

## A global giant in the making?

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| <b>Company/ASX Code</b>      | Sonic Healthcare/SHL   |
| <b>AGM date</b>              | Tuesday 19 November 2019   |
| <b>Time and location</b>     | 10am Intercontinental Hotel Macquarie Street Sydney              |
| <b>Registry</b>              | Computershare  |
| <b>Webcast</b>               | No   |
| <b>Poll or show of hands</b> | Poll on all items  |
| <b>Monitor</b>               | Allan Goldin assisted by Patricia Beal                           |
| <b>Pre AGM Meeting?</b>      | Yes with Chair Mark Compton and Company Secretary Paul Alexander |

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| <b>Item</b>     | <b>Consideration of accounts and reports</b> |
| <b>ASA Vote</b> | No vote required                             |

## Summary of ASA Position

In many ways, Sonic Healthcare (Sonic) appears to be a newly listed family company. This is a strange comment to make about a company that has been listed for more than 30 years, employs more than 37,000 people, and is one of Australia's very few global success stories. But maybe that is what you get when you have a CEO who is one of only three Australians to make Harvard Business Review's world's best performing CEOs list for 2019.

A great deal of Sonic's success can be put down to the fact that it sees itself as more of a federation than a company. Their acquisitions, which number at around 150, happened because they are a doctor led business that shares the same philosophy as their parent company. Barring possibly their largest ever acquisition, Aurora Diagnostics, this idea holds true. Aurora's acquisition was made mainly because it was a leading anatomical pathology provider, an area in which Sonic had limited exposure.

Sonic is a company which has a very strong belief in the importance of Corporate Responsibility but in modern accepted notion of Corporate Governance maybe not so much. This approach may have a great deal to do with the fact that for the last 16 years the two most powerful individuals and driving forces appear to be the CEO and CFO, who have also been executive directors that whole time.

The Company has many senior executives and options were granted to more than a 100 people, but if you read the Annual Report you will see that only three of the executives are listed as Key Management Personnel and all three of the them are also Directors, a situation found in virtually no other S&P/ASX200 company. This raises serious questions about the division between Directors and management responsibilities.

In addition, like most companies, as long as the auditors are providing a competitive price and doing what the board considers a good job, the appointment will continue. Given the global spread of the Sonic business it seems unlikely any firm other than one of the big 4 could carry out the audit.

Despite the matters mentioned above, the company has been successful. Arguably, it may be poised for even greater growth if the trend continues. In the provision of pathology services Sonic is Number 1 in Australia, Number 1 in Germany, Number 3 in United States and in their area the largest provider of laboratory contracts to the National Health Services in the UK.

When so much of your revenue is regulated by governments much of your profitability stems from the benefits of scale, Sonic is poised to add to their strengths in this area. In addition, it continues to exploit its efficient cutting edge procedures and market understanding to very good effect as was well demonstrated here in Australia, when they recently won the \$30 million National Bowel Screening program from their main Australian competitor.

ASA believes that it is important that the majority of directors be independent. Sonic is currently looking for a new (preferably medically qualified) director, but in the meantime they have 3 executive directors and one who as has held the role for more than 12 years; ASA and many others would consider him to be non-independent.

No matter how much of modern corporate governance you come into conflict with, one matter is paramount to ASA: alignment with retail shareholders. ASA very strongly believes that Directors must have an alignment with shareholders and the most tangible way that can be demonstrated is that within 3 years of being on the board, you purchase shares that are equivalent to one year's remuneration. While the MD and FD have significant skin in the game, a number of directors have holding valued at less than their annual fees.

## **Summary**

| (As at FYE)                           | 2019    | 2018   | 2017  | 2016  | 2015  |
|---------------------------------------|---------|--------|-------|-------|-------|
| NPAT (\$m)                            | 549.7   | 476    | 428   | 451   | 348   |
| UPAT (\$m)                            | 524     | 467    | 442   | 440   | 375   |
| Share price (\$)                      | 27.10   | 24.53  | 24.22 | 21.55 | 21.37 |
| Dividend (cents)                      | 82      | 78     | 75    | 71    | 69    |
| TSR (%)                               | 14.1    | 4.9    | 16.3  | 4.6   | 28    |
| EPS (cents)                           | 122.1   | 112.2  | 102.1 | 109.3 | 86    |
| CEO total remuneration, actual (\$m)* | 11.873* | 9.978* | 5.092 | 4.403 | 2.919 |

\* based on the date the options were exercised; if it was based on the date options vested the figures would be \$10.017m and \$8.771m.

For 2019, the CEO's total actual remuneration was **134.7 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2019 data from the Australian Bureau of Statistics).

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| <b>Item 1</b>   | <b>Re-election of Dr Jane Wilson as a Director</b> |
| <b>ASA Vote</b> | <b>Undecided</b>                                   |

### Summary of ASA Position

Dr Wilson was appointed to the board in July 2010. She is a registered General Medical Practitioner with a background in finance, banking and medicine.

Dr Wilson is currently a Guardian of the Future Fund, non-executive Director of ASX-listed companies Transurban Group (since January 2017) and Costa Group Holdings Limited (from April 2019), and a non-executive Director of the General Sir John Monash Foundation. She is also Co-Chair of the Australian Government Advisory Board on Technology and Healthcare.

The board in recommending Dr Wilson's re-election, recognising that she brings more than two decades of corporate governance and company oversight experience across a diverse range of companies and industries to the position, including extensive experience in corporate finance, innovation and the commercialization of technologies with a focus on the healthcare sector.

On the face of it, ASA considers Dr Wilson to be an excellent director, however Dr. Wilson's 3,770 shares are well short of that threshold which would show alignment with retail shareholders (at

\$30 shares are valued at \$113,000 compared to \$212,000 fees). Although we do want to vote for her we will be asking her at the AGM when she will purchase more shares.

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| <b>Item 2</b>   | <b>Re-election of Dr Philip Dubois as a Director</b> |
| <b>ASA Vote</b> | <b>Against</b>                                       |

### Summary of ASA Position

Dr Dubois was appointed to the board in 2001 and holds 8,770 shares. He is CEO of Sonic's Imaging Division and Chairman of the Sonic Imaging Executive Committee. A neuroradiologist and nuclear imaging specialist, he is currently an Associate Professor of Radiology at the University of Queensland Medical School.

In recommending Dr Dubois' re-election, the Board recognises the value of his strategic input and executive leadership experience in healthcare services, and in particular, his wealth of experience in diagnostic imaging. Dr Dubois' membership on the Board has significantly contributed to consolidating Sonic's imaging businesses into a cohesive group. Dr Philip Dubois has advised that, should he be re-elected by shareholders at this year's Annual General Meeting, he will permanently retire from the Board by the end of that three-year term.

Although we understand that Dr Dubois has been an extraordinarily valuable member of the board, we cannot vote for a director whose election leaves the Company without a majority of independent board directors.

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| <b>Item 3</b>   | <b>Adoption of Remuneration Report</b> |
| <b>ASA Vote</b> | <b>For</b>                             |

### Summary of ASA Position

If ASA practiced a tick the box mentality, based on our guidelines we would vote against this remuneration report as it breaches a few of our guidelines:

STI is paid 100% in cash,

LTI is measured only over 3 years

The board does not have a majority of independent directors.

There are no executive KMP who are not directors.

At the same time we acknowledge that having 75% of the STI based upon financial measures is a positive.

The LTI which is an unusual combination of options and performance rights has 50% based on a comparison of Total Shareholder Return measured against the S&P/ASX100 Accumulation Index. 25% is awarded based on the Company's aggregate earnings per share over 3 years being above 361 cents to achieve 40% of the award. The other 25% is based on average 3 year return on capital being better than the target set, which in the first year is set at 8.5%.

The testing nature of these measures is best demonstrated by the fact that on average only 41% of the LTI is awarded.

However as we have acknowledged in the past by voting our undirected proxies in favour of the remuneration report, this Company is very unusual in having the two executive directors with considerable shareholding having led the Company very successfully for 16 years. So despite our guidelines we will continue to make an exception.

#### CEO Remuneration framework

|                    | Target \$m | % of Total | Max. Opportunity \$m | % of Total |
|--------------------|------------|------------|----------------------|------------|
| Fixed Remuneration | 2.39       | 31.28%     | 2.39                 | 27.82%     |
| STI - Cash         | 2.63       | 34.40%     | 3.59                 | 41.66%     |
| LTI                | 2.63       | 34.32%     | 2.63                 | 30.52%     |
| Total              | 7.66       | 100.0%     | 8.61                 | 100%       |

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| <b>Item 4</b>   | <b>Approval of LTI grant to CEO/Managing Director Dr Colin Goldschmidt</b> |
| <b>ASA Vote</b> | <b>For</b>   |

#### Summary of ASA Position

This resolution is for a combination of options and performance rights that on issue are valued at \$2,629,971.

We have explained the tests that must be met and testing nature of the hurdles in above resolutions. We will vote our undirected proxies in favour of this resolution.

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| <b>Item 5</b>   | <b>Approval of LTI grant to CFO/Finance Director Chris Wilks</b> |
| <b>ASA Vote</b> | <b>For</b>   |

This resolution is for a combination of options and performance rights that on issue are valued at \$1,168,399.

In the earlier resolution we explained the tests that must be met and testing nature of the hurdles. We will vote our undirected proxies in favour of this resolution.

An individual (or their associates) involved in the preparation of this voting intention has a shareholding in this company.

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