Australian Shareholders' Association Limited
ABN 40 000 625 669
Suite 11, Level 22
227 Elizabeth Street, Sydney NSW 2000
PO Box A398, Sydney South NSW 1235
t (02) 9252 4244 | f (02) 9071 9877
e share@asa.asn.au

Will Technology One receive a second strike?

Company/ASX Code	Technology One / TNE
AGM date	Wednesday 23 February 2022
Time and location	10:30am AEST Brisbane Convention and Exhibition Centre Merivale St, South Brisbane
Registry	Link Market Services
Webcast	www.technologyonecorp.com/company/investors/annual-general-meeting-2022
Poll or show of hands	Poll on all items
Monitor	Paul Donohue
Pre AGM Meeting?	Yes, with ▪ Jane Andrews, Non-Executive Director / Chair of the Remuneration Committee. ▪ Richard Anstey, Non-Executive Director / Chair of the Nomination and Governance Committee. ▪ Edward Cheung, Chief Executive Officer. ▪ Paul Jobbins, Chief Financial Officer / EVP Corporate Services / Company Secretary. ▪ Stephen Kennedy, Head of Governance, Risk & Compliance / Company Secretary.

The individual involved in the preparation of this voting intention has a shareholding in this company.

Summary of issues for meeting

The ASA will be voting undirected proxies in line with the Technology One Board's recommendations this year although that support comes with some qualifications.

- While the appointment of Pat O'Sullivan to a new role as Lead Independent Director and Deputy Chair is good news for shareholders, it represents another missed opportunity to address the Board's gender imbalance.
- Richard Anstey's skills and experience are, no doubt, relevant to Technology One's Board, however after 16 years in the role can he still be considered "independent"?

Has Adrian DiMarco made peace with shareholders who delivered a first strike last year? This year's remuneration report looks acceptable to your ASA monitor, and we hope a second strike is averted.

Item 1	Consideration of accounts and reports
ASA Vote	No vote required

Summary of ASA Position

Few companies have a creation story as compelling as Technology One (TNE). In 1987, Adrian Di Marco founded the company in a demountable building at a Brisbane hide processing plant with seed funding from the MacTaggart family. Since those early days, the product has undergone four major evolutions with the current incarnation, a Software as a Service (SaaS) solution, set to turbo charge the company's economics.

Previously the software was implemented "on-premise", meaning it ran on the client's own computers. While this was the standard deployment model for decades, it meant the client took responsibility for some of the technical complexity, whereas with the SaaS model the software is accessed remotely via the Internet. This lets the customer focus on their business rather than the technology and reduces their total cost of ownership (TCO) by 30%.

There are significant benefits for Technology One. With the computing power centralised, it is easier to monitor, support, upgrade, back up and secure the solution. SaaS licences earn more revenue per year than the equivalent traditional license, partly to compensate Technology One for providing the infrastructure rather than the customer.

Technology One's customers have embraced the new platform with 637 already onboard and the remainder scheduled for migration by October 2024. Thanks to this rapid adoption rate, annual recurring revenue (ARR) from SaaS jumped 43% in 2021 to $192.3m.

These favourable economics are flowing through to the bottom line and have been recognised by the market. At the end of the reporting period, Net Profit After Tax (NPAT) was up 15% to $72.7m, Earnings Per Share (EPS) up 15%, dividend up 8%, share price up 43% and Total Shareholder Return (TSR) for 2021 was 45%.

The company clearly sees SaaS as the future referring to the old model as the "legacy license business" in their financial statements.

Governance and culture

The annual report shows the TNE Board has a broad range of skills and experiences, and all of the expected committees, frameworks and policies are in place.

The Board acknowledges they do not meet the ASX corporate governance guideline for an "independent Chair" but argue that Adrian Di Marco is the best person to lead the company, as demonstrated by his proven track record of shareholder wealth creation. ASA welcomes Mr Pat O'Sullivan's appointment as Lead Independent Director which is in line with the ASX Corporate Governance Council Principles and Recommendations for companies with a non-independent Chair.

One area where Technology One is out of step with other listed companies is gender diversity on the Board. Only two out of nine directors (22%) are female which is well below the generally accepted target of at least 30%.

The company recently published a sustainability report which is aligned with the UN Sustainable Development Goals. Some key observations include:

- Their exceptional workforce gender balance with 36.5% women, well ahead of the industry average.
- Their recent certification as carbon neutral through a combination of reduced travel and energy usage and the purchase of carbon offsets.
- Their pledge to donate 1% of their profit, product and employee time to charitable causes.

Workforce culture seems positive with many activities designed to foster a sense of belonging and to combat the isolation of remote working during COVID. This year, Technology One received more than 6,500 recruitment applicants which confirms their reputation as an employer of choice.

Key events

Three significant events occurred during the year.

- A plan was announced to end the on-premise business by October 2024 which will realise the vision to be a pure SaaS company. Most remaining non SaaS customers have welcomed the certainty of a transition date and many have made plans to move to the new platform.
- The UK division continues to grow and delivered its first profit of $1.6m, compared to a break even result last year. Localisation of the product for the UK market is proceeding well and enough modules have been completed to offer a complete UK solution, albeit with less functionality than offered to Australian customers.
- Scientia, a UK company servicing the higher education sector, was acquired for $23m. This will add advanced academic scheduling and timetabling to the OneEducation product. Integration of Scientia is proceeding well from both a technical and organisational perspective.

Summary

(As at FYE)	**2021**	**2020**	**2019**	**2018**	**2017**
NPAT ($m)	72.7	62.9	58.5	51.0	44.5
UPAT ($m)	72.7	62.9	58.5	51.0	44.5
Share price ($)	11.36	7.94	7.18	5.58	5.02
Dividend (cents)	13.91	12.88	11.93	11.02	10.18
TSR (%)	45	12	31	13	-14
EPS (cents)	22.64	19.75	18.43	16.14	14.20
CEO total remuneration, Statutory ($m)	1.95	1.77	1.61	1.40	1.15

For 2021, the CEO’s total statutory remuneration was 20 times the Australian Full time Adult Average Weekly Total Earnings of $93,444 (based on May 2021 data from the Australian Bureau of Statistics).

Item 2	Resolution 1 – Election of Director – Pat O'Sullivan
ASA Vote	**For**

Summary of ASA Position

Mr Pat O'Sullivan is a Chartered Accountant with a long history of senior management and board positions. He was the COO of Nine Entertainment for six years and, before that, CFO of Optus for five years. He is currently Chair of carsales.com and SiteMinder and Deputy Chair of Calvary Health. Pat previously served as a Director at iiNet, iSelect, APN Outdoor, iSentia, Marley Spoon and Afterpay. He is a graduate of the Harvard Business School's Advanced Management Program.

On 2 March 2021, Pat was appointed to the Technology One Board as Deputy Chair and Lead Independent Director and now seeks election as a Director.

ASA welcomes Mr Pat O'Sullivan's appointment as Lead Independent Director which is in line with the ASX Corporate Governance Council Principles and Recommendations for companies with a non-independent Chair.

"If the chair is not an independent director, a listed entity should consider the appointment of an independent director as the deputy chair or as the 'senior independent director', who can fulfil the role whenever the chair is conflicted."

However, two aspects are worth consideration: workload and gender. On the topic of workload, the ASX Corporate Governance Council Principles and Recommendations are clear.

"The role of chair is demanding, requiring a significant time commitment. The chair's other positions should not be such that they are likely to hinder effective performance of the role."

Given that Mr O'Sullivan already holds two Chairs and a Deputy Chair, the addition of a second Deputy Chair role may put unreasonable demands on his time.

At a pre-AGM meeting, two Non Executive Directors (Jane Andrews and Richard Anstey) vouched for Mr O'Sullivan's dynamism and commitment to this new role. Neither had any concern about his ability to devote the time and effort required.

On the gender issue, only two out of nine directors (22%) are female which is well below the 30% recommended by the ASX Corporate Governance Principles, the ASA voting guidelines, the ASX 200 average and the Board's own diversity target.

The benefits of increased diversity in decision making bodies are well known. Data published by the ASX shows companies whose boards are more diverse are often more profitable, have better risk management and have better corporate governance outcomes.

Gender diversity targets are noble, but equality won't just happen, there has to be a will and a conscious decision to make it happen. The role of boards in this debate is to create opportunities for suitably qualified female candidates to be nominated. Appointing another male director appears to be a missed opportunity.

At a pre-AGM meeting, two Non Executive Directors (Jane Andrews and Richard Anstey) explained they had a large number of applicants for the role, both male and female. Some women were short listed, but Mr O'Sullivan was, in their determination, clearly the standout candidate and was offered the position on merit.

Although the ASA would have preferred a female nominee, the creation of the Lead Independent Director role is a welcome advance, so we support Pat's election.

Item 3	Resolution 2 – Re-Election of Director – Richard Anstey
ASA Vote	**For**

Summary of ASA Position

Mr Richard Anstey's credentials as a technology entrepreneur are impressive with a career spanning 40 years including the successful sale of seven companies as well as ongoing involvement in more than 30 enterprises.

Mr Anstey is a Board member of Queensland University of Technology-Entrepreneurship, a Fellow of the Australian Institute of Company Directors and a Fellow of the Australian Institute of Management. He continues his career in venture capital and corporate advisory roles as a founder of iQ360 Pty Ltd.

Richard's skills and experience are, no doubt, relevant to Technology One's Board however after 16 years in the role, can he still be considered "independent"?

ASA's voting guidelines suggest a director ceases to be independent after 12 years. The ASX Corporate Governance Principles recommend a shorter tenure of 10 years but acknowledge that long service does not automatically lead to a lack of independence.

At a pre-AGM meeting, two Non Executive Directors (Jane Andrews and Richard Anstey) spoke on the topic of Richard's independence. Richard acknowledged he had been on the board for a long time but said he still felt independent. His other commitments give him the opportunity to interact with many other technology companies and he feels this keeps him fresh and he continues to bring new ideas and perspectives to the Technology One Board. Jane endorsed Richard's independence of thought and action and stressed that long tenure does not automatically lead to a loss of independence.

The Technology One Board is undergoing a process of renewal with several new Independent Directors appointed (Andrews in the FY16, Doyle in FY18, Rosenberg in FY19, Ball in FY20 and O'Sullivan nominated in FY21). Given that the majority of Independent Directors are relatively new, this is in line with the ASX Corporate Governance recommendation for a mix of long tenures for experience and short tenures for new ideas.

Consequently, ASA will vote undirected proxies for Richard Anstey's re-election but requests the Board consider his independence in the future as the more recent Directors gain experience.

Item 4	Resolution 3 – Re-Election of Director – Sharon Doyle
ASA Vote	**For**

Summary of ASA Position

Ms Sharon Doyle is the Executive Chair and majority owner of InterFinancial, a corporate advisory firm which helps organisations define and accelerate their strategic growth initiatives. She has an appreciation of the challenges facing technology companies and a strong understanding of the dynamics of the software as a service model.

She holds a Bachelor of Laws (Hons) and Bachelor of Information Technology (Dist) from the Queensland University of Technology, as well as a Graduate Diploma of Business Administration from the University of Queensland. She is a qualified member of the Australian Institute of Company Directors.

Ms Doyle is a Non-Executive Director at Auto & General. She was previously Vice President at Mincom, one of Australia's most successful enterprise software companies.

Her skills and experience are directly relevant to the Technology One Board and her relatively recent appointment in 2018 strengthens her credentials as an Independent Director. As one of only two female Directors, her reappointment is crucial to meet the Board's diversity goal of "not less than 30% of the Board to be of each gender by 2025".

Item 5	Resolution 4 – Adoption of Remuneration Report
ASA Vote	**For**

Summary of ASA Position

Technology One received a "first strike" at last year's AGM with 61.7% voting against the remuneration report while ASA voted in favour. A board spill is possible if the company receives a second strike. It is worth reflecting on the reasons for the negative vote before we discuss this year's remuneration report

The primary concern of the dissenters was the Board's use of discretion to award Long Term Incentives (LTI) even though targets had not been met. The LTI targets were set before the COVID pandemic, and the Board determined it was both unrealistic and unfair to hold Key Management Personnel (KMP) to the original hurdles.

A global pandemic is not a good environment for selling enterprise software so failure to meet the targets was beyond the control of the executive team and is not a reflection of any lack of effort on their part. This is the first time in the company's 33 year history that the Board has used their discretion, and it seems like exactly the situation for which the Board has that power.

The Chair, Adrian DiMarco, made his position very clear at the AGM and followed up with a series of interviews in which he criticised "arrogant" proxy advisers bullying companies over "governance correctness". He pointed out that the discretion only related to $210K of LTI which was not material for the company but was for the three executives concerned. Mr DiMarco said the first strike against the company was "needless distraction for our business" and caused significant angst for the leadership team.

This year's annual report includes a written response to the first strike that shows no deviation from Mr DiMarco's previous position. Noting that in the period in question the company delivered record revenue (up 4%), record profit (up 8%) and record SaaS ARR growth (up 32%).

In comparison, the FY21 remuneration report is a non-event. No Board discretion was exercised in FY21 and some changes have been made to the remuneration framework. These include:

- Improved readability of the Remuneration Report.
- Clarifying that the Malus provision for Deferred Short Term Incentives (STI) and LTI considers Executive KMP expectations (e.g. code of conduct) and other irregularities. This was the existing practise, but it has now been formalised.
- Clarifying that the Retention Bonus is actually an STI deferral component.
- Disclosing progress against our mandatory shareholding requirement for Non-Executive Directors.

Technology One's remuneration framework is primarily a profit share model that it is heavily biased towards STI measured against Net Profit Before Tax. With the bulk of their remuneration at risk, executive performance is encouraged as under-performance would have a significant negative impact on their remuneration.

The Remuneration Committee believes the framework is working as designed, with a clear correlation between shareholder wealth creation and executive remuneration in both the short-term and long-term. Total Executive KMP remuneration grew by 12% YoY which is well below the 19% growth in NPBT. Over five years remuneration is up 11% vs NPBT growth of 13%.

None of the executives appear to be excessively compensated compared to their peers in other high growth technology companies and the remuneration framework seems appropriate for a company with a SaaS ARR revenue stream.

Please refer to Appendix 1 for more detailed analysis of the Remuneration Report.

Item 6	**Resolution 5 – Contingent Resolution to Spill the Board**
ASA Vote	**Against**

Summary of ASA Position

Hopefully, a second strike will be avoided, and this resolution won't be voted on.

ASA votes against board spills where removing all directors who signed off on the remuneration report and who were not up for election or re-election at the AGM is disruptive to the company delivering on its strategy. An orderly development of the board is preferred unless a complete shake-up is warranted.

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Appendix 1
Remuneration framework detail

TNE’s remuneration framework is primarily a profit share model that it is heavily biased towards Short Term Incentives (STI) measured against Net Profit Before Tax (NPBT). With the bulk of their remuneration at risk, executive performance is encouraged as under performance would have a significant negative impact on their remuneration.

In other businesses, this might be a cause for concern as it could encourage short-term thinking or risk taking. However, with a Software as a Service (SaaS) model, with its relatively fixed cost base, today’s sales turn into not just this year’s profits but also ongoing Annual Recurring Revenue (ARR) which provides long term shareholder value.

The components of the remuneration framework are as follows:

- **Fixed.** The cash component is quite low compared to other ASX-listed technology companies.
- **Short Term Incentives (Current).** Each executive agrees on an STI target at the commencement of their contract term and from this the “Executive Net Profit Before Tax” is determined. This is effectively their share of the profit before deducting tax and incentives. This percentage grows with each year of service. STI is uncapped to retain executives and encourage high performance over the long-term.
- **Short Term Incentives (Deferred).** A quarter of STI is deferred for two years to encourage retention. If an executive resigns within this period, they forfeit any deferred STI.
- **Long Term Incentives.** Between 75% and 100% of the fixed component is payable as a LTI linked to company growth and shareholder wealth creation. The metrics are Total Shareholder Return (TSR) against the ASX All Technology (XTX) index and Earnings per Share (EPS) growth with both averaged over a three year period. For each metric, there are mid and stretch targets to encourage outperformance. All remuneration components except LTI are paid as cash.

The FY21, remuneration outcomes can be summarised as follows.

- Net profit before tax growth of 19%.
- No increase in fixed remuneration.
- STI outcomes up 18%.
- LTI outcomes up 4%, although this varied +/- between individual KMP.
- The Executive Chair was offered an LTI of $400,000 which he declined as he has in previous years.
- Board fees remain unchanged at $141,000 per Director, including statutory superannuation contributions.
- All Directors, except for Pat O’Sullivan, hold at least the minimum shareholding of one year’s pre tax Directors’ fees in TNE shares. Pat is the newest Director so his holding of 87% is understandable.
- No Board discretion was exercised.

The Remuneration Committee believes the framework is working as designed, with a clear correlation between shareholder wealth creation and executive remuneration in both the short term and long term. Total Executive KMP remuneration grew by 12% year on year which is well below the 19% growth in NPBT. Over five years remuneration is up 11% vs NPBT growth of 13%.

The following table provides a summary of the CEO's remuneration.

CEO rem. for FY21	Statutory $m	% of Total	Framework $m	% of Total
Fixed Remuneration	0.533	27%	0.000	n/a
STI - Cash	0.798	41%	uncapped	n/a
STI - Deferred	0.175	9%	25% of STI for 2 years	n/a
LTI	0.441	23%	75% to 100%	n/a
Total	1.947	100.0%	n/a	n/a

*Deferred STI (refer to section 4.3) was introduced in FY19 for the first time. FY21 amount includes one third of the FY19 award plus one third of the FY20 award plus one third of the FY21 award.