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BHP BILLITON SUBMISSION: ISS 2017 BENCHMARK POLICY CONSULTATION

“Europe, U.K. & Ireland Policies - European Pay for Performance Methodology”

We wish to comment on the pay-for-performance model’s method for addressing part-year CEOs.

Question 7 in ISS’s FAQ for the European Pay-for-Performance Methodology describes the approach to part-year CEOs as follows:

7. During the recent financial year, a company had multiple CEOs in post. How does the model handle this?

If the company has co-CEOs in post at the same time, the higher total compensation figure will be used. However, the impact of co-CEO compensation costs may be addressed separately as part of ISS' qualitative executive compensation evaluation.

If only one CEO is in post at any point in time, ISS will typically use the pay of the CEO in office at the end of the fiscal year as an input to the model. Exceptions can be made in case there have been multiple recent CEO changes, in which case ISS will include the pay of the longest serving CEO. For CEOs in office for only part of the year, ISS will calculate an annualized basic pay figure.

We believe this approach will lead to significant distortions in the model’s output where the CEO in office at the end of the fiscal year has only been in office for a short period of time.

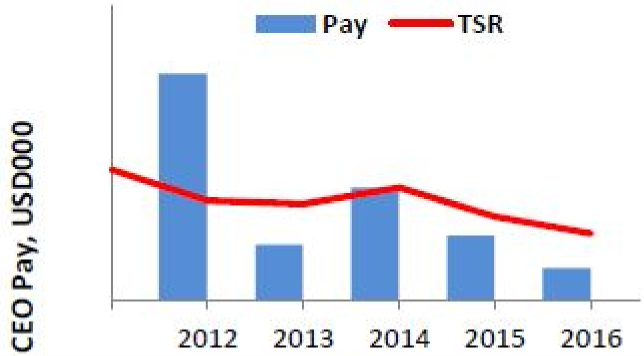
As an example, our current CEO, Andrew Mackenzie, was appointed CEO effective 10 May 2013, only 1.5 months before the end of our financial year (30 June).

The Pay-for-Performance remuneration figure included in the model for Mr Mackenzie is USD 3,925,000. This consists of an annualised base salary of USD 1,700,000 (in line with the FAQ), together with actual (not annualised, and not pro-rated) STI, LTI, pension and benefits.

This is shown in the ‘Absolute Alignment’ (or ‘Pay-TSR Alignment’) graph extracted below from ISS’s proxy voting report on BHP Billiton Plc’s Annual General Meeting.

ABSOLUTE ALIGNMENT

CEO realized pay trends versus value of a USD100 investment made on the first day of the five-year period.



	2012	2013	2014	2015	2016
Pay(USD000)	16,092	3,925	7,988	4,582	2,241
Indexed TSR	76.17	73.69	86.01	64.13	50.96
CEO	Kloppers, Marius	Mackenzie, Andrew	Mackenzie, Andrew	Mackenzie, Andrew	Mackenzie, Andrew

Using a pay figure of USD 3.9 million for 2013 will not produce meaningful outputs from the Pay-for-Performance model when one considers:

- Mr Mackenzie was CEO for a very small fraction of the year: only 14% (10 May 2013 to 30 June 2013). Using only 14% of the largest components of his pay (STI and LTI), and only 14% of his pension, delivers a total pay figure that is clearly too low when the following are taken into account.
- In his prior less-senior role (from which he was promoted to CEO), Mr Mackenzie was paid over $10 million for the year in question (after pro-rating STI and LTI).
- The person who served as CEO for the vast majority (86%) of the year – Marius Kloppers – was paid $15.99 million for the part of the 2013 year he was CEO.

Systematically understating pay means, in terms of the ISS Pay-for-Performance model, that:

- In the part-year CEO's first year in office (i.e. when the abnormally low compensation figure is for the current year in Pay-TSR Alignment), the company will be disproportionately likely to get a good Pay-TSR Alignment score.
- Five years later (i.e. when the part-year pay figure is the figure for Year-minus-5), the company will be disproportionately likely to get a bad Pay-TSR Alignment score.

These outcomes follow as a consequence of (a) the point-to-point methodology used for Pay-TSR Alignment, and (b) the anomalous methodology currently used to calculate part-year CEO pay.

To avoid anomalous outcomes, we believe the methodology for part-year CEOs should involve annualising all relevant components of the pay of the CEO in office at the end of the year.

If you annualise only the salary, and not the other regular components of the compensation package, you will systematically understate the pay of the person in question. The only instance where this would not occur is where:

- the STI and LTI are both zero;

- there is no pension contribution; and
- there are no other benefits, or, if there are other benefits, they are included in full due to being one-off items (for example, in the 1.5 months to 30 June 2013, BHP Billiton CEO Mr Mackenzie relocated from the UK to Australia and was provided with a one-off relocation allowance of US$700,000 which was included in full in the reported part-year pay number).

Kingfisher plc example

For illustrative purposes, included below is another FTSE 100 company, Kingfisher Plc. The CEO pay figure for 2015 is understated due to the current methodology as discussed above. This is clearly evident in the ISS graph at the bottom of this page.

Kingfisher's CEO at the end of the 2015 financial year had been in office for only 55 days. ISS calculated the 2015 pay for Kingfisher's CEO as shown in the table below, which also shows the CEO's pay for the following full year in office:

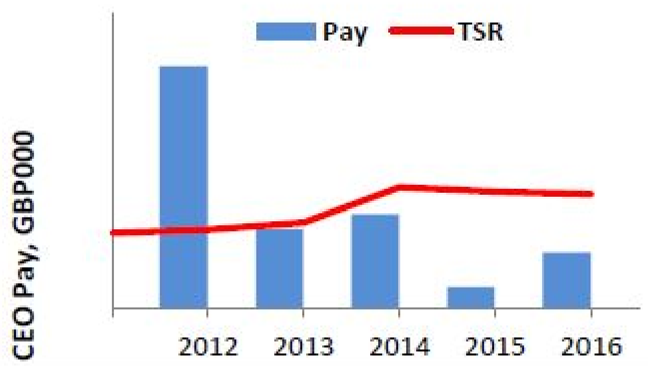
£	2015 – ISS methodology	2016 – actual pay as reported
Base salary	690,000*	700,000
Taxable benefits	13,600	228,100
STI	29,100	967,400
LTI	0	0
Pension	13,000	87,500
Total	745,700	1,983,000

* Base salary: £690,000 (consisting of actual salary of £104,000 for 55 days, annualised)

Comparing the Taxable benefits, STI and Pension rows illustrates why the methodology applied for the 2015 part-year is inappropriate.

ABSOLUTE ALIGNMENT

CEO realized pay trends versus value of a GBP100 investment made on the first day of the five-year period.



	2012	2013	2014	2015	2016
Pay(GBP000)	8,628	2,817	3,334	746	1,983
Indexed TSR	104.45	113.89	160.53	154.76	151.43
CEO	Cheshire, Ian	Cheshire, Ian	Cheshire, Ian	Laury, Véronique	Laury, Véronique