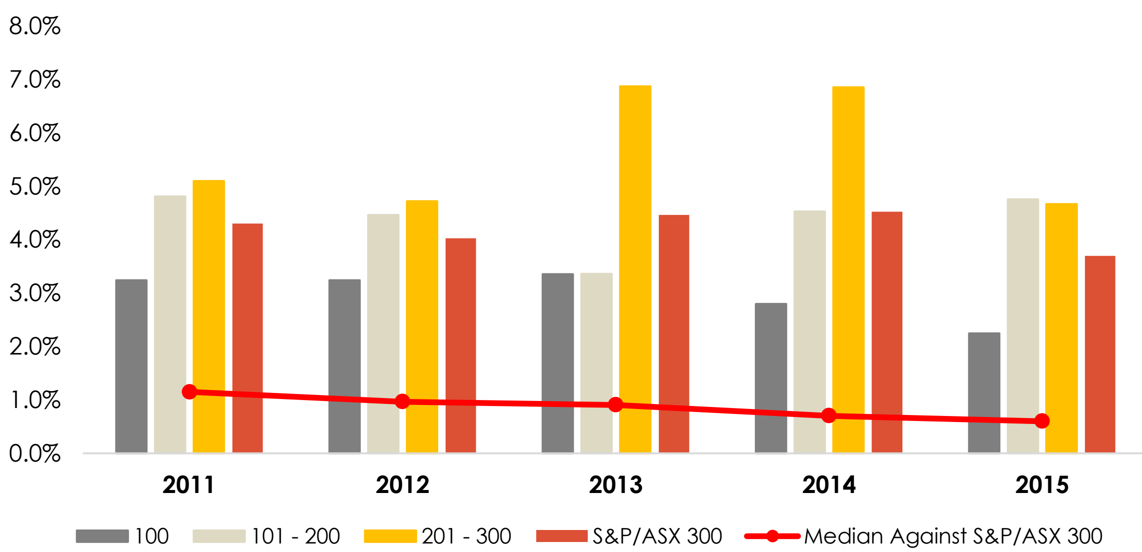
A MODEST REVOLT

In 2015 the flickering signs of investor willingness to oppose board-endorsed directors (noted in 2014) became more visible: At Origin Energy, Bradken & Villa World incumbent directors resigned immediately prior to the annual meeting presumably in the face of significant investor opposition (vote results were never disclosed). The number of 'strikes' on remuneration report resolutions also increased slightly, from 16 across the S&P/ASX 300 in 2014 to 19 in 2015. The ongoing phenomenon of management narrowly avoiding defeat also continued.

Shareholders show willingness to challenge directors

Graph 1 below shows most S&P/ASX 300 board endorsed candidates are almost guaranteed to be elected.

Graph 1: Average votes against management on directors 2011 – 2015[1]



The slight improvement overall shown in director margins of victory in 2015 however masks the fact that 2015 saw an unprecedented four board endorsed directors resign immediately prior to the annual general meeting. These directors – Origin's finance director Karen Moses, Bradken non-executive directors Eileen Doyle and Peter Richards and Villa World's audit committee chair Gerry Lambert – all presumably resigned rather than face significant votes against their reelection. As the vote results for these individuals were never disclosed this

[1] All aggregate vote result data for 2011 is from 1 July 2011 unless otherwise stated.

data is excluded from graph 1. Common to all three cases were significant concerns either over company or individual performance: Origin's AGM followed shortly after a disappointing annual result and capital raising as part of a strategy to trim its burgeoning debt levels. The Bradken AGM came at a time when the board had rejected a takeover proposal only to shortly afterwards renegotiate debt covenants and issue preference shares to reduce debt. At Villa World, Lambert had previously been a long-serving director of would-be copper producer CuDeco which had raised capital via selective placements while conducting share buybacks.

These defeats followed 2014 when Cabcharge, another company with a number of frustrated investors, announced the resignation of a newly appointed non-executive director immediately prior to the AGM. Historically it has been rare for board endorsed directors to be defeated at ASX companies, absent disputes with major strategic investors.

In 2015 there were further examples of the ability of strategic holders, as opposed to other investors, to bend boards to their will. At AusNet Services a dispute between directors not aligned with major holders Singapore Power and State Grid saw incumbent non-executive director Tony Iannello voted from the board (as seen below, it also saw other resolutions defeated or incur significant votes against). At Cardno, at an AGM which coincided with a disputed proportional takeover offer from a consortium led by a private equity firm, all board endorsed directors suffered significant against votes (a slight increase in the offer following the AGM saw the board endorse the bid).

As graph 1 suggests however, the indignity of defeat or near-defeat was an unknown for most directors. In the 728 director election resolutions where data is available only eight directors received votes against of more than 40% - three at Cardno, two at Energy World Corp and three at News Corporation (excluding AusNet's Iannello).

The News Corporation results were similar to 2014 – half of the 12 directors had votes against of more than 30% (in 2014, 11 suffered this fate) and only three directors would have received a majority without the support of the Murdoch family's voting stake (in 2014 only one director would have received a majority without the Murdoch family's support). A non-binding shareholder resolution calling for an end to the dual class capital structure that gives the Murdoch family influence disproportionate to its economic interest at News Corporation was also narrowly defeated.

A similar story of a major shareholder shielding a board from defeat also occurred at Brickworks. A director candidate put forward by major shareholder Perpetual as part of its ongoing campaign against Brickworks' cross-shareholding arrangements with Washington H Soul Pattinson, would have been comfortably elected to the Brickworks board but for the votes of Washington H Soul Pattinson.[2]

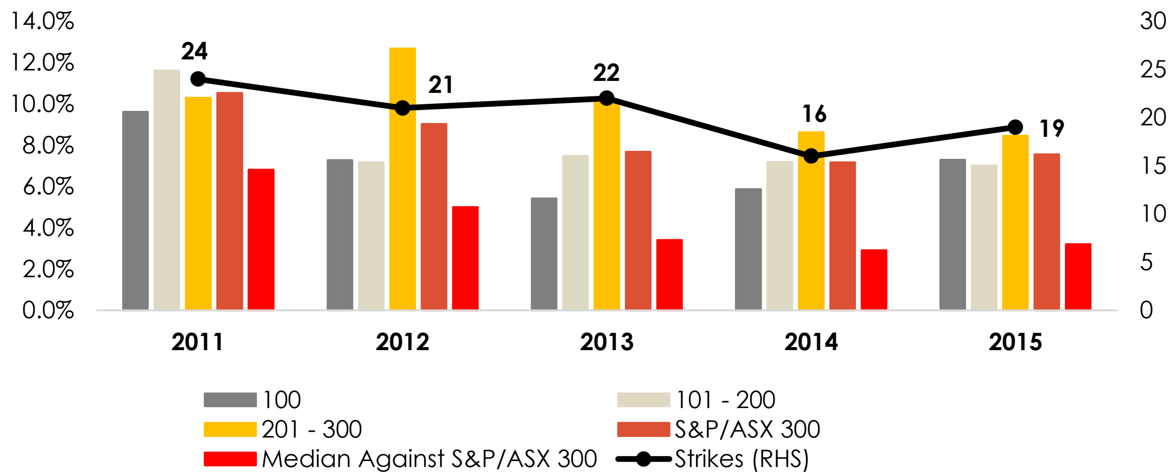
Striking similarities

The level of opposition to management on remuneration report resolutions in 2015 was consistent with 2014, albeit slightly higher. As graph 1 shows below, there were three more

[2] Soul Pattinson owns 44.2% of Brickworks which in turn owns 42.7% of Soul Pattinson. Robert Millner serves as chairperson of both entities and Michael Millner is deputy chair of Brickworks and Thomas Millner is on the Soul Pattinson board.

strikes on remuneration report resolutions in 2015 in the S&P/ASX 300 than in 2014 with two of these, at AusNet Services and Cardno, being due to disputes with major holders noted above.[3]

Graph 2: Average votes against on remuneration reports 2011 – 2015 in the S&P/ASX 300[4]



Consistent with the slight increase in opposition to management on remuneration reports, the median vote against rose for the first time since the year of the introduction of the 'two strikes' regime in 2011. Overall dissent levels however remained low, with the median against vote rising from 2.9% to 3.2%, still well below the median of 6.8% in 2011. The average no vote also rose, from 7.2% in 2014 to 7.6% driven by higher levels of opposition in S&P/ASX 100 companies where the average vote against rose from 5.9% to 7.3%, similar to opposition levels recorded in 2012. The number of remuneration reports outright defeated fell, from four in 2014 to three in 2015.[5]

There were three companies in 2015 that incurred a second strike and in every case the vote against their 2015 remuneration report was larger than in 2014: Mortgage Choice, UGL and Reckon. All three easily avoided the board spill resolution although UGL did see more than 20% of votes cast in favour of spilling the board.

---

[3] Under the two strikes regime, applicable to Australian listed companies since July 2011, a company that incurs a vote against a remuneration of 25% or greater (a first strike) must, the following year, include as part of its notice of annual meeting a conditional resolution. If put to the meeting and passed this resolution (the 'spill resolution') would require all directors (other than the CEO) in office at the time of the second remuneration report to resign and seek reelection at a separate general meeting. This conditional resolution is only put to the second AGM if the remuneration report at the second AGM incurs a vote against of 25% or more (a second strike). The spill resolution requires a majority to pass; key management – those whose remuneration is disclosed – may not vote on the remuneration report or spill resolutions.

[4] The aggregate vote data includes vote results on resolutions similar to remuneration reports required in other jurisdictions eg. the US 'say on pay' votes and the UK remuneration report, remuneration policy and remuneration implementation reports. Strikes include only those at Australian companies (and Dexus Property Group in 2011 which voluntarily submits to the governance regime of a listed Australian company).

[5] This brings the total number of S&P/ASX 300 remuneration reports defeated since two strikes was introduced in July 2011 to 13 to the end of 2015.

Table 1: 2015 strikes in the S&P/ASX 300

Company	Against vote (%)	Company	Against vote (%)
Tiger Resources Limited	68.7	Liquefied Natural Gas Limited	34.4
Arrium Limited	62.4	Prime Media Group Limited	34.2
Mortgage Choice Limited	**51**	Ansell Limited	33.2
UGL Limited	**45.1**	Premier Investments Limited	31.7
Webjet Limited	44.9	Village Roadshow Limited	31.5
AusNet Services Limited	41.2	Decmil Group Limited	31.2
Bradken Limited	40.7	ALS Limited	27.2
Cardno Limited	40.7	Downer EDI Limited	26.9
Pacific Brands Limited	39.9	Impedimed Limited	25.1
Reckon Limited	**36.8**		

Note: Companies in bold incurred a second strike.

Among the 2015 strikes, Premier Investments was this year's representative of a company that incurred a strike solely due to members of key management personnel being prohibited from voting on the remuneration report. Chairperson and major shareholder Solly Lew was unable to vote, and had he voted Premier would have been well short of incurring a strike given his associates hold approx. 43% of shares on issue.

At Village Roadshow however, which narrowly avoided strikes on its remuneration report in 2013 and 2014, the votes of 44% shareholder Village Roadshow Corporation (VRC) was unable to stave off a strike in 2015. An overwhelming majority of non-VRC shares voted against the remuneration report; VRC continues to vote on the report despite being jointly controlled by three Village directors – Robert Kirby, John Kirby & Graham Burke.

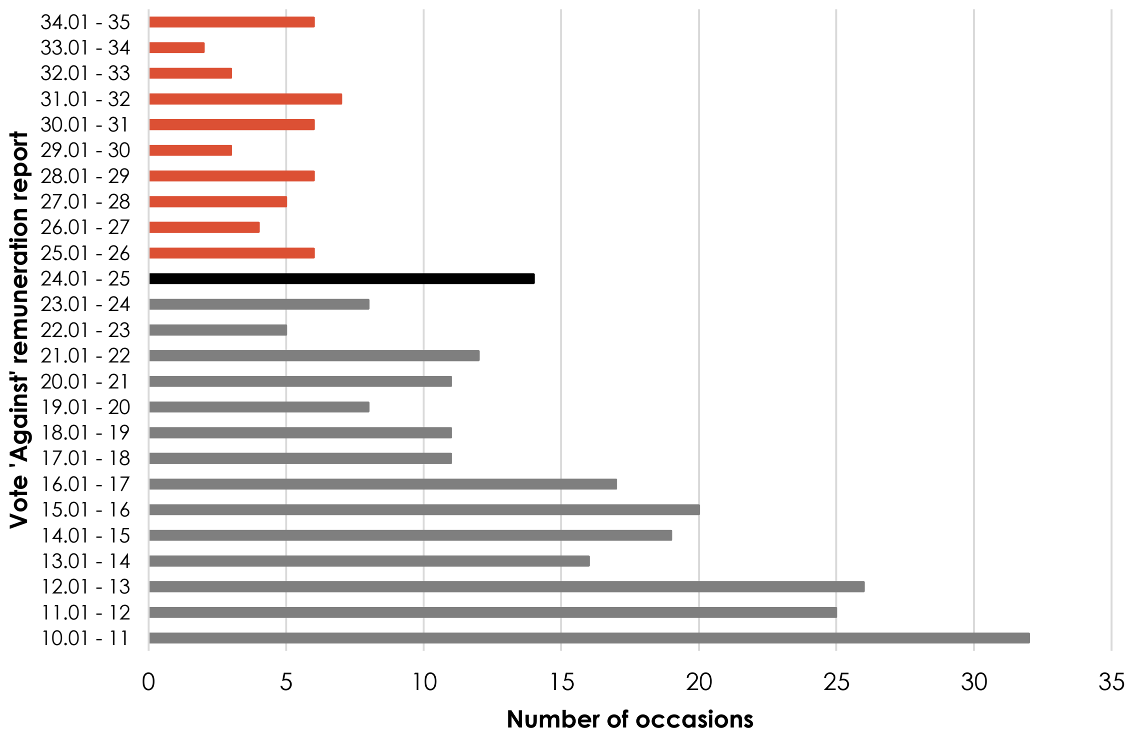
In 2015 there was again a 'bulge' of companies that narrowly managed to avoid a strike, consistent with findings since the two strikes regime began in 2011. As shown in graph 3, the most common result on a remuneration report since 2011 when the vote against is higher than 17% is a vote against of between 24% and 25%. In 2015 there were three companies that incurred votes against of between 24% and 25% and unusually, two were members of the S&P/ASX 100: Spark Infrastructure and Carsales (the other was Technology One which unlike the Top 100 entities did not put the resolution to a poll).[6] Another Top 100 company, Santos, recorded a vote against of 23.4%.

---

[6] Spark Infrastructure is not a company – its structure consists of a loan note stapled to a trust – but it has adopted the governance structure of a listed Australian company.

In 2015 one company, Impedimed, reported a vote against on its remuneration report of 25.1%, the narrowest defeat reported by a company on its remuneration report since the two strikes regime was introduced. Since July 2011, 14 S&P/ASX 300 entities have received votes against of between 24% and 25% while just six have received between 25% and 26%.

Graph 3: Incidence of votes 'Against' remuneration reports 2011 - 2015



The ability of management to avoid defeat in close votes is at least in part due to their information advantage, as OM has previously noted. Management are aware of the level of opposition as votes are lodged and through the tracing provisions of the Corporations Act are able to discover those shareholders voting against and lobby them directly to change their votes. Anecdotal evidence also suggests management continues to spend shareholder funds on 'proxy solicitors' – third party firms which assist management with securing shareholder support for management-backed proposals.

Defeated resolutions

Out of 1,437 non-remuneration report and spill resolutions in 2015 only 16 management resolutions were defeated or withdrawn due to likely shareholder opposition, up from 13 in 2014. Unlike 2014 however, where the resolutions where management was defeated were clustered around seven companies, with seven resolutions from Intrepid Resources alone, investor opposition was more widespread in 2015 with 10 companies featuring.

Table 2: Defeated or withdrawn resolutions

Resolution	Vote against management (%)	Vote to defeat management (%)	Withdrawn?
AusNet Services – approve director fee cap	80.6	50.1	No
CuDeco – approve shareholder options	71.9	50.1	No
Ansell – approve executive options	65.8	50.1	No
AusNet Services – placement approval	60.6	50.1	No
AusNet Services - director election	60.5	50.1	No
CuDeco – approve placement	51.9	50.1	No
Origin Energy – elect Karen Moses (CFO)	N/A	50.1	Yes
Origin Energy – equity issue to CEO	N/A	50.1	Yes
Origin Energy – equity issue to CFO	N/A	50.1	Yes
Bradken – elect Peter Richards	N/A	50.1	Yes
Bradken – elect Eileen Doyle	N/A	50.1	Yes
Villa World – elect Gerry Lambert	N/A	50.1	Yes
Spark NZ – approve director fee cap	N/A	50.1	Yes
Invocare – approve termination benefits	N/A	50.1	Yes
PanAust – approve termination benefits	N/A	50.1	Yes
Tabcorp Holdings – approve CEO equity	N/A	50.1	Yes

Source: Company disclosures & OM estimates.

Where resolutions are withdrawn there is always some doubt as to why, in the absence of explicit explanation. At Origin Energy, the company's decision to withdraw proposed equity incentive allocations to the CEO, Grant King, and CFO, Karen Moses, was announced on 7 October 2015, two weeks prior to the AGM and was described as a decision by the board and the two executives in recognition of Origin's debt reduction initiatives, including a major equity raising. The resignation of Moses was announced on the day of the AGM.

The resolution withdrawn by Tabcorp was a proposal seeking to 'compensate' the CEO for the diminution in value of his outstanding equity incentives as a result of the entitlement offer. At PanAust the AGM took place after the major shareholder had secured control of the company through a takeover offer and the resolution withdrawn involved approval to allow a former executive to retain unvested equity incentives subject to their original performance conditions.

There was however no doubt that the resolutions withdrawn at Invocare and Spark NZ were withdrawn in the face of shareholder opposition. At Invocare the company stated the resolution was withdrawn due to concerns over the termination benefits for the outgoing CEO, which involved automatic vesting of all long term incentives on foot when the CEO's contract was not renewed. At Spark NZ the company announced on 30 October 2015, a week prior to the AGM, that it would not put a proposal to modestly increase its director fee cap to the meeting in response to concerns from some shareholders.

Outside of the outright defeats at Ausnet, flagged above, the defeat of resolutions at CuDeco marked the end of the company's strategy of raising capital via selective placements and diluting existing holders. These defeats also sparked the exit of a number of board members including the founding executive chair, Wayne McCrae. At Ansell a proposed allocation of options to the CEO was overwhelmingly defeated by shareholders at an AGM held in the wake of a significant earnings downgrade.