

13 August 2010
John Kliver
Executive Director
Corporations & Markets Advisory Committee
GPO Box 3967
SYDNEY NSW 2001

CAMAC review of executive remuneration reporting requirements and framework: Ernst & Young submission

Dear John

Ernst & Young is pleased to provide this submission to the Corporations and Markets Advisory Committee ("CAMAC") in response to the Information Paper on executive remuneration released on 13 July 2010.

The Government, in response to the Productivity Commission's ("PC") final report on director and executive remuneration released in December 2009, has asked CAMAC to:

- ▶ Examine the existing reporting requirements contained in section 300A of the Corporations Act and related regulations and make recommendations to reduce the complexity of remuneration reports.
- ▶ Review the existing remuneration setting framework and make recommendations on how the incentive components of executive remuneration could be simplified.

Our views and comments are based on our experience working with Australian and overseas company Boards and management on a range of executive remuneration-related issues. Ernst & Young does not provide legal advice and consequently we defer to CAMAC, and the legal firms who provide submissions, regarding the best manner to implement any changes within the legislative framework.

In summary, our key views in relation to CAMAC's review are:

1. The remuneration reporting framework should be simplified by encouraging a consistent and logical structure for remuneration reports through a new recommendation in the ASX Corporate Governance Principles and Recommendations which specifies the sections and order for the report.
2. The items required for disclosure that increase complexity and do not add to the reader's understanding should be removed. Full details are contained herein.
3. The regulation of executive incentive arrangements is unnecessary and will prevent companies from being able to tailor their remuneration approach to their specific strategy and circumstances.
 - ▶ Different incentive plan approaches will be necessary for different companies, and possibly for the same company, as needs and priorities change over time. The Board, with its deep knowledge of the business, is best placed to exercise judgement in ensuring that remuneration structures are appropriate for a company's circumstances.

- ▶ Remuneration structures that are linked to company performance will naturally be complex given the complex nature of, and influences on, company performance. The design of remuneration structures reflects the need for companies to take into account business strategy, market practice, shareholder views, employee perspectives, management of risk and intricate tax, accounting and regulatory rules.
- ▶ While regulation of remuneration in the financial services industry has increased globally, the same level of regulation is not required for broader industry from a risk management perspective, and would limit companies' ability to tailor remuneration arrangements to suit their strategic needs.

However, we believe there are remuneration governance and process principles emanating from the Financial Stability Board's recommendations that have been applied in the financial services sector that are relevant for the broader industry and would benefit many companies.

4. Changes to the complex rules around equity awards may enable companies to simplify executives' incentives. Tax rules, in particular, give rise to significant complexity in the design of equity-based incentive plans and, in many respects, place Australia out of step with the majority of our international competitors.

Key suggested changes are:

- ▶ Removal of cessation of employment as a taxing point;
- ▶ Taxing share options at exercise rather than vesting; and
- ▶ Removal of the "75% rule" to allow tax deferral for grants of shares.

We trust the information and views provided in this submission are useful. We would be pleased to discuss any aspects of our submission in more detail at your convenience.

Kind regards,



Mike Hogan
Partner
Human Capital

Tel: (02) 8295 6853



Bruno Cecchini
Partner
Human Capital

Tel: (03) 9288 8423



Chris Galway
Partner
Human Capital

Tel: (02) 8295 6476

1. Simplification of remuneration report disclosures

1.1 Effectiveness of the current reporting framework

The remuneration reporting requirements in Australia are strong and effective relative to other developed nations. However, there is room for improvement.

In our experience, companies recognise that the remuneration report is the primary method of communicating their remuneration approach to shareholders. We have found that the following aspects of the current disclosure requirements, however, can hinder attempts to effectively explain executive remuneration approaches:

- ▶ **Utility of some disclosures:** Companies' ability to use the remuneration report to articulate their remuneration approach can be undermined by the large volume of mandatory disclosures. Several of the disclosures add length and complication to the report, without adding to shareholder understanding.

Examples include:

- ▶ The requirement to disclose five year earnings and total shareholder return performance in the link between performance and reward section: This requirement is poorly defined and may not align with the performance period and measures of the company's incentive plans. If this is the case, it solely serves to lengthen disclosures in a way that is not meaningful.
- ▶ Disclosure of the five highest paid executives (in addition to key management personnel ("KMP")): This disclosure introduces variability to year-on-year reporting in terms of who is disclosed, complexity regarding terminology and does not add information where there is overlap between the KMP and the five highest paid executives, which is common.

We note that the PC recommended the removal of this requirement.

- ▶ The percentage of remuneration consisting of share options: The purpose of this requirement is unclear. Its inclusion does not appear to add any insights for shareholders.
- ▶ **Potential misinterpretation of disclosures:** A significant issue for many companies is the requirement to disclose accounting values within the remuneration disclosure tables. These values do not reflect the value earned and delivered to executives, and can therefore mislead the reader. Despite this fact, the commentary frequently quoted in the wider media focuses on these accounting values and represents these values as "remuneration", which is mistakenly interpreted by the public as "take home pay", which it is not. This results in misleading reporting, and adds to the public's misconceptions regarding remuneration quantum.

We note that, in response to this issue, the PC recommended the additional disclosure of actual levels of remuneration received by the individuals named in the report (see section 1.2.2 for our suggestions on how this may be achieved).

- ▶ **The requirement and intent of some components of the legislation is unclear:** There are aspects of the current requirements that are unclear or ambiguous. The absence of a clear rationale for each of the disclosures can result in inconsistent interpretation of the requirements.

Examples include:

- ▶ The requirement to discuss the proportions of remuneration that are linked to performance and those that are not: This requirement is interpreted by companies in a range of different ways, including showing target remuneration mix, maximum remuneration mix, and actual remuneration mix (based on accounting values). Some companies describe the mix qualitatively while others list or illustrate by executive. The end result is that the disclosed information cannot be compared on a company by company basis.
- ▶ The method used to assess performance: This is often interpreted as being a requirement to explain the performance hurdles (which is in fact covered by a separate disclosure requirement), and is sometimes interpreted as explaining how the performance hurdles are actually assessed (e.g., using an external data provider to undertake the relative Total Shareholder Return assessment).

The problem of interpretation is particularly exacerbated for smaller listed companies who may not use remuneration or legal advisers to assist with interpreting the requirements when preparing the remuneration report.

1.2 Suggested “ideal” remuneration report

1.2.1 Structure and overview of content

A key differentiator that can make a remuneration report comprehensible to shareholders is a clear and logical structure that makes use of headings, tables and diagrams where relevant. Such a structure must be complemented by clearly marked disclosures which provide meaningful information to shareholders on the company’s remuneration approach and why this approach is appropriate, given the company’s context and business strategy.

The following suggested remuneration report template and content overview is intended to meet these needs¹:

Topic	Contents
Part A: Executives	
1. Overview / summary	<ul style="list-style-type: none"> ▶ Description of the company’s executive remuneration framework in terms of fixed remuneration and incentives, noting any key changes to the framework in the current year. ▶ Key details of current year approach: incentive payments (and vesting) and rationale, termination payments and rationale, and any one-off payments. ▶ Details of any expected reviews of, or changes to, remuneration structures in the coming year.
2. Remuneration strategy	<ul style="list-style-type: none"> ▶ Remuneration objectives, approach to quantum, approach to remuneration mix, key objectives of each remuneration element (e.g., fixed remuneration, incentives, retention payments) and details of any significant changes.
3. Incentive plans	<ul style="list-style-type: none"> ▶ Detailed plan descriptions, including overview of the performance measures in the plan, rationale for their selection, their weightings, targets and vesting schedules. An exception should be provided for targets that are commercially sensitive, which will typically apply only to plans with short-term performance targets, but may apply to other incentive plans that use company-specific commercially sensitive targets. ▶ Details of any outstanding equity grants (i.e., name of plan, grant date, award vehicle, number of instruments and vesting dates, but not the accounting value of the awards).

¹ Note: this “ideal” remuneration report is a refined version of our earlier submission to the PC.

Topic	Contents
4. Remuneration opportunity & contracts	<p>Summary of each executive's remuneration opportunity for the year:</p> <ul style="list-style-type: none"> ▶ Fixed remuneration (as at the start of the year and any amendments made during the year). ▶ Cash incentive opportunities (target and maximum, to the extent the company has specified opportunities). ▶ Equity incentive opportunities (expressed as a dollar value or a percentage of fixed remuneration with an explanation regarding how this is converted into a number of shares/rights/options). <p>Contractual information:</p> <ul style="list-style-type: none"> ▶ Length of contract, notice periods, sign-on arrangements, termination entitlements and details of any guaranteed payments.
5. Performance and reward link (including remuneration outcomes)	<ul style="list-style-type: none"> ▶ Table presenting current year and prior year individual remuneration data using "actual" values (see section 1.2.2 for discussion regarding the presentation of "actuals"). ▶ Summary of cash-based incentives paid in the year to each executive. This should include the amount of cash paid in relation to service over the year (i.e., excluding any deferral) and the cash value of any longer-term incentives or retention payments that were paid during the year. <ul style="list-style-type: none"> For the payments that relate to the current year performance, disclosure should include a high-level summary of the company and executives' performance against targets, the total payment earned (dollar value and as a percentage of maximum), and the split between immediate cash payment and deferral. For payments that relate to multi-years, disclosure should provide a summary of the incentives that was paid during the year, including an explanation of what period the amount relates to and how the value has changed over the period. ▶ Summary of current year share-based payment vesting by executive, including performance against the relevant hurdles, the number of awards that vested and the value of the vested awards at the date of vesting. ▶ Summary of the changes in each executive's company shareholdings (number of shares held) and dollar value over the year (split to show both (a) wholly owned shares, vested but restricted shares and vested but unexercised options; and (b) unvested equity awards). Value of equity to be based on share price at year-end less any exercise price (if applicable). ▶ Details of termination payments made in the current year, including a breakdown of the components of the payment and the rationale for the payment (with reference to contractual entitlements). <p>See Appendix B for an example of how a company may present the information described above.</p>
Part B: Non-executive directors ("NED")	
6. NED policy and outcomes	<ul style="list-style-type: none"> ▶ Description of the company's NED remuneration framework: fee pool, policy base fees, committee fees, benefits and participation in equity plans, noting any key changes to the framework in the current year ▶ Current year and prior year individual remuneration data using "actual" values

The above remuneration report would be supplemented by the Notes to the Annual Financial Report, which would include details of the aggregate accounting value of KMP remuneration outcomes (by remuneration element) and a description of the fair valuation methodology used for share-based payments.

1.2.2 "Actual" remuneration disclosures

As included in our template report, we support the disclosure of "actual" remuneration values. However, "actual" will need to be defined. For consistency, we suggest that all remuneration values (not just share-based payments) be disclosed on an "actual" basis. To the extent that definitions for each element are not specified, there is the risk that inconsistencies in approaches will lead to a reduction in comparability of amounts disclosed by different companies. This has already been evidenced by the difference amongst companies who have voluntarily disclosed this information.

We suggest the following definitions:

Remuneration element	Definition (note all values are pre-tax)
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Fixed remuneration	Fixed amounts (i.e., salary, superannuation and other benefits) for the 12-month period ² .
Cash incentives paid (split into plans operated by the company*)	Amount of cash paid in relation to service over the year (i.e., excluding any deferral) and the cash value of any longer-term incentives or retention payments that were paid during the year.
Share-based payments (split into plans operated by the company)	Share-based payments that vested during the year (i.e., where there is no longer a “real risk of forfeiture”, although disposal restrictions may still apply). The value would be the cash gain available to executives in relation to equity awards that vested during the year (i.e., the cash gain based on the share price at vesting, before tax, net of any exercise price or other payment required from the executive, if the executive was to have sold the equity at the time the award vested).

* Should state which plans relate to 12-month performance and which relate to greater than 12-month performance periods.

Some clients have raised concerns regarding the disclosure of “actual” remuneration outcomes where a remuneration element has a lengthy vesting period. The concern is that there will be a potential interpretation disconnect between performance and payment, since shareholders may be reviewing actual remuneration outcomes that relate to performance several years ago. We believe that, for this reason, the “actual” remuneration tables should be included in the “performance and reward link” section with an accompanying description of the time period where performance generated the payment.

Determining the “actual” value of termination payments also requires definition, as the amount currently disclosed in the “termination benefits” column of the remuneration report does not correspond with the value requiring shareholder approval (e.g., it does not include the accelerated accounting expense associated with any early vesting of share-based payments). Accordingly, we recommend adopting disclosure requirements around termination payments that align with the definitions used in the termination benefits legislation. This would require companies to list all the components related to termination for each executive using the same terminology and definitions as used in the legislation.

1.3 Implementation of changes

We recognise that the nature of the remuneration report is such that its final form will depend on many factors, such as the complexity of the company’s remuneration approach (particularly where segmentation occurs due to various jurisdictions of operation) and whether there were any significant changes to remuneration policy / practice in the financial year. We therefore suggest that the remuneration report template be implemented through a combination of guidelines and legislation.

Principle 8 of the ASX Corporate Governance Principles and Recommendations, “remunerate fairly and responsibly”, could include a recommendation that states:

The remuneration report should be structured into the following sections and order:

Executives:

1. Overview/summary
2. Remuneration strategy
3. Incentive plans
4. Remuneration opportunity and contracts
5. Performance and reward link (including remuneration outcomes)

Non-executive Directors:

6. NED policy and outcomes

² Due to the complexity associated with valuing benefits (e.g., accruals to defined benefit pension funds), we suggest that the components of fixed remuneration be determined in accordance with AASB124.

The recommendation could be accompanied (in the commentary) by a suggested template for the remuneration report. The template could be in the form of a hypothetical remuneration report, such that it provides an example of the suggested structure, length and specific contents of the remuneration report.

The changes regarding the mandatory content should continue to be through the Corporations Act and the accompanying Regulations.

Appendix A provides a detailed overview of the additions, modifications and deletions required to implement the report structure and content outlined in 1.2.1. While companies would face an initial task of familiarising themselves with the changed requirements, we believe the changes would not increase the ongoing compliance burden. Importantly, our approach would not require a separate “plain English statement” to provide crucial information to shareholders. Rather, the removal of complex accounting disclosures would make it easier to use plain English throughout the report.

Appendix B provides an example of how a company may present information in Section 5: Performance and reward link, including “actual” remuneration outcomes.

2. Simplification of executive incentive arrangements

2.1 The Productivity Commission's findings and our perspective

The PC, through their extensive research into the link between performance and reward, concluded that "Remuneration structures are company- and context-specific and a matter for boards to resolve rather than being amenable to prescriptive direction." (PC report, Finding 2, page 382).

The PC notes that different incentive plan approaches will be necessary for different companies, and possibly for the same company, as needs and priorities change over time. The Board, with its deep knowledge of the business, is therefore best placed to exercise judgement in ensuring that remuneration structures are appropriate for a company's circumstances. The PC also makes the point that the assumption that companies differ from one another is a fundamental principle behind the ASX Corporate Governance Council's "if not, why not" disclosure rule, and that prescribed remuneration structures are unlikely to promote improved performance (PC report, page 219).

In our view, remuneration structures that are linked to company performance will naturally be complex given the complex nature of, and influences on, company performance. The design of remuneration structures reflects the need for companies to take into account various factors (discussed below) when designing incentives.

Further, any review of remuneration needs to consider the global nature of the executive talent pool used by Australian companies. Many Australian companies not only recruit executives into Australia, but also recruit executives into significant international roles in other countries. Australian companies therefore require Australian regulations to be no more stringent than overseas regulations.

On a related point, many of our clients are faced with the issue of having to balance remuneration expectations and practices in more than one market, which can further complicate remuneration design (e.g., while the United States has historically favoured unhurdled option plans, Australian shareholders and advisory groups prefer to see hurdles applied to long-term incentives). This point emphasises the need for companies to be able to tailor the remuneration approach to their commercial needs, which may encompass jurisdictional differences.

2.2 The complexities of designing effective executive incentive plans

Outlined below are the key considerations for companies in designing incentive plans. We believe all elements are important when designing incentive plans. Balancing all considerations will naturally lead to complex incentive outcomes.

Factor	Considerations
Business strategy	The fundamental principle of incentive design is that incentives should be aligned to the business' strategic objectives. As a result, there are a range of different award vehicles, performance measures and targets, and performance periods that are applied, given that company strategies differ.
Market practice	Incentives should be informed (without being led) by market practice to support the company's ability to attract and retain talent.
Shareholder engagement	In today's governance environment, it is important to develop remuneration arrangements that are generally supported by shareholders and shareholder advisory groups. However, companies should place greater weight on what the Board considers appropriate, rather than on what shareholders may support, since the Board is closest to the business' needs. Commercial rationale for the approach should be provided, particularly if differing from shareholder views.
Value to employee	Incentive arrangements should be valued by employees and drive performance. Plans should focus on measures of performance and performance periods that are meaningful to the individual.
Risk alignment	Incentives should support prudent risk management. This issue has been highlighted by the recent global financial crisis and subsequent reviews of remuneration governance within the financial services sector. The Australian Prudential Regulation Authority ("APRA") has stated that performance-based remuneration should be designed in such a way as to discourage risk-taking behaviour, particularly amongst risk and financial control personnel.
Taxation, accounting and regulatory	Incentive plans need to be tax and cost effective and compliant with all legal and regulatory obligations. The existing tax, accounting and regulatory framework for plans, particularly equity-based plans, is extremely complex and often

Factor	Considerations
requirements	conflicts with commercial design objectives and with different areas of applicable legislation (refer section 2.4 for suggested changes to the rules around equity awards).

2.3 Differences between the financial sector and broader industry

The Australian financial services sector, through the recent APRA guidelines, has been the focus of executive remuneration reform. It is recognised that the performance and stability of financial services has significant potential for flow-on effects to the economy. This is the case with many sectors, but arguably more so for the financial sector, given that this sector provides funding for a broad range of companies and individuals. For this reason, the financial sector in Australia is a regulated industry that is governed by legislation.

The above view is supported by the Financial Stability Board (“FSB”) and global regulators, who acknowledge the critical role the financial sector plays in the global economy. The FSB and global regulators have made (and continue to make) changes to the way this sector is regulated. For example, and as noted by CAMAC in their Information Paper, both the United Kingdom’s Financial Services Authority (“FSA”) and the European Commission (“EC”) have proposed changes to the rules governing remuneration within the financial sector with the aim of aligning remuneration arrangements with effective risk management.

While regulation of remuneration within the financial services industry has increased globally, the same level of regulation is not required for broader industry from a risk management perspective, and would limit companies’ ability to tailor remuneration arrangements to suit their strategic needs.

However, we believe there are remuneration governance and process principles emanating from the FSB’s recommendations that have been applied in the financial services sector that are relevant for the broader industry and would benefit many companies. For example, the FSB principle that a company’s Board must monitor and review the remuneration system to ensure the system operates as intended may be beneficial for the majority of companies.

2.4 Opportunities for simplification

The majority of the considerations listed in section 2.2 that generate complexity for incentive plans and structures cannot be easily simplified through the implementation of guidelines or regulations.

However, the taxation and regulatory framework is one aspect within the Government’s and regulators’ control where there are opportunities for incentive simplification. The Government may be able to achieve some of this potential simplification by changing the complex rules around equity awards. The tax rules, in particular, give rise to significant complexity in the design of equity-based incentive plans and, in many respects, place Australia out of step with the majority of developed economies.

- ▶ **Cessation of employment taxing point:** Shareholders, their advisory groups and the PC (directly) and the new termination cap legislation (indirectly) promote maintaining individuals in incentive plans post-cessation of employment (e.g., when an executive retires). However, the current laws result in a taxation point in the year employment ceases, despite no benefit being realised by the individual at that time, and indeed may never be realised where performance hurdles apply and are not met.

This taxation rule generates complexity as companies need to consider approaches to manage the impact of the taxing point arising before awards vest. In some cases, this has resulted in additional plan provisions that apply only to participants who cease employment and remain in the plan, treating them differently to participants who continue to be employed by the company.

Recommendation: We recommend the removal of cessation of employment as a taxing point, in order to align the taxation point with the time at which the executive is able to realise a benefit from the award. Removal of the taxing point will also enable companies to align executive and shareholder interests in the period up to and beyond cessation of employment without introducing additional complex plan provisions.

Further, removal of cessation of employment as a taxing point would be consistent with the taxation rules in the majority of Australia’s international competitors. Finally, we note that the introduction of reporting obligations requiring companies to provide details of equity awards at the time they are subject to tax should be sufficient to protect tax revenue.

- ▶ **Tax treatment of option plans:** The changes to the taxation of employee share schemes (which apply from 1 July 2009) have introduced significant complexity regarding the tax treatment of share options. Under the new tax rules, share options are generally taxed before they are exercised, with the taxing point typically being at vesting. Under the current valuation rules for equity awards, a tax liability can arise on share options even if they are not “in the money” at vesting. If the participant does not exercise the options before they expire (for example, because the options remain “underwater”), the tax rules do not provide for a refund of the tax paid at vesting.

The tax treatment of options under the new rules has caused many companies to significantly amend or simply terminate their option plans. Share option plans, which previously provided a straightforward and well-understood form of equity incentive, are for many companies no longer a viable scheme due to the tax complexities in Australia. Further, this tax treatment poses a problem for small to medium enterprises, particularly early stage companies, who often use options in lieu of cash remuneration to attract skilled and motivated employees due to limitations in capital and cash flow. This sector is a major driver of innovation and productivity, which in turn drives strong economic growth (and tax revenue).

Recommendation: We recommend the taxation rules are revised such that options are taxed on exercise, rather than vesting. This will ensure individuals are not taxed until they realise a benefit. The approach is consistent with the former rules in Australia and most other developed economies.

- ▶ **Removal of 75% rule for shares:** The current tax legislation requires that at least 75% of permanent employees in Australia with at least three years service have (or have previously had) the opportunity to acquire shares or rights/options under an employee share scheme in order to defer tax on grants of shares until the vesting point. The rationale for retaining this requirement when the tax rules were changed is unclear and is likely to limit the number of companies that can offer shares to executives as a form of equity incentive without giving rise to adverse tax implications for participants.

Recommendation: We recommend removal of the 75% test. This will ensure consistency of treatment between using shares and using rights or options as the vehicle to deliver equity incentives.

Appendix A – Suggested changes to disclosure requirements

The following includes our suggested changes to the current disclosures required by the Corporations Act in respect of the remuneration report. The summary table is a refined version of the table included in our earlier submission to the PC, of which CAMAC has a copy.

Where no change is noted to a particular section of the *Corporations Act 2001* (the “Act”) or regulation of the *Corporations Regulations 2001* (the “Regulations”) (together, the “legislation”), we recommend that disclosures be retained.

Suggested change	Comments
1. Modify	
(a) Description of performance and remuneration link	It is difficult to specify the precise disclosures that would illustrate how company performance and remuneration are aligned because of differing business strategies for different companies (and therefore differing performance measures and performance periods).
300A(1)(b) 300A (1AA and 1AB)	The specificity of 300A (1AA and 1AB) encourages companies to detail earnings and shareholder returns over the required period in isolation of remuneration outcomes. In most companies' remuneration reports, this information does not increase shareholder understanding.
AND	
(b) Vesting percentages of bonuses and share-based payments	We suggest replacing these requirements with a revised requirement, as detailed below.
2M.3.03 (1) item 12	<p>The revised requirement should include disclosure of the following:</p> <ul style="list-style-type: none"> ▶ Summary of cash-based incentives paid in the year to each executive. Should include the amount of cash paid in relation to service over the year (i.e., excluding any deferral) and the cash value of any longer-term incentives or retention payments that were paid during the year. For the payments that relate to the current year performance, disclosure should include a high-level summary of the company and executives' performance against targets, the total payment earned (dollar value and as a percentage of maximum), and the split between immediate cash payment and deferral. For payments that relate to multi-years, disclosure should provide a summary of the incentive that was paid during the year, including an explanation of what performance period the amount relates to (and how the value has changed over the period). ▶ Summary of current year share-base payment vesting by executive including performance against the relevant hurdles, the number of awards that vested and the value of the vested awards at the date of vesting. ▶ Summary of the changes in each executive's company shareholdings (number of shares held) and dollar value over the year (split to show both (a) wholly owned shares, vested but restricted shares and vested but unexercised options; and (b) unvested equity awards. Value of equity to be based on share price at year-end less any exercise price (if applicable). ▶ Details of termination payments made in the current year including a breakdown of the components of the payment, and the rationale for the payment (with reference to contractual entitlements).
(c) Remuneration mix 300A(1)(e)(i)	<p>Inconsistent information is disclosed. To promote more consistent disclosure, we recommend modifying the requirement to explain the relative proportion of remuneration related to performance under 300A (1)(e)(i) to specifically require disclosure of the following (as a proportion of total <i>target</i> remuneration):</p> <ul style="list-style-type: none"> ▶ Fixed (not related to performance) ▶ Performance-based (split into its constituent components, for example, short and long-term incentives) <p>Total target remuneration should be based on “remuneration opportunity” for target levels of performance (refer 2b overleaf).</p>
(d) Presentation of prior year individual remuneration data	Individual remuneration data for the current and prior year should be presented in the same table (some companies currently present two tables) so that the remuneration for each individual can be easily compared to the prior year.
2M.3.03 (1) 2M.3.03 (2) items 6, 7, 8, 9 and 11	Executive remuneration (including executive directors) and non-executive director remuneration should be presented in separate tables to simplify presentation and increase shareholder understanding.
(e) Share option and right disclosures	The disclosures specific to share options and rights would be equally relevant for other share-based payment vehicles (e.g., restricted shares and cash payments linked to share price) as all have an associated accounting expense. The wording of the disclosure requirements for share options and rights should therefore be extended to cover all forms of share-based payments.
2M.3.03 (1) item 15 2M.3.03 (3)	

Suggested change	Comments
2. Add	
(a) Actual remuneration outcomes for each KMP (realised values)	<p>Per the PC Recommendation and Ernst & Young prior submissions to the PC.</p> <p>We caution that "actual" needs to be defined. We propose the following definitions:</p> <ul style="list-style-type: none"> ▶ Fixed remuneration: Fixed amounts (i.e., salary, superannuation and other benefits) for the 12-month period³ ▶ Cash-based incentives: Amount of cash paid in relation to service over the year (i.e., excluding any deferral) and the cash value of any longer-term incentives or retention payments that were paid during the year. Should be split into the different plans operated by the company clearly showing what plans relate to 12 month performance and which relate to greater than 12 month performance periods. ▶ Share-based payments: Share-based payments that vested during the year (i.e., where there is no longer a "real risk of forfeiture", although disposal restrictions may still apply). The value would be the cash gain available to executives in relation to equity awards that vested during the year (i.e., the cash gain based on the share price at vesting, before tax, net of any exercise price or other payment required from the executive, if the executive was to have sold the equity at the time the award vested). Should be split into the different plans operated by the company. <p><i>Note that all values are pre-tax.</i></p> <p>Determining the "actual" value of termination payments also requires definition as the amount currently disclosed in the "termination benefits" column of the remuneration report does not correspond with the value requiring shareholder approval (e.g. it does not include the accelerated accounting expense associated with any early vesting of share-based payments). Accordingly, we recommend adopting disclosure requirements that align with the definitions used in the termination benefits legislation (i.e., specifically listing all the components related to termination using the same terminology as the legislation).</p>
(b) Remuneration opportunity	<p>Summary of remuneration opportunity of each executive for the year, including:</p> <ul style="list-style-type: none"> ▶ Fixed remuneration (as at the start of the year and any amendments made during the year) <p>Cash incentive opportunities (target and maximum, to the extent that these are provided for) should be split into the different plans operated by the company clearly showing what plans relate to 12 month performance and which relate to greater than 12 month performance periods.</p> <ul style="list-style-type: none"> ▶ Equity incentive opportunities (expressed as a dollar value or a percentage of fixed remuneration with an explanation regarding how this is converted into a number of shares/rights/options). Split by the plans that the company operates.

³ Due to the complexity associated with valuing benefits (e.g., accruals to defined benefit pension funds), we suggest that the components of fixed remuneration be determined in accordance with AASB124.

Suggested change	Comments
<p>(c) Selected items from the Productivity Commissioner's disclosure checklist</p> <p>Bullets 1, 2, 3 and 5 of the PC's Finding 2.</p>	<p>We suggest that the following disclosures be included in the remuneration report (perhaps as guidance for what is intended by 300A (1)(a)(i)):</p> <ol style="list-style-type: none"> Rationale for remuneration policy (in terms of strategy, risk profile and shareholder alignment) Rationale for remuneration mix policy (see also 1b) Details and rationale for remuneration and performance benchmarking comparator groups Details of any mechanisms to guard against extreme incentive payments from formulaic incentive plans <p>We suggest that companies disclose points i, ii and iii in the Remuneration Strategy section of the remuneration report (see section 1 of this report), alongside the key objective and features of each remuneration element (e.g., fixed, STI and LTI). Point iv should be disclosed in the detailed STI plan description (see section 1 of this report).</p> <p>Note that point i should focus on incentive arrangements, as the information companies disclose in relation to fixed remuneration policy tends to be generic and provides limited insight to shareholders.</p> <p>While we agree that companies should consider the full range of potential outcomes when designing remuneration (bullets 4, 6, 7 and 8 of Finding 2), we do not believe they should be required to disclose how or whether they have done so, as this would add unnecessary complexity to remuneration reports.</p>
(d) Termination payments	<p>Where termination payments are made during the year, the remuneration report and Notice of Meeting should disclose the value of the termination payment (calculated with reference to the definitions in the termination payment approval requirements). The disclosure requirements should be amended accordingly. While the current legislation does not specify a method for valuing equity awards, we believe that the methodology should be consistent with the "actual" values. The disclosure should be accompanied by the company's rationale for the payment and the proportion of the payment that was pro-rated for time and performance.</p> <p>Where the individual is potentially entitled to payments in future years in relation to their current role (e.g., vesting of LTI awards that are not accelerated and therefore vest per the original grant conditions), the "actual" value of any amounts that are expected to vest / be paid to the individual in future years should also be disclosed⁴. Where the value of the future benefit is not known, the maximum value based on the number of equity awards and the current share price (less any consideration paid or exercise price payable) should be disclosed.</p>
3. Move to the Notes to the Annual Financial Report	
(a) Fair valuation methodologies	Per the PC recommendation and Ernst & Young prior submissions to the PC.
(not required disclosure in the remuneration report)	
(b) Accounting value of remuneration outcomes for each KMP.	Accounting costs (including those associated with share-based payments) should be disclosed only in the Notes to the Annual Financial Report and only in aggregate (i.e., for all KMP). Accounting values are useful to indicate the cost of the company's remuneration approach and are therefore more relevant as a supplement to the financial statements. Individual accounting disclosures for KMP would be unlikely to increase shareholder understanding when "actual" values are already disclosed. Disclosure of both accounting values and actual values on an individual basis will result in unnecessary complexity and encourages comparisons that are not meaningful.
2M.3.03 (1) items 6 and 11 2M.3.03 (2)	As aggregate accounting costs of KMP remuneration are already a required disclosure in the Notes to the Annual Financial Report, the requirements to disclose accounting values in the remuneration report should be removed and replaced with requirements to disclose actual values.
4. Remove	
(a) Methods used to assess performance conditions	The requirement to disclose how the satisfaction of performance conditions is assessed and why it is assessed in this way tends to yield inconsistent information about company <i>process and approvals</i> . For example, companies might specify who carries out the calculations and the specific formula used. What is more relevant is information about <i>vesting schedules</i> : how different levels of performance affect the quantum of the incentive payment / award.
300A (1) (ba) (iii)	
(b) Minimum and maximum values of bonuses and share-based awards in future periods	The value of deferral into future periods is typically linked to a variable that has no meaningful maximum and cannot be reliably forecasted (e.g., share price). The other requirements of 2M.3.03 already provide sufficient information regarding the impact of current year grants on remuneration in future periods as they require disclosure of the vesting date and relevant vesting criteria.
2M.3.03(1) item 12(h)	

⁴ The accounting cost will be captured in the Notes to the Annual Financial Report

Suggested change	Comments
<p>(c) Other accounting disclosures regarding options</p> <p>300A (1)(e)(iii), (iv) and (vi)</p>	<p>The following accounting disclosures provide minimal, if any, increment to shareholder understanding:</p> <ul style="list-style-type: none"> ▶ Accounting value of options exercised during the year (actual value at vesting and actual value of shareholdings is more relevant); ▶ Accounting value of awards lapsed during the year (percentage is more relevant); ▶ The percentage of remuneration consisting of options (overall remuneration mix is more relevant).
<p>(d) Description of incentive plans that do not relate to current year grants</p> <p>2M.3.03 (1) item 12</p>	<p>Descriptions regarding incentive arrangements should only be provided for those under which current year grants were made (or future year grants have been contracted). Disclosure for prior year plans would have been mandated in the relevant year and can detract from current year information.</p> <p>For completeness, there should be a reference directing the reader to the relevant year's remuneration report for further detail on legacy plans.</p>
<p>(e) Individual disclosures for the five-highest paid executives if they are not KMP.</p> <p>300A(1)(c)(iii) and (iv)</p>	<p>Per the PC recommendations and Ernst & Young prior submissions to the PC.</p> <p>In our view, it is relevant to disclose information for all KMP as these are the individuals who have the ability to make decisions on behalf of the company and its shareholders. Consequently, it is for these individuals that shareholders require information to assess the extent to which remuneration is aligned with their interests.</p>

Appendix B – Performance & reward link structure and content

The information set out below is an example of how a company may present the information contained within Section 5: Performance and reward link, as suggested in our “ideal” remuneration report. This section includes “actual” remuneration outcomes for the current and prior year.

5. Performance and reward link

5.1 Overall remuneration earned for 2009/10

The following table summarises the remuneration earned by each executive (i.e., the cash values received and the value of shares that vested during the year) and the comparatives to the prior year.

Executive		Fixed remuneration (\$000s)			Cash- based incentives (\$000s)	Share-based payments (\$000s)		Total remuneration realised (\$000s)
		Base salary	Superannuation	Non-monetary benefits	Short-term incentive earned	Deferred short-term incentive (value vested during year)	Long-term incentive plan (value vested during year)	
Executive A	2010							
	2009							
Executive B	2010							
	2009							
Executive C	2010							
	2009							
Executive D	2010							
	2009							
Executive E*	2010							
	2009							

* Executive E ceased employment with the company on dd/mm/yy. Details of his termination benefit are provided in section 5.2.

The incentive amounts illustrated above were determined as follows:

Cash-based incentives

Both the company and executives performed well against the targets set, with most, but not all, targets being met or exceeded.

Executive	Total short-term incentive earned		Cash short-term incentive paid (\$000s)	Short-term incentive deferred to future years (\$000s)
	Value (\$000s)	As a % of maximum opportunity		
Executive A				
Executive B				
Executive C				
Executive D				
Executive E				

Share-based payments

The deferred amounts from the 2007/2008 short-term incentive vested during the year. The following table summarises the amounts that were earned in 2007/2008 and how their value changed based on the share price movement from the deferral date to the date of vesting.

Executive	Short-term incentive earned in 2007/08		Deferral		
	Cash value (\$000)	Deferral (\$000)	Number of shares/rights	Value at deferral on dd/mm/yy (share price of \$X)	Value at vesting on dd/mm/yy (share price of \$X)
Executive A					
Executive B					
Executive C					
Executive D					
Executive E					

In terms of the long-term incentive plan, tranche 2 of the 2006/2007 grant (i.e., 50% of the 2006/2007 grant) and tranche 1 of the 2007/2008 (i.e., 50% of the 2007/2008 grant) was tested. Performance against target was as follows:

- ▶ **Tranche 2 of 2006/2007 grant:** The Compound EPS growth for the period was 12% p.a. which exceeded the stretch target for the 2006/2007 grants of 10% p.a. Therefore 100% of the tranche vested.
- ▶ **Tranche 1 of 2007/2008 grant:** The Compound EPS growth for the period was 8% p.a. which was below the threshold target for the 2007/2008 grants of 9% p.a. Therefore no portion of the tranche vested and the tranche lapsed.

The value realised is summarised below:

Executive	Grant	Number of shares granted	Number of shares vesting	Value at vesting on dd/mm/yy (share price of \$X)
Executive A	Tranche 2 of 2006/2007 grant			
	Tranche 1 of 2007/2008 grant			
Executive B	Tranche 2 of 2006/2007 grant			
	Tranche 1 of 2007/2008 grant			
Executive C	Tranche 2 of 2006/2007 grant			
	Tranche 1 of 2007/2008 grant			
Executive D	Tranche 2 of 2006/2007 grant			
	Tranche 1 of 2007/2008 grant			
Executive E	Tranche 2 of 2006/2007 grant			
	Tranche 1 of 2007/2008 grant			

5.2 Executives who ceased employment during the year

As a result of a change to the company's operation structure, Executive E's employment was terminated on dd/mm/yy. In accordance with his contract, he received the following payments at termination:

Component	Payment
Statutory entitlements	
Accrued leave	\$X
Long service leave	\$X
Termination benefit	
Payment in lieu of notice period	\$X
Early vesting of 2008 long-term incentive grant*	\$X

* Pro-rata for time (two-thirds of the performance period had elapsed) and performance (a performance test at cessation date indicated awards were tracking at full vesting). The value presented is based on share price at the date of termination.

5.3 Changes in value of shareholdings

The following table summarises the fluctuations in **vested** shareholdings and the value of those shareholdings by executive.

Executive	30 June 2009				30 June 2010				Change in value
	Shares held	Vested but restricted shares	Vested but unexercised options	Value (share price of \$X)	Shares held	Vested but restricted shares	Vested but unexercised options	Value (share price of \$X)	
Executive A									
Executive B									
Executive C									
Executive D									
Executive E									

The following table summarises the fluctuations in **unvested** shareholdings and the value of those shareholdings by executive.

Executive	30 June 2009			30 June 2010			Change in value
	Unvested shares/rights	Unvested options	Value (share price of \$X less any exercise price)	Unvested shares/rights	Unvested options	Value (share price of \$X less any exercise price)	
Executive A							
Executive B							
Executive C							
Executive D							
Executive E							