Executive Remuneration in Australian Biotechnology

2014
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Introduction

2013 signalled a turning point in the global Life Sciences economy. As the Biotechnology economic cycle turned and a window in the US IPO market was thrown wide open, businesses rushed to take advantage of burgeoning capital raising opportunities.

Inevitably, reinvigorated investor appetite for the sector spilled over to this part of the world. Although the number of new Biotechnology listings in Australia could be described as modest, capital-starved Australian Biotechs had greater range and viability of alternatives to pursue.

Well managed organisations, with strong leadership and options at-the-ready, moved swiftly and substantially advanced their prospects in these changed circumstances.

The unique demands of the Biotechnology sector have always required their leaders to think strategically, be nimble and be decisive. However, when the fundamentals of an industry change rapidly, such attributes can be the difference between those that succeed and those that don’t.

Developing a pool of both Executive and Non-Executive leadership talent is an ongoing challenge for the Australian Life Sciences sector. Identifying, selecting, attracting and retaining this talent presents an individual challenge for each participant in the sector.

By focusing on Life Sciences as a distinct and unique sector, HPM Executive’s Remuneration Review has been developed with these challenges in mind. Compiled annually, it is intended to provide guidance to Boards of Directors and Chief Executives of Australian Biotechnology companies, on remuneration benchmarks specific to their sector.

HPM Executive

HPM Executive is a research-lead, retained Executive Search firm. We conduct senior Executive Search assignments and provide Human Resource Consulting services, exclusively within the Health & Life Sciences sector.

Our boutique structure fosters flexibility, ensuring alignment with the specific needs of individual customers. Clients greatly value our ability to grasp their business strategy, assimilate technical or scientific concepts and generate innovative sourcing strategies.

HPM Executive is particularly oriented toward the Biotechnology sector. We routinely engage with the Board and Executives of both listed and unlisted biotechnology companies to help them overcome the challenges of Talent Management.
Chief Executive Officer

General Observations

It has become commonplace that this Review reveals only minor change in Base remuneration paid to Biotech CEOs.

2013 was no exception, where the average CEO Base remuneration package remained essentially unchanged.

However, we also regularly report sizeable swings (both positive and negative) in the value of CEO Total compensation.

Belying the strong rises registered last year, the average CEO Total compensation package was off around 8%.

This softness is probably due to falls in the value of equity-based performance incentives in 2013.

We continue to observe considerable remuneration variance within the CEO job family, with Base compensation ranging from $101,000 to $744,000. Total Compensation packages ranged up to $1.3m in the 2013 financial year.

Performance Incentives

Fewer than half of Biotech CEO’s received a Short-Term Incentive Last year (41%), although the average bonus was around 4% higher, at $91,800.

Growth in the quantum of cash bonuses has been reported in 4 of our past 5 Reviews, though the proportion of Base remuneration (27% in 2013) remains consistent throughout this period.

We were interested to note that all but one of the Executive job families, each of whom report into the CEO, were more likely than their CEO to receive a cash bonus.

Although fewer CEO’s were granted options in 2013 and the reported value of option grants fell to the lowest level recorded, Long-Term incentives remain a key element of CEO remuneration,

We remain vigilant to emerging trends regarding the use of Long-Term Incentives in the sector. In particular, we consider what impact changes in tax legislation have on option grants and the potential to deter use of Equity-based compensation.

In this light, we note with interest, steady growth in the value of LTIs paid to CEO’s over the past 4 years.

Currently, a quarter of all ASX listed company CEO’s are not paid any form of At-Risk remuneration. This proportion is consistent with our past observations.

Interestingly, the highest paid executive in this years’ review was CEO of one of the Small Cap companies, valued at less than $20m.

This package was worth about 8.5% of the value of the company. By contrast, we found that the CEO’s of the largest companies in the survey typically received Total Compensation packages in the order of 0.03-0.04% of the value of their organisation.

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<th>25th Percentile</th>
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<tr>
<td>Total Compensation</td>
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<tr>
<td>Short Term Incentive</td>
<td>$44,800</td>
<td>$61,700</td>
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</table>
Senior Executives

Remuneration by Market Capitalisation

Some minor fluctuations occurred within CEO Base remuneration when compared by Market Capitalisation. However, similar to previous years, there are distinct differences in remuneration paid to CEO’s of Larger companies ($60m+).

CEO’s of the largest companies saw the greatest fall in the value of their Total compensation, due principally to a drop in value of Long-term Incentive grants by up to 50%. When the fall in STI participation for this cohort is also taken into consideration, we saw Total compensation packages drop by up to 23% for Larger company CEO’s.

Notwithstanding, average Base remuneration for larger companies CEO’s is $417,000, almost 35% greater than their smaller company colleagues.

Smaller companies make up the bulk of members of the Listed Biotech sector, with 46 organisations in our review holding a Market Capitalisation less than $60m.

While Base remuneration remained relatively stable within this cohort, Short-term Incentives paid to CEO’s of the Smallest companies (<$20m) actually rose 13% in the period.

Again, CEO’s of smaller companies were significantly less likely than their larger company counterparts to receive some form of At-Risk remuneration. 34% of CEO’s of the smallest companies received no performance incentive at all.

Inter-state Variation

When Board Remuneration Committees review the structure and value of CEO remuneration packages, there are numerous factors to consider, not least of which are geographic norms.

It has long been noted in this review that Victoria is home to the largest proportion of Listed Biotechnology companies in Australia.

Accordingly, we typically find Victorian CEO’s are more highly remunerated than their counterparts in other locations. This situation is likely accentuated by the fact that two-thirds of the larger companies in our review (who pay more), are registered in Victoria.

However, the gap in remuneration that previously existed between states has diminished over time. We now see CEO Base remuneration as being more or less equal across the country.

While average CEO Base remuneration remained stable in NSW, it fell in Victoria (-6%), while CEO’s of SA/WA/QLD based Biotechs saw their average Base salary rise by 12%.

Total compensation packages were generally reflective of the national trend, falling heavily in Victoria (over 20%), less so in NSW (-7%) while rising slightly (3%) in SA, WA & QLD (the smallest regional cohort).

Once again, it would appear that cuts in Long Term Incentives are the primary cause of these falls.

CEO Remuneration by Market Cap.
Chief Operating Officer

The Chief Operating Officer/General Manager job family remained the most highly remunerated member of the Biotechnology Executive group in 2013.

The year-on-year remuneration trend for COO’s was generally positive. Average Base remuneration increased slightly (2.8%) and Total compensation rose by a similar amount.

Half of the COOs in this review received a Short Term Incentive, though the average bonus was a slightly lower than the previous year.

COO’s/GM’s based in NSW fared better than their interstate counterparts, registering above average increases (8%) in both Base remuneration and Total compensation.

COOs in the largest companies ($100m+) also received above average increases in Base remuneration (14%).

These rises were offset by Total compensation falls of a similar size for GM’S in the smallest companies (<$20m).

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<tr>
<td>Total Compensation</td>
<td>$218,400</td>
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<td>$371,200</td>
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<tr>
<td>Short Term Incentive</td>
<td>$21,500</td>
<td>$37,500</td>
<td>$56,100</td>
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Chief Scientific Officer

In recent reviews, we have reported substantial remuneration variability in the Chief Scientist job family. This apparent state of flux continued into 2013.

Average Base remuneration rebounded, rising 13% on last year and regaining much of the ground lost in recent years. However, the dollar value of average Short Term Incentives fell by over 30%.

Therefore, the average CSO bonus fell from 23% of Base remuneration, to 15%.

Notwithstanding, cash bonuses were paid to 50% of CSO’s - more widely distributed than past observations.

Rising Base remuneration effectively limited the negative impact falling STI’s had on Total compensation. CSO Total compensation rose 11% on average from the prior year.

By far the biggest beneficiaries of this improvement were Chief Scientists in mid-sized companies ($20-60m).

Both the reported value of Long Term Incentives and CSO participation in equity-based remuneration remained steady.

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<td>$275,300</td>
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<tr>
<td>Short Term Incentive</td>
<td>$19,000</td>
<td>$29,300</td>
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Senior Executives

Chief Financial Officer

Our review of 2012 identified an arrest in a long-term decline in remuneration packages paid to Biotech CFO’s. In 2013, CFO remuneration was a case of marking time.

Base remuneration remained essentially on par with the prior year, while average Total compensation packages were slightly lower, (-2½%).

While participation in Short-Term Incentives remained at similar levels to last year, actual value of the average bonus fell around 4%. CFO bonuses are around 16% of the average Base salary package.

Long-Term Incentives paid to this job family rose minimally over the period.

Total compensation for CFO’s of the smallest companies (>$/20m) barely moved, mid-sized ($20-60m) rose strongly and larger company CFO packages ($60-100m) fell away sharply.

It appears that most gains went to CFO’s of the largest companies ($100m+), where remuneration packages rose 11%.

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<tr>
<th>Base Remuneration</th>
<th>Total Compensation</th>
<th>Short Term Incentive</th>
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<td>50th Percentile</td>
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<tr>
<td>75th Percentile</td>
<td>$246,300</td>
<td>$36,900</td>
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Commercial Director

The Business Development job family also experienced something of a recovery from accumulated, substantial falls in remuneration reported over the past few years.

However, remuneration trends for the Biotechnology’s most senior Commercial executives could be best described as sluggish.

While average Base remuneration paid to Commercial executives improved 8.5% in 2013, the average Short-Term Incentive was slashed, down 50% from the year prior.

On one hand; nearly half the Commercial Directors of ASX Listed biotech’s received a bonus. On the other, the average bonus was only 10% of Base remuneration, and the smallest performance incentive of this year’s review.

Total compensation for this job family was up over 5% and the value of Long-Term Incentives remained steady.

Nonetheless, this years average Total compensation figure is only 6% higher than that reported in 2008 and is actually 3% lower than the average over the past 7 years.

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<tr>
<th>Base Remuneration</th>
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<tr>
<td>75th Percentile</td>
<td>$234,500</td>
<td>$30,400</td>
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</table>
Senior Executives

Clinical Operations

2013 was a positive year for remuneration in the Clinical job family, rebounding well from poor outcomes reported the year earlier.

While we recorded slightly positive changes in Base remuneration, up 2%, the average Total compensation package rose substantially for this group, up 11% over the prior year.

We believe this is due, in the most part, to a significant increase in value of the average Short–Term Incentive. STI’s were more than twice as large as those paid last year.

The most notable results for this group were seen in mid-sized companies ($20-60m). Here, average Total compensation packages paid to this cohort were 35% higher than the national average.

In our opinion, this is probably indicative of the intensity of Clinical development many organisations pursue at this stage of their life cycle.

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<td>$147,200</td>
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<td>$204,100</td>
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<tr>
<td>$223,400</td>
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Development & Discovery

By far the smallest cohort in our review, the Development & Discovery job family is prone to some inconsistency. Both negative and positive outcomes need to be considered in light of the small sample size.

We reported last year that this cohort had recovered from falls recorded in 2011. In 2013, we saw the average Base remuneration again drift down 3%.

Short-Term Incentives plummeted, down 40% on the prior year, inevitably translating into falls in the average Total compensation package, which was down 12%.

However, what really influenced salaries was the evaporating STI participation rate. 38% of executives in this job family received a bonus in 2013, compared with 90% the year earlier.

Conversely, the value of Long-Term Incentive grants made to this group actually rose substantially, up 24%.

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<td>$198,600</td>
<td>$200,800</td>
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<tr>
<td>$241,600</td>
<td>$305,400</td>
<td>$35,000</td>
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For this year’s review, we were able to collate the remuneration details of 166 Non-Executive Directors of Australian Biotechnology companies.

In 2013, the average Director’s Base fee was almost $55,000. This represents a slight dip, (-4.5%) on observations reported last year.

Average Total emoluments received by Non-Executive Directors also fell, in line with the drop in base fees.

Further analysis reveals that the majority of these falls were experienced by those Directors remunerated at the higher end of the spectrum.

This report has commented widely on the use of equity-based compensation for Board Directors. Non-Executive Directors participating in such schemes rose sharply in 2013 to 28%, although the average value of equity grants actually fell.

Base fees paid to Chairmen of ASX Listed Biotechs regained some ground, rising slightly (2.5%) in 2013 to an average of $91,000.

However, this small increase was entirely negated by a 7% fall in Total emoluments, the average of which was $105,600.

Although the proportion of Chairmen receiving equity-based compensation has risen to 30%, the average value of these grants was dramatically lower (-48%) than observed in 2012.

When analysed by market capitalisation, we have previously identified marked differences in compensation within this cohort. We noted with interest that in 2013, such differences were less apparent than typically observed.

Although Chairmen of larger companies ($60m+) were slightly more likely to receive equity-based compensation, the average value of these grants were less than half that received by their smaller company counterparts.
Methodology

This review examines public companies listed on the Australian Securities Exchange. We focus on organisations engaged at all stages of Research, Development and Commercialisation of Life Sciences related technologies.

The exchange identifies over 100 of its members as constituents of a Health Care & Biotechnology sector. In order to provide meaningful comparison, our cohort excludes companies in the ASX200 healthcare index and those with registered offices located overseas. We identified 67 companies which had supplied sufficient data for us to review.

The Corporations Act requires a company’s Annual Report to include detail related to the remuneration of each director of the company and five named company executives who receive the highest remuneration for that year. The 2013 Annual Reports of these 62 companies were source documents for analysis.

Remuneration

This review provides commentary and insight on remuneration outcomes, composition and trends. Our research is focused on identifying the following core elements of remuneration:

**Base Remuneration** – salary or professional fees (in the case of Non-Executive Directors) and superannuation contribution.

**Short Term Incentives (STI’s)** - compensation linked to the achievement of specified performance hurdles, ”at risk” of not being earned (typically cash bonuses).

**Total Compensation** – the total of all financial and fringe benefit payments that together make up the total reportable employment cost.

Base remuneration tends to be constant over a 12-month period and is negotiated in consultation with the Chief Executive Officer and/or Board of Directors. It is a reasonable benchmark for like-for-like comparison within the sector.

This review reports on Total compensation without discriminating between the occurrence or value of fringe benefits.
Methodology

Job Families

The high degree of inter-company variability in the roles of named company executives is a significant barrier to an effective sectoral remuneration review.

In order to create a valid platform for like-for-like comparison, we allocate individuals to one of the following, industry-common job families, as appropriate:

- **CEO** – Chief Executive Officer, the most senior named executive.
- **COO** – Chief Operating Officer, the most senior named General Operational executive, including General Managers and Country Representatives.
- **CSO** – Chief Scientific Officer - the most senior named scientist, excluding Chief Medical Officers
- **Development & Discovery** – this family includes the most senior scientific executives specifically focused on Drug Discovery and/or Product Development.
- **Clinical & Regulatory** – this family includes the most senior executives involved in Clinical Trials, Regulatory Affairs and Quality Control.
- **Commercial Director** - the most senior named Business Development executive. This includes Licensing, Sales and Marketing job families.
- **CFO** – Chief Financial Officer, the most senior named finance executive.

Long Term Incentives

Incentivising continued high performance over the medium to long term is an internationally accepted strategy for attracting and retaining talented staff. We strongly believe Long Term Incentives (typically granted in the form of equity-based compensation) are an essential component of “at-risk” remuneration for both senior executives and Non-Executive Directors in the Biotechnology sector.

Like STI’s, granting of Long Term Incentives (LTI’s) is generally linked to the achievement of specified performance hurdles and in many circumstances, organisations disclose nil payments of Long Term Incentives to certain executives and/or directors.

Notwithstanding, the reported value of LTI’s in an Annual Report are derived from a range of valuation models, utilising subjectively calculated variables. The reported value of any LTI grant may dramatically overstate or understatement their actual value on realisation.

For these reasons, utilisation of Long Term Incentives is referenced, but their value is not a major focus of this review.
Methodology

Other Points of Comparison

Geography is a distinctive feature of remuneration in Australia and has conventionally been a key factor in our assessment of trends in the biotechnology sector. Our 62 companies are geographically distributed as follows; New South Wales - 21, Victoria - 27, with results from 14 companies in Queensland, South Australia and West Australia combined.

Size and maturity are critical differentiators within any sector. This is particularly the case when considering the diverse range of activities engaged in by Biotechnology sector enterprises.

To derive a benchmark for like-for like comparison, we segmented our cohort according to market capitalisation as at 31st June 2013. For the purposes of this review, segmentation occurs at $20m (33 companies); $20m-60m (13); $60m-100m (6) & $100m+ (10).
About The Author

Jason Borrie is a Director of HPM Executive and manages day-to-day client engagements. He has held international consulting and leadership roles in the recruitment industry since 1995.

Following a 10 year career within one of the world’s largest Executive recruitment firms based in Sydney, Jason established the Health & Life Sciences division of a boutique Executive Search firm prior to launching HPM Executive.

Jason has partnered with a broad range of health sector enterprises, many of which focus on research, development and commercialisation of innovative technologies. His clients include International and Australian pharmaceutical, biotechnology and medical device companies, as well as medical research institutes.

Jason has been compiling the HPM Executive Remuneration Review on an annual basis since 2005. This report is extensively disseminated within the Australian Life Sciences community and regarded to be the foremost publication of its type.

For further information regarding this review, to undertake an assessment of individual company remuneration or to find out more about our other services, please contact Jason on +61 421 418 516.

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