Australian Shareholders' Association Limited
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A train wreck of a year

Company name/ASX Code	Tabcorp Holdings Limited/TAH
Meeting Time/Date	10.00am AEDT Wednesday, 23 October 2024
Location	Pullman Sydney Hyde Park
Registry	Link Market Services
Type of Meeting	Hybrid
Monitor	Mike Muntisov assisted by Steve van Emmerik and Lewis Gomes
Pre AGM Meeting?	Yes, with Chair Bruce Akhurst, Chair-elect Brett Chenoweth, Chair Rem Committee David Gallop, Co Sec Chris Murphy, Investor Relations Terry Couper

1. How we intend to vote

2	Re-election of Ms Janette Kendall as a Director	For
3	Adoption of Remuneration Report	Against
4	Grant of Options to Managing Director and CEO-elect	Against
5	Spill meeting resolution	Against

2. Summary of Issues and Voting Intentions for AGM

The main issues for the AGM are the failure to rectify the many deficiencies of the remuneration scheme after a first strike last year, and the plan under new CEO Gillon McLachlan after the abandonment of the TAB25 performance targets.

3. Matters Considered

Key events

On the positive side, Tabcorp secured a 20-year exclusive Wagering and Betting Licence in Victoria under more favourable conditions than the expiring licence. The company is seeking similar tax reforms in the NSW market.

However, the major event that distracted the company and the market was the resignation of CEO Adam Rytenskild. See further details below under 'Management Changes'.

On 28 August 2024 the company announced that their TAB25 strategy would not achieve its targets on Return on Invested Capital (ROIC), digital revenue market share and operating cost control.

Key Financials

In a soft wagering market, the company announced non-cash impairments of $1.5B (pre-tax) due to the reduced carrying value mainly of the Wagering and Media segment and the NSW Wagering Cash Generating Unit.

	2024	2023	2022
Statutory NPAT ($m)	(1,359.7)	66.5	(118.4)
Underlying NPAT ($m)	28.0	84.3	(18.1)
Statutory EPS (cents)	(59.6)	2.9	(5.3)
Underlying EBIT ($m)	97.4	150.5	95.2
Dividend per Share (cents)	1.3	2.3	N/A
Share Price at End of FY ($)	0.70	1.11	1.065
Total Shareholder Return (%)	-36%	6%	
Realised CEO Remuneration ($)	$3.3m[2,3]	$1.9m[2]	
Statutory CEO Remuneration ($)	$1.1m[2,3]	$2.8m[2]	N/A

Statutory NPAT and EPS are the audited figure from the financial accounts. Underlying NPAT is (usually) an unaudited figure used in management presentations or commentary. Total Shareholder Return is calculated as the share price change over the year plus the dividend declared during the year, divided by the share price at end of previous year. This may differ from the figure quoted by the company.

[2]The figures appear lower than the remuneration details given in the Appendix because no LTI awards are in play given the newly struck scheme and the use of options in the LTI.

[3] Part year only and includes notice period and termination payment

Key Board or senior management changes

The CFO, Daniel Renshaw stepped down in August 2023. His replacement, Mark Howell ex-Coles, commenced in April 2024.

The CEO Adam Rytenskild resigned as CEO on 24 March 2024 due to alleged improper behaviour, reportedly being crude comments made about the head of a regulatory authority. We understand that the board undertook an independent investigation of the incident and satisfied itself that the behaviour was inappropriate and sought Mr Rytenskild's resignation. Subsequently Mr Rytenskild took legal action against Tabcorp claiming unfair dismissal.

Chairman Bruce Akhurst acted as interim CEO while a search for a replacement was undertaken.

After the end of the financial year, on 5 August 2024, Mr Gillon McLachlan, former head of the Australian Football League, commenced as the new CEO.

On September 19, 2024, Tabcorp announced the retirements of Chairman Akhurst and director Justin Milne, apparently after large shareholders expressed their grave concerns about the company performance. The chairman-elect is existing director Mr Brett Chenoweth.

Review of Board on Governance, Transparency, Fairness to Retail Shareholders

Positives

- The Board has an independent Non-Executive Chair and majority of independent directors.
- The Board is close to ASA's guideline threshold of at least 40% female directors (3 of 8).
- Tabcorp policy is for Directors to hold at least one year's worth of member base fees in company shares, within 3 years.
- The company meaningfully discloses ESG issues and risks facing the business and the processes to manage them. It discloses independent ESG ratings of the company in the Annual Report.
- The company has a track record of raising capital fairly by using a pro-rata renounceable entitlement/rights offer (PAITREO).

Areas for Improvement

- The company skills 'matrix' of the directors is more like a skills 'table' and could be improved. However, it was published in the Annual Report this year.
- The ASA is not in favour of companies making political donations. This subject has been discussed with Tabcorp previously and they believe that involvement in political party forums is important in protecting shareholder interests. In FY24 a total of $193,000 in political donations were made (FY23: $161,000). These are typically balanced between the parties. At least Tabcorp now disclose the quantum of donations in the annual report.

4. Rationale for Voting Intentions

Resolution 2: Re-election of Ms Janette Kendall as a Director (for)

Ms Kendall was appointed to the board in August 2021. She has qualifications in Business and Marketing. Her executive career was in marketing at Galaxy Entertainment and Crown Resorts. Her shareholding is on track to meet Tabcorp's shareholding policy (accounting for time from demerger). Her workload is within ASA guidelines, and she is considered independent.

A downside is her membership of the Remuneration Committee which continues with a remuneration scheme which does not align with ASA guidelines and is out of kilter with realistic benchmarks. (See Resolution 3)

On balance the ASA proposes to support her election.

Resolution 3: Adoption of Remuneration Report (against)

The key issue is that Tabcorp's remuneration framework has not reflected the reduction in size and complexity of the company since the de-merger with The Lotteries Corporation. Last year the company suffered a first strike on remuneration as a result.

In response the company reduced the Chairman's fee but did not make any change to the CEO remuneration. The company justifies the remuneration levels by benchmarking against a bespoke comparator group of 46 companies with revenues between $1B and $4B. Tabcorp ranks last by market capitalisation in this group of comparator companies (as at 5/9/24) yet pays its CEO and chair around the top quartile remuneration.

The company argues that they must pay 'above median' benchmarks because they are not competing on a level playing field, they are transitioning the company, and there is a higher degree of personal risk and exposure working in the gambling industry. However, even allowing for 'above median' at the 75th percentile level, the pay is still too high when judged against similar sized companies.

Further, the LTI scheme does not meet ASA guidelines on several measures including the use of options (see Resolution 4).

For these reasons, ASA will be voting undirected proxies against the remuneration report.

More details of the Remuneration framework are provided in Appendix 1.

Resolution 4: Grant of Options to CEO/Managing Director (against)

The Long-Term Incentive (LTI) scheme for the CEO involves the use of options.

ASA does not favour the use of options because their pricing is opaque and can results payouts well in excess of the ordinary shareholder's returns. An illustration of this effect is given in Appendix 2.

ASA will be voting undirected proxies against this resolution.

Resolution 5: Spill meeting resolution (conditional) (against)

This resolution will only be put to the meeting if there is a second strike (>25% vote) against the remuneration report.

ASA believes that a spill of the board could be justified given its inadequate response on remuneration after last year's first strike and the poor performance of the company's TAB25 strategy. However, given the strict and lengthy regulatory checks that directors must go through to be appointed to Tabcorp's board, the disruption to governance and operations would be more severe than for most ASX companies.

Therefore, on balance ASA will vote undirected proxies against this resolution.

Monitor Shareholding

The individual (or their associates) involved in the preparation of this voting intention has no shareholding in this company.

Appendix 1
Remuneration framework detail

CEO rem. Framework (FY25)	Target ($m)	% of Total	Max. Opportunity ($m)	% of Total
Fixed Remuneration	1.500	33%	1.500	22%
STI - Cash	0.750	17%	1.125	17%
STI - Equity	0.750	17%	1.125	17%
LTI	1.500	33%	3.000	44%
Total	4.500	100%	6.750	100%

Positives

- CEO's actual take-home remuneration, as well as the target and maximum opportunity of each component is clearly disclosed.
- At least 50% of CEO's pay is genuinely at risk [67% at target].
- STIs are not more than fixed remuneration (at target).
- The majority of STIs are based on disclosed performance criteria.
- 50% of STIs is paid in equity with a 2-year holding lock.
- No retesting of performance hurdles is allowed.
- Termination payments do not exceed 12 months fixed pay.
- Vesting in a takeover or "change of control" event is at the discretion of the Board.

Areas for Improvement

- The total quantum of the CEO remuneration package is <u>not</u> reasonably within typical benchmarks.
- The quantum of the Chairman's fee is <u>not</u> reasonably within typical remuneration benchmarks.
- The LTI award is based on only one measure, Return on Invested Capital (ROIC), rather than at least two measures favoured by ASA. The company argues that the option exercise price is a second measure.
- ASA's preferred measure for LTI award is Total Shareholder Return (TSR), which was used by the 'old' Tabcorp as one of two measures but has been dropped by the new Tabcorp.
- Actual LTI hurdles and criteria (average measured over 3 years) for FY25 awards are shown in the following table:

Performance Criteria	Contribution % of total LTI award	Threshold performance	Vesting at threshold performance	Performance for 100% vesting
ROIC	100% (i.e. single LTI measure)	8.3%[1]	35%[1]	9.7%

[1] Target performance is 9.0% which results in 50% vesting

- The LTI award is in the form of options which ASA does not favour. (See Appendix 2 for why)
- The options, by necessity, are priced at fair value via the Black-Scholes model. This is not easy for most shareholders to understand.
- LTI hurdles are measured over three years, not ASA's preferred four years or more.

The company changed its remuneration peer group in FY23 to companies with revenues between $1B and $4B in the ASX50-200. Tabcorp ranks last by market capitalisation in this group of 46 companies as at 5/9/24.

Appendix 2 - Scenario Analysis of Tabcorp LTI options scheme

Summary

Tabcorp's Long Term Incentive (LTI) scheme involving options can result in rewards to the CEO and other KMPs not aligned with ordinary shareholder's experience.

Under Tabcorp's scheme it is possible for the CEO to earn a payout of two times the reward under a conventional rights scheme for the same performance.

In one scenario the LTI payout could increase by $5m for an EBIT performance increase of $15m.

The LTI scheme

Tabcorp's single performance measure for the Long-Term Incentive (LTI) award is Return on Invested Capital (ROIC). ROIC is defined as underlying EBIT divided by [shareholders equity plus net debt].

If the ROIC performance measure is met, then some options awarded as part of the LTI scheme will vest (35% to 100%).

'Fair' pricing of options is based on the Black-Scholes model which relies on certain inputs such as risk-free rate, duration of option, volatility etc.

In the FY24 scheme, the 'fair price' of options was $0.13 when the Tabcorp share price was $0.815 (p89 2024 Annual Report)

The current Tabcorp share price is $0.50 (30/9/24). For simplicity let's assume an option price of $0.10 for this illustration. At this price a total of 30 million options ($3M LTI quantum divided by $0.10 per option) will be awarded to the CEO with an assumed exercise price of around $0.50 (current share price).

The following table sets out the key LTI ROIC performance targets set by Tabcorp for the FY25 LTI, and their equivalent EBIT values.

ROIC PERFORMANCE LEVEL	EQUIVALENT EBIT[1]	% OF OPTIONS VESTING
8.3%	$175M	35%
9.0%	$190M	50%
9.7%	$205M	100%

1. BASED ON SHAREHOLDER EQUITY OF $1,247M (P94) AND NET DEBT OF $860M (P106 OF ANNUAL REPORT)

As a reference, in FY23 Tabcorp achieved an EBIT of $150M with an average share price of approximately $1.00 in the 30 days after announcing the result.

Scenario 1

In this scenario it is assumed that the ROIC achieved is 9.0% or $190M EBIT. From the table above one can see that 50% of options will vest, namely 15 million options.

If we assume the same Price/net enterprise value ratio from FY23 then the Tabcorp share price could be of the order of $0.77.

Based on the ‘net settlement’ procedure set out in the Remuneration report, the CEO would then qualify for 15 million x ($0.77 - $0.50) = **$4.05 million**.

If the CEO was issued the more common share rights on the same terms instead, his LTI payment would be worth 50% x 6 million shares ($3M LTI quantum divided by $0.50 share price) x $0.77 = **$2.3 million**. This would be the same experience as a shareholder who purchased shares at 50c.

Scenario 2

In this scenario it is assumed that the ROIC achieved is 9.7% or $205M EBIT. As a result, 100% of options will vest, namely 30 million options.

Using the same assumptions and calculations as in Scenario 1, the share price could be $0.81 and the payout to the CEO would be **$9.3M** (30 million x ($0.81 - $0.50), whereas under a rights scheme the payout is worth **$4.9M** (100% x 6 million shares x $0.81).

Scenario 3

In this scenario, the ROIC performance just fails to reach the threshold level of 8.3%, or EBIT of $175M.

In this case no options would vest so there would be no reward under the LTI.

This would be the same under a rights scheme.

Relativities

It is interesting to note that if the CEO can lift EBIT performance from $190M (50% award) to $205M (100% award), that is by $15M, the LTI payment to the CEO could increase by $5M. It should be noted however that the ROIC/EBIT performance measurement is an average over three years.

Further, if the share price exceeds those assumed then the options scheme delivers a greater multiple of that achieved under the more common rights scheme.

Disclaimer

The scenarios presented are merely simplified illustrations based on the assumptions stated and are not intended as forecasts nor likely outcomes.