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- What is governance
- High level overview of King III
- King III principles
- Implications of King III on remuneration practices
WHAT IS GOVERNANCE? (CONT)
“Good governance is essentially about effective leadership. Leaders need to define strategy, provide direction and establish the ethics and values that will influence and guide practices and behaviour with regards to sustainable performance.”

Sources: King’s Counsel PwC Sept 2009; Executive guide to King III PwC; SARA Reward practice notes; King III Code of Governance; KPMG Quick reference guide to King; King III in a nutshell Cliffe Dekker Hofmeyr
WHAT IS GOVERNANCE? (CONT)

- Remuneration governance entails:
  - Promoting the highest standard of corporate governance, transparency and consistency in the disclosure and decision making of remuneration-related matters – typically for executives but also applicable for all staff in the organisation
  - Adhering to minimum standards in the composition of remuneration committees and the finalisation of mandates for these committees
  - All remuneration related decisions must be governed by a well documented policy to prevent ad hoc decisions
What is governance? (cont)

The Governance Framework Model

Legal Entity
- Memorandum & Articles of Association, Constitution or Charter
- The Board's Governance
- Quality System, Its Policies & Procedures
- Board Culture
- The Board's Attitudes & Behaviours, The Way The Board Works

Legal System
- Legislation & Regulation
- Local, State or Commonwealth Legislation & Regulations

Contracts & Agreements
- Internal & External
- Individual & Organisational Contracts & Agreements

Standards or Quality Systems
- Industry or Government Standards or Quality Systems

Your Organisation's Vision, Mission, Values, Core Business

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HIGH LEVEL OVERVIEW OF THE CODE

- Report launched by the IoD on 01 September 2009
- Implementation date: 01 March 2010
- Followed international governance trends
- King III consists of two documents:
  - Code of governance – a set of principles
  - The Report – recommendations of the best practices for each principle
- Practice notes published in September 2010 & March 2013
- King III applies to all entities regardless of their form or manner of incorporation
The use of instructive language is important e.g.
- ‘must’ indicates a legal requirement
- ‘should’ indicates good governance
- ‘may’ indicates areas where certain practices are proposed for consideration

‘Apply or explain’

Each principle is of equal importance and together they create a holistic approach

Therefore, substantial application of the Code and Report therefore does not achieve compliance
OVERARCHING KING III REMUNERATION PRINCIPLES

- Principle 2.25: Companies should remunerate directors and executives fairly and responsibly.
- Principle 2.26: Companies should disclose the remuneration of each individual director and certain senior executives.
- Principle 2.27: Shareholders should approve the company’s remuneration policy.
IMPLICATIONS FOR REMUNERATION PRACTICES

- Remuneration philosophy and strategy
- Base pay and benefits
- Variable pay including short term incentives and long term incentives
- Executive Employment Contracts
- Disclosure and Remuneration of Executive Directors
- Non-Executive Director fees
- Remuneration Committees and Governance
- Shareholder engagement
## Implications for Remuneration Practices: Remuneration Philosophy, Strategy & Policy

<table>
<thead>
<tr>
<th>King III principle</th>
<th>Implications</th>
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</thead>
<tbody>
<tr>
<td>147: Companies should adopt remuneration policies and practices for executives that create value for the company over the long term. Policies and practices should be aligned with the company’s strategy, reviewed regularly and linked to the executive’s contribution to company performance</td>
<td>• Remuneration philosophy &amp; strategy support business, human resources and people strategies</td>
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<td></td>
<td>• Remuneration policy should be designed to give effect to the remuneration strategy</td>
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<td></td>
<td>• Remuneration strategy should be approved by the Remco. Policies should be reviewed annually.</td>
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<td></td>
<td>• Remuneration mix included in overall policy</td>
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<td>• Performance scorecards should indicate the manner in which exec reward is related to the value created for shareholders</td>
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</tbody>
</table>
# Example of Pay Mix indicating Strategic Intent

<table>
<thead>
<tr>
<th>Remuneration component:</th>
<th>Time frame:</th>
</tr>
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<tbody>
<tr>
<td><strong>Total Guaranteed Package</strong> = Base pay + benefits + benefits</td>
<td><strong>Monthly</strong></td>
</tr>
<tr>
<td>TGP</td>
<td>• Attraction</td>
</tr>
<tr>
<td>Allowances</td>
<td>• Internal &amp; external equity</td>
</tr>
<tr>
<td></td>
<td>• Service</td>
</tr>
<tr>
<td></td>
<td>• Indiv performance</td>
</tr>
<tr>
<td>STI</td>
<td>• EVP (Employer of choice)</td>
</tr>
<tr>
<td></td>
<td>• Align with Wellness strat.</td>
</tr>
<tr>
<td>STIP (incl Def Bonus)</td>
<td>• Encourage savings and interest in share performance</td>
</tr>
<tr>
<td>Co-Invest Plan</td>
<td>• Compliance with legislative, negotiated and contractual commitments</td>
</tr>
<tr>
<td>LTI</td>
<td>• Line of sight with financial targets</td>
</tr>
<tr>
<td></td>
<td>• Employment equity</td>
</tr>
<tr>
<td></td>
<td>• Safety RCR</td>
</tr>
<tr>
<td>MTI</td>
<td>• Attract &amp; retain</td>
</tr>
<tr>
<td>SAR</td>
<td>• Encourage shareholding</td>
</tr>
<tr>
<td></td>
<td>• Reward ind performance</td>
</tr>
<tr>
<td></td>
<td>• Align with bus life cycle</td>
</tr>
<tr>
<td></td>
<td>• Wealth creation</td>
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</tbody>
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**Implications for Remuneration Practices: Remuneration Philosophy, Strategy & Policy**

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</table>
| 151: In proposing the remuneration policy, the Remco should ensure that the mix of fixed and variable pay, in cash, shares and other elements, meets the company’s needs and strategic objectives. Incentives should be based on targets that are stretching, verifiable and relevant. The Remco should satisfy itself as to the accuracy of recorded performance measures that govern vesting of incentives. Risk-based monitoring of bonus pools and long-term incentives should be exercised to ensure that remuneration policies do not encourage behaviour contrary to the company’s risk management strategy. | • In the setting of targets, required behaviour should be aligned to the company’s enterprise-wide risk management strategy  
• The balance between short and long term incentives should ensure an appropriate focus on the shorter term and longer term business objectives |
# Implications for Remuneration Practices: Base Pay/VP

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| 157: In setting remuneration policies, Remco should ensure that remuneration levels reflect the contribution of senior executives and executive directors and should be rigorous in selecting an appropriate comparative group when comparing remuneration levels. There should be a balance between fixed and variable components to allow for a fully flexible bonus scheme. | • Base pay + Benefits + STI + LTI  
• The percentage contribution of each component should be set and regularly reviewed  
• Comparative group: select from a similar market sector and size companies  
• Ensure that similar size roles are compared  
• For international data points: consider the adjustment of data with cost of living factors  
• Fully flexible bonus = no bonus if performance is below threshold. |
**Implications for Remuneration Practices: Benefits**

<table>
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| 152. The Remco should scrutinise all benefits including pensions, benefits in kind and other financial arrangements to ensure that they are justified, correctly valued and suitably disclosed | • Competitive and appropriate  
• Meet legislative requirements  
• Costs justified  
• Well governed  
• Fair and non-discriminatory  
• Differentiation between executive benefits and employee benefits - is this justified  
• Correctly valued and disclosed |
## Implications for Remuneration Practices: Variable Pay

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| 148: Factors affecting company performance, but *outside the control* of executives, and to which they have made no contribution should only be considered to a limited extent. At lower levels in the company the effect of outside factors should be ignored. | • Remuneration policies should seek to moderate the effect of uncontrollable factors  
• Overall sustainable performance should still be targeted, within a mix of financial and non-fin targets  
• Affordability and business sustainability need to be considered |
## Implications for Remuneration Practices: Variable Pay – Long Term Incentives

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<thead>
<tr>
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<tr>
<td>Principles 166, 167, 168, 169, 170, 171, 172, 173, 174, 175, 176, 177, 178, 179.</td>
<td>• Participation should be restricted to employees and exec directors&lt;br&gt;• Fair value of LTI component should form part of your pay mix&lt;br&gt;• Highly leveraged incentive schemes should be used with care&lt;br&gt;• Regular annual grants – sign-on and promotional grants?&lt;br&gt;• Vesting of rights determined by corporate performance targets&lt;br&gt;• Avoid ‘all or nothing’&lt;br&gt;• No automatic waving of corporate targets</td>
</tr>
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# Implications for Remuneration Practices: Variable Pay – Long Term Incentives

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| Principles 166, 167, 168, 169, 170, 171, 172, 173, 174, 175, 176, 177, 178, 179. | • No fixing of the share price or discount on share price before grant date  
• Minimum vesting period: 3 years; max: 7 years for new schemes  
• No re-testing in subsequent periods  
• Regular annual grants  
• No re-pricing or surrender of underwater options  
• No backdating or grants within a closed period  
• Salient features of schemes included in the remuneration report  
• Retention schemes separately disclosed |
## Implications for Remuneration Practices: Non-Executive Director Fees

<table>
<thead>
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</table>
| 153: Base & attendance fee  
154: Although permitted by the Act, the chairman and other non-executive directors should not receive share options or other incentive awards geared to share price or corporate performance, as such incentives align their interests too closely with executives and may be seen to impair their objectivity. | • No share options, conditional shares or bonuses linked to the achievement of targets  
• International practice: combine cash with full value unconditional shares that have no corporate performance targets attached  
• BEE shares are in order provided shareholder approval has been obtained |
| 155: Fees to be approved in advance. The Act requires a special resolution at intervals of not more than two years for this purpose. | |
**Implications for Remuneration Practices: Remuneration Committees**

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<thead>
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| 150: The Remuneration Committee should assist the Board in its responsibility for setting and administering remuneration policies in the company’s long term interests. The Committee considers and recommends remuneration policies for all levels in the company but should be especially concerned with the remuneration of senior executives, including executive directors, and should also advise on the remuneration of non-executive directors | • Review the mandate for your Remco  
• Scope is at all levels (policy)  
• Specific approval for executive remuneration  
• Two over one principle |
**Implications for Remuneration Practices: Remuneration Governance and Disclosure**

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<tr>
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| 181. In its annual remuneration report, to be included in the integrated report, the company should explain remuneration policies followed throughout the company with a special focus on executive management, and the strategic objectives that it seeks to achieve, and should provide clear disclosure of the implementation of those policies | • Include salient features of rem strategy and policies in remuneration report – although the emphasis is on directors and snr executives, would typically include a broader perspective as it applies to all employees  
• How these drives performance and shareholder value creation  
• How these have been implemented  
• Salient features of incentive plans  
• Employment policies as these relate to executive contracts and severance  
• Disclosure of actual rewards received |
**Implications for Remuneration Practices: Remuneration Governance and Disclosure**

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</table>
| 180. ...disclosure of each executive, non-executive and prescribed officers details in terms of base pay, bonuses, share based payments, granting of options / rights, restraint payments, and all other benefits (incl present values of future awards) | • Prescribed officers to be identified  
• Typical trend is to disclose remuneration details for Exco members  
• Disclosure by name |
| Principles 159, 182, 183, 184, 185 | • Policy on setting base pay and benchmarks  
• Explain any ex gratia payments  
• Disclose executive employment contracts  
• Disclose performance metric  
• Maximum and potential dilution |
## Implications for Remuneration Practices: Remuneration Governance and Disclosure

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</table>
| 186. Every year the remuneration report should be tabled to shareholders for a non-binding advisory vote at the annual general meeting. The vote enables shareholders to express their views on the remuneration policies adopted and on their implementation. | • Remuneration report tabled as a resolution at the AGM  
• Purpose: provide shareholders with an opportunity to influence the board’s perspective on remuneration and express their views on the adoption of the remuneration policy and its implementation  
• Less than 50% of the votes favourable, no immediate and direct consequence – the Remco is advised to engage with investors to understand underlying concerns. |
Key Take Outs

- Companies should consider a more holistic approach to reward management and how this impacts the organisation’s EVP
- Pay mix should be more clearly defined and determined
- Remuneration policy needs to contain much more detail in terms of benchmarks, competitor groups, variable pay schemes, linkage to performance management processes etc
- Annual review of all performance targets related to variable pay plans – use combination of financial and non-financial targets
- Strong link between executives’ performance and rewards
- Remco members need to be continuously informed of the status of remuneration plans implemented
- Review your Remco Charter regularly and ensure alignment
- Review the level of disclosure and get buy in on how much to disclose
Why Spur's executive pay policy was shot down

The billion-rand restaurant chain MD says it will be put to another vote.

JOHANNESBURG – Capitalist activists voted down restaurant franchise owner, Spur’s (JSE:SUR) executive compensation policy for a variety of reasons and not just because it planned to hike non-executive directors pay by 40%.

This emerged after the company held discussions with shareholders, Spur’s MD Pierre van Tonder told Moneyweb.

At its annual general meeting (AGM) on December 2, 45.87% of its shareholders voted against endorsing its remuneration policy and 35.31% abstained.
Why Allan Gray voted against Sappi’s executive pay policy

The paper giant may change its policy after talking to the top fund manager.

JOHANNESBURG – Clients of top investment manager, Allan Gray were the main shareholders which voted against Sappi’s remuneration policy, as Allan Gray felt it was too skewed towards short-term rewards.

The casting release paper maker revealed at its annual general meeting (AGM) on February 8 that just over a third of shareholders had voted against its remuneration policy. Allan Gray clients, who own 22.2% of the paper giant, according to Sappi’s 2011 annual report, were amongst the shareholders who voted against the policy.

Ian Liddle, chief investment officer of Allan Gray, told Moneyweb that it agreed with most of Sappi’s pay philosophy but not with the balance between the short- and long-term awards.

“Sappi is too heavily skewed to short-term awards such as annual bonuses,” he said.
Once again, proxy season has revealed some eye-popping numbers in executive compensation packages, generating heat from shareholders, labor organizations and some analysts who contend the links between CEO pay and performance are frayed. Among the most-talked about compensation reports this year is the $1.6 billion option package for UnitedHealth Group CEO William McGuire at a time when more than 40 million Americans lack health insurance. Former Exxon CEO Lee Raymond retired with a $400 million package as consumers face soaring gasoline prices. AFL-CIO members hired a plane to fly over Pfizer's annual meeting in Lincoln, Neb., in April with a banner reading: "Give it back Hank!" -- a reference to CEO Hank McKinnell's $83 million pension plan set to take effect in 2008. McKinnell has already earned $65 million since he became CEO in January 2001. At the time of the meeting, Pfizer shares had dropped 46% in value under McKinnell's watch.
CEO Skill and Excessive Pay: A Breakdown in Corporate Governance?

STANFORD GRADUATE SCHOOL OF BUSINESS—What do Disney, AT&T, Exxon, and Verizon have in common? Based on economic performance and what they paid their CEOs from 1991-2002, a new academic study argues that all these firms were headed by CEOs who were paid too much.

These firms, say the researchers, are among a group of companies headed by CEOs whose pay is negatively related to job skill: The CEOs seem to be rewarded—in most cases, quite amply—for their bad performance. Disney's Michael Eisner, for example, was paid $38 million above the industry average when for three out of six years the company’s performance actually declined in relation to other firms in the entertainment industry.
We need more capitalist activists - Theo Botha

Also King III needs to be simplified.

CAPE TOWN - The King III code of corporate governance is too onerous and demanding for companies to adhere to and should be simplified. This is according to Theo Botha, or “the capitalist activist” as he was described at a Cape Town Press Club event on Wednesday. Although compliance with the code is not legislated, listed companies are expected to comply with the principles. But King III has over 70 principles that companies need to comply with. The challenge, says Botha, is that it is detailed and time-consuming to review and assess what principles are being applied and where the gaps are.

Remuneration issues are a big bug-bear at the moment. “When it comes to remuneration policy, disclosure is critical. The problem is that when it comes to bonuses and other incentives it is impossible to assess whether they are justified or not because the key performance indicators against which performance is measured are seldom disclosed.”

For instance: “How can Nick Wentzel the former CEO of Reunert walk away with R18.2m – R12m of which was a severance package – after just 14 months in the job? You can ask the questions in an annual general meeting (AGM) but many directors just talk in circles around you.”