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Meet Our Principals *and* Keep An Eye Out!

Welcome to our December 2019 Newsletter!

Our final quarterly newsletter for 2019 addresses a breadth of issues ranging from graduate employment and salary outcomes, an update on the 2019 AGM season, important data pertaining to KMP remuneration and a look at where we currently stand in relation to the alignment – or misalignment – between shareholders and regulators.

We're also delighted to announce the availability of the complete series of our Research Reports Service, *Insights*.

The series includes:

- **CEO Remuneration Insights**
- **CFO Remuneration Insights**
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Examining Chief Executive Remuneration and Entitlements

Following a recent address to the Armidale Business Chamber, Dr Phillip Lowe, the Governor of the Reserve Bank, was reportedly questioned about his views on the high salaries “at the top end” of Australia’s leading companies.

Dr Lowe was highly critical of the substantial salaries and bonus payments made to CEOs, saying:

“As a regular Australian, it disturbs me. Some people who are paid extraordinarily high amounts of money and working Australians have relatively low wages and getting small wage increases... There is a mindset that says, we have to pay you five or 10 or \$20 million so that you deliver value for the company...”

These comments closely followed the release of a **report by the Australian Council of Superannuation Investors (ACSI)** on CEO Pay in ASX200 Companies. This research, conducted by Ownership Matters on behalf of ACSI, revealed that the average realised remuneration of the top 10 CEOs from companies ranked in the ASX200 was \$14,834,376 in the 2018 financial year. This was substantially influenced by the top three ranked CEOs – Alan Joyce (Qantas), Nicholas Moore (Macquarie Bank) and Michael Clarke (Treasury Wine Estates) – whose realised rewards were in excess of \$19 million. The range of rewards for the top 10 CEOs varied from \$23,876,351 down to \$10,017,376. The substantial reward outcomes arose from a combination of at-risk cash and equity-based remuneration.

Egan Associates’ observation is that a proportion of the CEO reward outcomes realised during the 2018 calendar year as distinct from statutory disclosed reward arose from equity grants some years earlier. Across the ASX 200, a proportion of executives received benefits where securities were allocated as a proportion of their fixed pay at a discount to the prevailing share price based on an accounting valuation reflecting the risk of failure/forfeiture. This approach is not widely adopted today as boards have had

brought to their attention the inappropriateness of allocating equity at a substantial discount to market price for the purpose of ensuring executives are well rewarded, albeit that their performance may not reflect top quartile outcomes.

The ACSI report also found that that more than half of the top ASX100 CEOs received at least 70% of their maximum bonus entitlements in the 2018 financial year.

The median realised pay for an ASX100 CEO reached \$4.5 million. It is reported by ACSI that the findings in relation to chief executive remuneration confirm and lend support to the prevailing corporate ‘culture of entitlement’ surrounding annual bonuses and incentives in many large Australian companies.

Following the **Hayne Royal Commission**, public trust and confidence in the financial services sector in particular has been significantly undermined,

Examining Chief Executive Remuneration and Entitlements (Cont'd)

resulting in the increasing engagement of regulators in reviewing remuneration disclosures and transparency. It is therefore surprising that amid such intense scrutiny, at-risk cash and equity-based remuneration levels remain so high.

Countering this, ACSI has reported trends toward lower base pay for incoming CEOs, reducing their cash rewards by deferring a portion of benefits into equity and implementing bonus clawback provisions in cases of poor executive performance. The latter is in alignment with the current climate of **corporate governance reviews** by the ASIC's Corporate Governance Taskforce, which have been focusing on the oversight of non-financial risk and practices regarding the payment of variable remuneration to key personnel.

Egan Associates recently completed its own comprehensive analysis of CEO remuneration and reward levels across the ASX 500, examining levels of fixed remuneration, annual incentives and the value of equity awards by ASX rank, by revenue and industry sector for the 2018 calendar year. Our research differs from ACSI in that it has not reported realised remuneration, but rather in relation to equity awards, has calculated the underlying incremental value of grants made in prior years where securities remain unvested at the end of the 2018 calendar year. The numbers therefore do not incorporate the accumulation of value upon the vesting of securities which may have been granted in the 2014 or 2015 financial years. In our



Judgement, the vesting of securities which may have been granted in the 2014 or 2015 financial years. In our judgement, the most appropriate foundation for measuring CEO reward is managing those calculations on an annual basis.

There is value in reflecting upon the level of incentives paid to executives among the ASX ranked companies to acknowledge both the average annual incentive as a proportion of fixed remuneration and to also report on the median and average improvement in those organisations' profitability from the prior year. In this context, we are reflecting upon the profit improvement in the ASX 500 financial years ending in the 2018 calendar year over the 2017 calendar year. Our **research highlights significant reward outcomes at the level of CEO, in a context where year-on-year profitability improvements did not appear to support such significant incentives** as proportions of fixed remuneration, as seen in the table on the following page.

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Examining Chief Executive Remuneration and Entitlements (Cont'd)



The data reveals the significant and aggressive level of incentives among Australia's top 50 companies compared to the balance. Egan Associates has also considered Earned Annual Remuneration, which comprises a combination of fixed remuneration and annual incentives awarded. In light of the current climate of tightened regulation and scrutiny of corporate governance and variable remuneration of key personnel, Egan Associates look forward with interest to comparing the 2019 data with the data below. ■

ASX Rank	Average profit improvement (from 2017 to 2018)	Median profit improvement (from 2017 to 2018)	Average annual incentive as % of fixed remuneration
1-10	8.2%	-9.6%	185%
11-50	20.5%	36.1%	106%
51-100	15.2%	-3.5%	73%
101-200	69.6%	6.98%	61%
201-300	-24.3%	11.8%	67%
301-400	>500%	36.1%	35%
401-500	-69.5%	-75.2%	33%

In an environment where CEO pay is under intense regulatory and media scrutiny, care must be taken in determining the structure and amount of CEO pay.

Get all the information you need by ASX Rank (ASX 500), Revenue band and Industry sector with our comprehensive *CEO Remuneration Insights* Research Report.

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Graduate Employment and Salary Outcomes

Quality indicators of Learning and Teaching (QLT) has just released its **2019 Graduate Outcomes Survey (GOS) Report**, which measures the short-and-medium-term employment outcomes of students graduating from Australian undergraduate and postgraduate university degrees in 2016.

The findings in the Report are consistent with previous QLT findings that since the Global Financial Crisis, students have taken longer to establish themselves successfully in full-time employment in their chosen careers. For 2016 undergraduates, 72.6 percent of those completing the GOS secured full-time employment four months after graduating, and 87.4 percent of graduates had secured employment.

Three years later, the same cohort had achieved 90.1 percent full-time employment and 93.3 percent overall employment. These rates have remained relatively stable since 2007.

University graduates have significantly lower levels of unemployment than the general population, with 3.3 percent unemployment in graduates compared with **5.3% unemployment** in the general population. According to the Australian Minister for Education, Dan Tehan, over the last year more than 250,000 new jobs have been created, and

university graduates have been the primary beneficiaries of those jobs.

The median salary of graduates in full-time employment four months after completing their undergraduate studies was \$58,700 in 2016. By 2019, this cohort of graduates achieved a median salary of \$72,800, representing an average increase of 24 percent over the three-year period. For postgraduate students, the median full-time salary four months after completion was \$80,000, rising to \$95,000 three years later.

Of the 40 universities participating in the GOS,

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Graduate Employment and Salary Outcomes (Cont'd)



Sydney University had the highest undergraduate employment rate, with 93.2 percent of students achieving full-time employment within three years of graduating. This was closely followed by the University of Notre Dame, the University of Queensland and Australian Catholic University. Across all universities, undergraduate students of Medicine and Pharmacy had the highest rates of securing full-time employment within four months of completing studies. Within three years of graduating, Dentistry, Medicine and Law students achieved the highest rates of full-time employment.

The Report reveals significant disparity in gender pay both in the short- and medium-term results, both for undergraduate and postgraduate coursework students. For male, compared with females earning \$75,800 (17 percent lower) and \$89,700 (18.5 percent lower) respectively. QILT suggests that these

discrepancies are likely due to a range of factors, including occupation, age, experience, personal factors and possible inequalities within workplaces.

A recent report by KPMG, *"She's Price(d)less: the Economics of the Gender Pay Gap"*, sheds more light on the primary drivers of gender pay disparity in the Australian workforce. KPMG report a "stubbornly flat" gender pay gap of between 14-19% over the past 20 years, meaning that women earn on average \$241.50 less than men."

"gender discrimination is the biggest contributor to inequality, accounting for almost 40% of the gender pay gap"

The report found that gender discrimination is the biggest

contributor to inequality, accounting for almost 40% of the gender pay gap. Gender discrimination is defined as workplace culture, decisions in hiring and promotion, and access to career development opportunities. Other major contributors identified in that report include years not working due to career interruptions (child-care and caring for elderly family members), part-time employment and unpaid work, as well as occupational and industrial segregation.

Despite the persistence of the gender pay gap in university graduates and employees more broadly as indicated above, increasing numbers of women in director roles are being recognised as being Australia's most powerful directors. In a recently released list by consultants, Board Outlook, seven of the top ten most powerful Australian directors (by market capitalisation) were female. It will be interesting to observe whether changing leadership dynamic filters through to future graduates.



CEO remuneration is the subject of increasing regulatory and stakeholder scrutiny.

Click here to find out what Australia's ASX500 CEOs are earning in fixed remuneration, incentives and total rewards in our comprehensive report.



2019 AGM SEASON

The 2019 AGM season is now well underway, with more than 60 ASX 200 companies having already held their AGMs.

After a tumultuous 2018 AGM season which saw 12 of the ASX 200 companies receive first strikes on their remuneration reports, the timing of which coincided with the Hayne Royal Commission, the results from AGMs this year appear to be following similar trends. Strikes have already been reported against the remuneration reports of several large Australian companies, including CSR Limited, WorleyParsons Limited, Carsales.com.au. Strikes have also been reported against Iluka Resources,

CYBG, Speedcast and Adelaide Brighton.

AGMs are scheduled to continue throughout the remainder of 2019/early 2020, with many top companies facing possible board spills on the back of receiving first strikes in 2018, including NAB, Westpac, ANZ, Harvey Norman, Goodman Group and Healthscope. Telstra, Computershare and Tabcorp are among the companies who have already held their 2019 AGMs and have avoided a second strike on their remuneration reports. Myer and the Commonwealth Bank of Australia have held their AGMs and successfully passed their remuneration reports.

Reflecting on the 2018 AGM season, ASIC released a report in early 2019 which identified a number of key

themes arising, including:

- Increased strikes by shareholders on remuneration reports, coupled with an upsurge in the number (92) of material 'against' votes (see also our 2018 article on the ASX 300);
- Tightening of board accountability, particularly following the Hayne Royal Commission;
- A strong focus on environmental, social and governance (ESG) issues, particularly sustainability and climate change risk; and
- The need for improvements in gender diversity.

In relation to the votes against remuneration reports, it appears that there may be an

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2019 AGM Season (Cont'd)

underlying trend towards using votes not only to express discontent regarding remuneration, but also to send a message to key stakeholders about company performance more broadly, particularly share price falls. ASIC reports that where companies received strikes against their remuneration reports, these generally resulted from the company's share price performance, remuneration amount and/or structure, or conduct issues. Shareholder discontent with remuneration itself focused on the amount of pay, the lack of consequence on pay for poor performance, the complexity of the remuneration structure, combined or tailored incentive plans or the lack of transparency about incentive plan operation.

Of particular interest this AGM season is the issue of how companies, particularly those in the Financial Services sector, respond to APRA's July 2019 recommendation that financial measures in relation to short- and long-term bonus incentives should be limited to 50 percent of the criteria, with the remaining fifty percent to be measured against non-



financial goals. Investors, proxy advisors and directors, including the Australian Shareholders Association, Ownership Matters and ISS, have reportedly voiced their concerns regarding the interplay between non-financial metrics and the two-strikes rule. NAB, Westpac and ANZ reportedly all received investor strikes after championing moves toward non-financial metrics for bonus payments.

Overall, it appears that the magnitude of votes against remuneration reports so far is less than in 2018, where some companies received more than 50% of votes against. The exception as at early November is Thorn Group,

which reportedly received more than 87% of votes against its 2019 report. So far, there have been no second strikes in 2019.

The 2019 AGM season has seen a rise personal protest votes against individual directors. Those facing re-election in 2019 have had demonstrably higher votes against their candidature, however to date, all candidates have secured or retained their positions, with Tabcorp directors the latest to secure their roles.

In the 2018 AGM season, four ASX 200 companies received requisitions on ESG issues, particularly in relation to climate change and human

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2019 AGM Season (Cont'd)

rights. In 2019, there is a continued focus by activists including Market Forces and the Australasian Centre for Corporate Responsibility on using shareholder-requisitioned resolutions to pursue environmental, social and governance issues, however to date, no such resolution has received more than 2.5% of votes.

It is reported that in 2019, BHP and Origin are being targeted by climate change activists. BHP in particular is reportedly being pressured by superannuation funds and Atlassian co-founder Mike Cannon-Brookes to improve its stance on climate change, for example by cutting ties with associations including the Minerals Council of Australia. Origin reportedly has five climate resolutions proposed for its 2019 AGM. In relation to human rights, it is reported that Qantas, Coles and Woolworths face share-

holder queries over contracts for supply chain workers and involuntary transportation.

Finally, gender diversity was highlighted as an important issue in the 2018 season and remains a key focus in 2019. It is reported that TPG Telecom Ltd will be targeted by industry super funds for the lack of women on its board, together with ARB Corporation Ltd and Tassal Group Ltd which also had no female board members in 2018. In the 2019 AGMs held thus far, it appears that the proportion of female candidates nominated for elections has been significantly higher than the proportion nominated for re-election. Although only preliminary findings, these suggest steps towards greater gender equality. ■

ASX 500 : KMP REMUNERATION



Egan Associates have conducted detailed remuneration research across the ASX 500 companies at the level of Key Management Personnel. In order to inform boards, CEOs and principal HR executives, we have published a series of comprehensive *Insights*.

These reports cover:

**Non-Executive Directors: ASX 400 and NZX50 (NEDs);
Chief Executive Officers (CEOs);
Chief Financial Officers (CFOs); and
Key Management Personnel (KMP) (excluding NEDs and CEOs).**

We have also prepared a **KMP Reward Relativity Report** which provides extensive data and analysis of pay relativity across the different types of KMP.

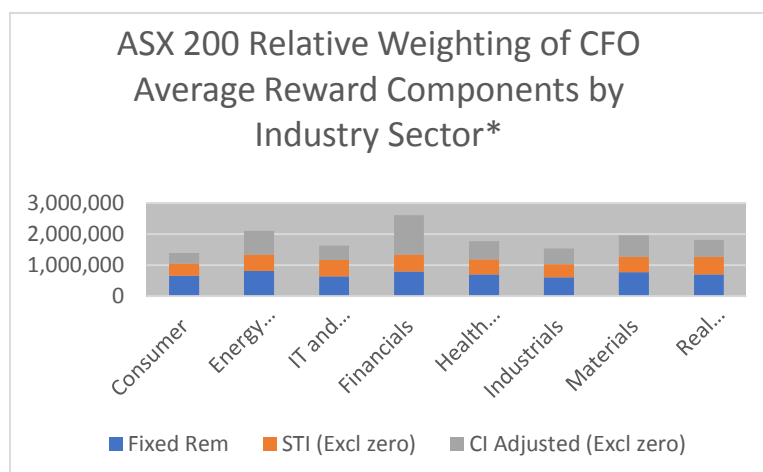
Our comprehensive analysis provides financial information organised by ASX rank, annual revenue bands and industry sector (see example table below).

ASX 500 Revenue Bands : A\$'000				
ASX RANK	75th %ile	Median	25th %ile	Average
Top 10	57,361	22,621	18,518	34,508
Rank 11-50	9,595	4,287	2,467	7,337
Rank 51-100	3,322	1,672	1,089	3,308
Rank 101-200	937	485	247	988
Rank 201-300	373	167	52	455
Rank 301-400	251	146	36	194
Rank 401-500	160	47	0	98

Our research has revealed considerable differences between industries and highly varied reward differentials between the market 25th percentile and 75th percentile, influenced by both market capitalisation, annual revenue and industry sector.



across the ASX 200 by industry:

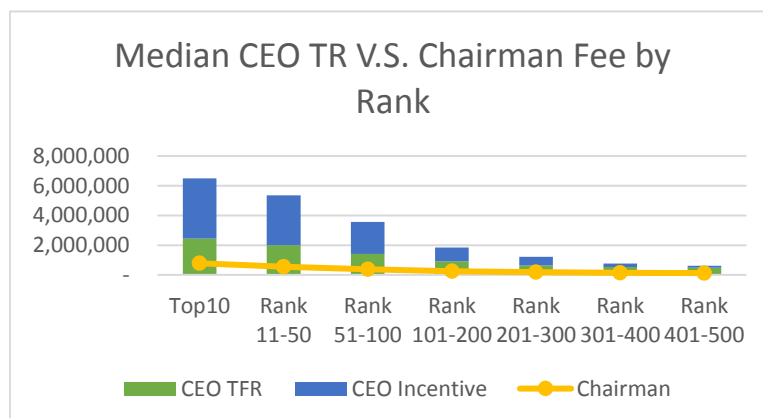


Annual Incentive payments appeared if not misaligned, unaligned, with the improvement in profitability having regard to all disclosed and reported remuneration in covering financial years within the 2018 calendar year compared to the prior calendar year.

Our research also revealed a high degree of variability in in many segments of the market in relation to the apportionment of total reward having regard to fixed remuneration, annual incentives and equity-based incentives valued adopting annualised carried interest as distinct from statutory disclosures.

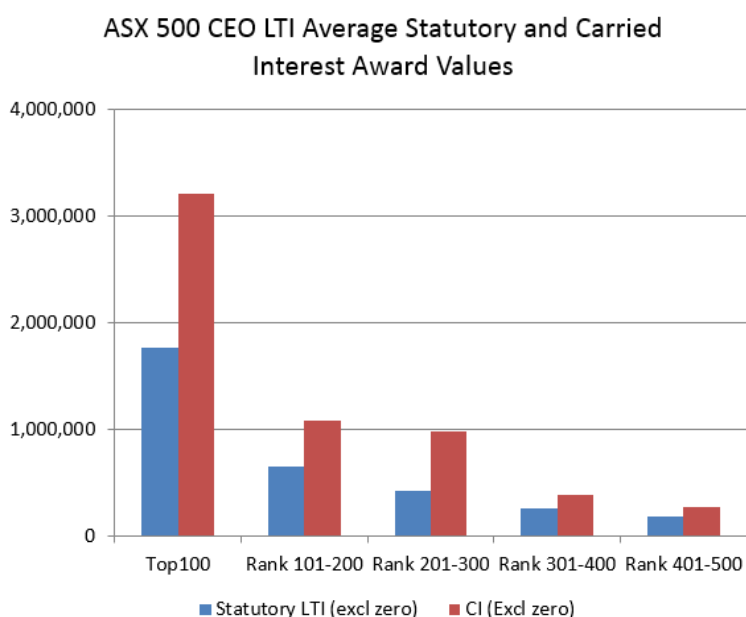
Our guidance on the proportionality of reward between fixed annual incentives and long-term incentives is illustrated in the in the adjacent figure, which highlights CFO reward arrangements on average

What was also fascinating was the relationship between the CEO's fixed remuneration as well as his/her total reward compared to a board chairman. This gap in part reflects tradition, though may also reflect issues raised in the Hayne Royal Commission and other observations of regulators that boards in the current environment are focusing increasingly on governance and less on an organisation's strategy, its development and growth opportunities, its globalisation and its operational challenges including culture.



While disclosing statutory LTI values, we have also calculated the underlying annualised carried interest of equity holdings under long term incentive plans that remained unvested at the end of the 2018 calendar year priced to market at 30 June 2019. The figure below highlights the potential misinformation in statutory disclosures when compared to underlying accruing benefits.

ASX 500 : KMP Remuneration (Cont'd)



Our research did not however highlight the value of realised benefits at the time a KMP exercised their rights to vested securities granted under an LTI plan which may have been held for between three and five years. Nor did we undertake detailed research highlighting the distortions created where performance rights or share rights were allocated at a substantial discount to the prevailing market based on

CEO Statutory LTI by Revenue Band : A\$				
REVENUE	75th %ile	Median	25th %ile	Average
>15B	3,252,085	2,621,155	1,826,549	2,402,817
5-15B	2,115,679	1,373,275	751,214	2,223,784
1-5B	1,937,931	1,065,428	539,346	1,388,264
500M-1B	869,261	600,233	365,481	658,307
250-500M	1,024,204	468,119	345,528	634,102
100-250M	545,542	242,427	114,085	340,889
<100M	513,173	282,340	142,770	367,778

While all information is produced in tabular form highlighting reward arrangements in respect of fixed remuneration, annual incentives, equity based incentives and total reward under a number of ASX bands including the top 10, the next 40, the

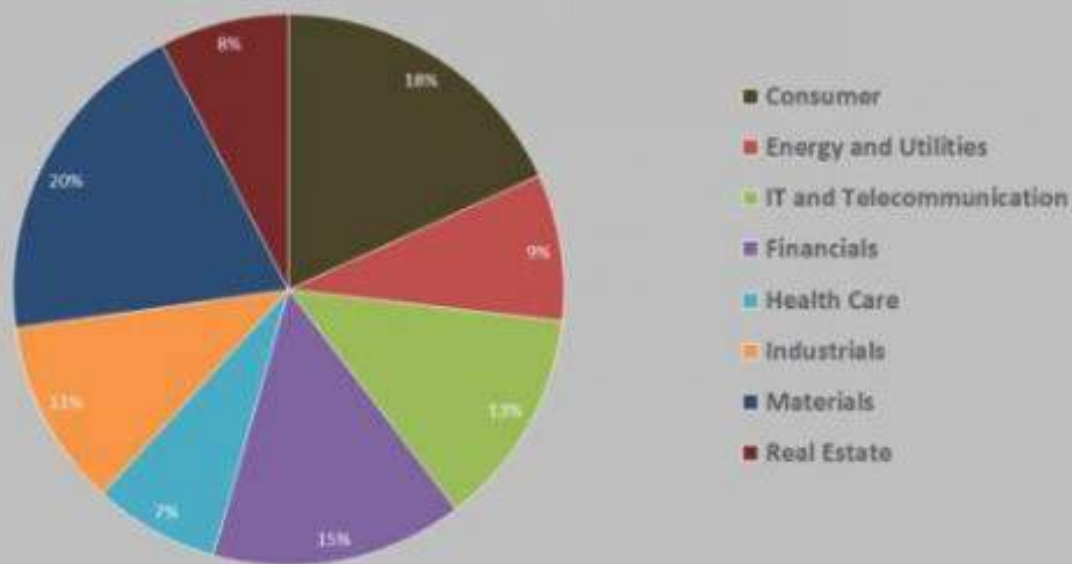
ASX 500 : KMP Remuneration (Cont'd)

next 50 and then in bands of 100 between 101-200, 201-300, 301-400 and 401-500 (excluding NEDs), we have also compiled information within Revenue Bands including organisations with revenues of <\$100 million as well as those with revenues between \$100-250 million, \$250-500 million, \$500 million-1 billion, \$1-5 billion, \$5-15 billion and >\$15 billion.

Our research has also compiled data across the ASX 200 and those companies ranked between 201-500 across eight Industry Sectors including Consumer, Energy & Utilities, Financials, Healthcare, Industrials, IT & Telecommunications, Materials (including the Resources sector) and Real Estate.

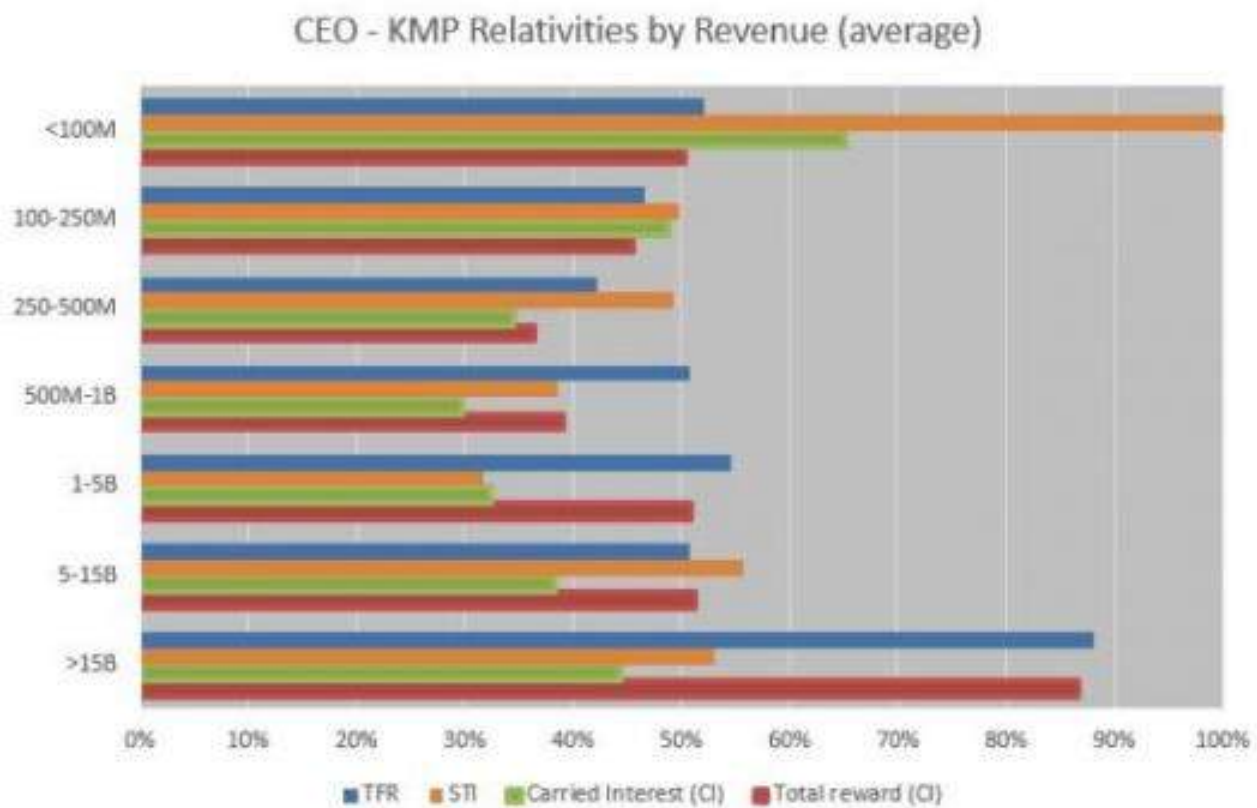


ASX 500 Companies by Sector

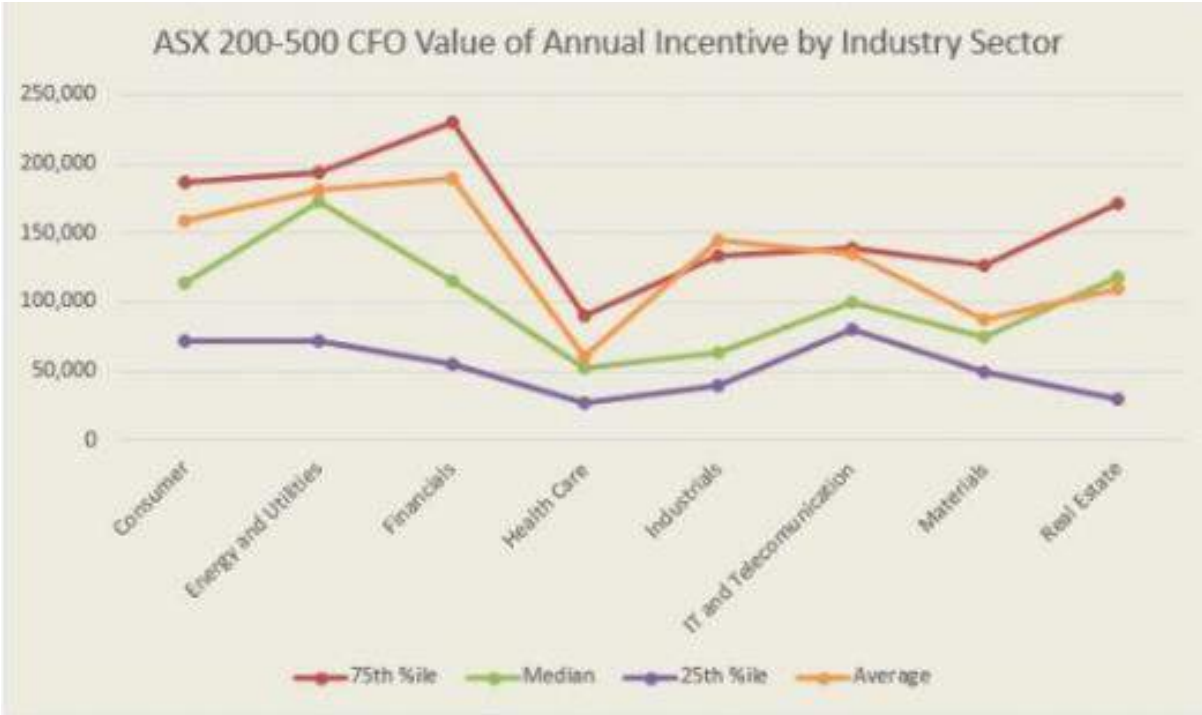


In our report on Reward Relativities, we compare the proportion of KMP reward, including CFOs though excluding the CEO, in relation to fixed remuneration, annual incentives, equity incentives and total reward by ASX Rank, Revenue Bands and Industry Sector. Illustrative of this circumstance having regard to annual revenue is the following:

ASX 500 : KMP Remuneration (Cont'd)



Illustrative of the manner in which our reports highlight reward differentials differential, is the graph below which compares the value of annual incentives received by CFOs among companies in several industry sectors ranked between ASX 201 to 500. ■



Misalignment Between Shareholders and Regulators



In his findings, Commissioner Hayne nominated six norms of conduct underpinning any regulation to include: obey the law; do not mislead or deceive; act fairly; provide services that are fit for purpose; deliver services with reasonable care and skill; and, when acting for another, act in the best interest of that other.

Drawing upon these norms or principles, in recommendation 5.3 of the Hayne Report, it stated that APRA should require financial institutions to “decide their remuneration systems to encourage sound management of non-financial risks and to reduce the risk of misconduct”. It was also recommended that APRA should upgrade its remuneration requirements to ensure that: sufficient attention is given to financial risks including misconduct; limits are set on the use of financial metrics associated with long-term equity-based remuneration; Boards play a more active role in assessing remuneration outcomes; and there is more scope for clawbacks of rewards.

In response to these and other issues arising during the Commission’s Hearings, in late 2018, APRA produced the Banking Executive Accountability Regime (BEAR). While shareholders are not at ease with many of the subjective elements incorporated in BEAR, regulatory oversight is being broadened while remaining focussed.

Since then, APRA has been consulting on the design, governance and outcomes of remuneration practices in Australia’s prudentially regulated firms. In July 2019, APRA proposed an upgrade to the prudential framework for remuneration, which includes: a cap (proposed 50%) on the use of financial metrics and elevation of the importance of non-financial metrics in determining remuneration outcomes; more active involvement at the Board level in determining remuneration outcomes; and longer vesting periods (plus malus and clawback provisions) to promote the long term interests of the company and its shareholders.

These proposals have been met with significant criticism and opposition, particularly the proposed cap on financial metrics, with many arguing that it places undue weight on non-financial metrics which may not be as transparent or reliable as profit-based measures. There has also been criticism of the undue burden created by the expanded role of the Board in remuneration decisions, where traditionally this has been the domain of senior management.

Misalignment Between Shareholders and Regulators (Cont'd)



Subsequently, again reflecting the Commission's findings, we understand that Treasury with input from ASIC is developing a consultation paper due for release at the end of 2019 and draft legislation to facilitate ASIC's use of the law in a more aggressive manner. There has also been suggestion by Treasury that BEAR will be extended not only to all prudentially regulated entities but also to non-prudentially regulated financial firms, with a major focus on business conduct.

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In October 2019, ASIC received judicial guidance on the application of the fairness standard if business conduct as set out in section 912A(1)(a) of the Corporations Act 2001, which provides that financial services licensees must do all things necessary to ensure that their services are provided "efficiently, honestly and fairly". The Full Court of the Federal Court of Australia recently allowed ASIC's appeal of a 2018 decision which found that Westpac's recommendations to customers to switch super funds did not constitute "personal financial advice." In its judgment, the Court stripped the Hayne principles back to one core business conduct principle, "be fair". In addition to providing clarity on the division between financial and general advice, this case also serves as a test case for ASIC and may form the basis of future investigations and/or prosecutions in the financial services sector and beyond.

We understand that banks today are required to create and register accountability maps which specify which members of their senior staff are accountable for every function. The purpose of this initiative is to allow regulators to know whom to target when something problematic arises and is brought to their attention. It is intended that the emerging regime will create subjective standards for banks to act with honesty, integrity, due skill, care and diligence and to deal with regulators in an open, constructive and co-operative way.

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Comment emerging with the conduct of AGMs and votes on Remuneration Reports are increasingly focussing on the basic or core accountabilities of KMPs incorporating the Board, Chief Executive Officer and senior executives.

Questions are also arising, given the level of fixed remuneration, as to whether the principles being articulated in the emerging role of the regulators' oversight should act as gateways or modifiers in determining annual bonus or incentive payments in particular, rather than being a source of additional payment where in the view of many shareholders and institutional investors under the BEAR

Misalignment Between Shareholders and Regulators (Cont'd)

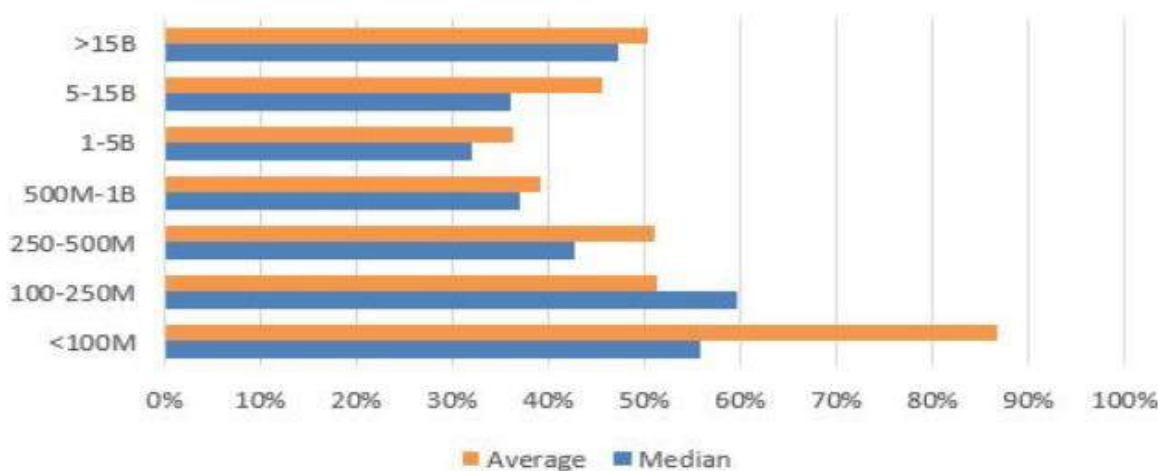
regime management could well be receiving significant incentives for fulfilling their core accountabilities while not enhancing shareholder value.

Critical comment has also arisen at AGMs in relation to management receiving special or supplemental bonus payments associated with acquisition or divestment initiatives, which many would believe represent a core and recurring obligation of the KMP population for which they receive their basic remuneration.

The graphs below highlight the proportionality of reward of CEOs and KMPs managing with oversight of businesses with revenues exceeding >\$15 billion down to those with revenue of <\$100 million. The data is drawn from the constituency of the ASX 500.



TR with CI relativities between CEOs and KMPs -
by Revenue

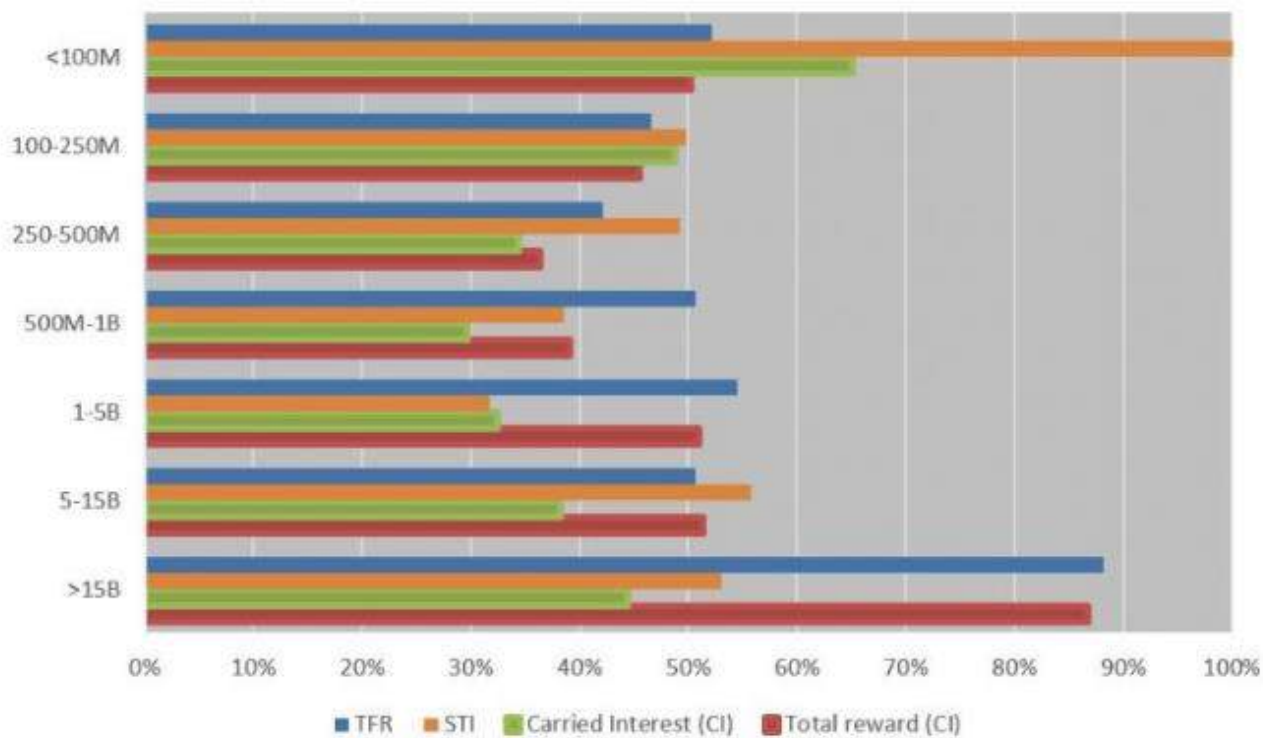


In terms of total reward, small organisations with revenues of less than \$100 million reveal more a partnership model on average though a corporate model at the median. Again, it is the top quartile that is driving this distortion. Among the major corporates, the average total reward of a KMP approximates 50% of that of the CEO. In the next band of companies with revenues between \$500 million and \$15 billion, the median level of total reward compared to the CEO is less than 40%, with the average exceeding that in the larger revenue band. In companies with revenues below \$500 million, the average total reward for KMP exceeds 50% in all categories, with the median exceeding 50% other than in groups with revenues between \$250 million and \$500 million.

Misalignment Between Shareholders and Regulators (Cont'd)



CEO - KMP Relativities by Revenue (average)



For further information on KMP Reward and KMP Reward Relativities see our latest Reports covering essential data and information on all aspects of KMP reward. Just click [HERE](#)!



Meet our Principals

John Egan and Zoe Lockyer are two of the most highly regarded professionals in the fields of remuneration and governance in Australia.

John Egan founded Egan Associates in 1989 and is considered to be one of Australia's foremost experts in resolving complex remuneration and governance matters.

Zoe Lockyer has extensive experience in managing all aspects of reward as both an in-house and external consultant at global, regional and local levels.

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CEO remuneration is the subject of increasing regulatory and stakeholder scrutiny. Find out what Australia's ASX500 CEOs are earning in fixed remuneration, incentives and total rewards in our comprehensive report.

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