

Regulation of Director and Executive Remuneration in Australia

Productivity Commission Issues Paper

April 2009

1 Introduction

“The Productivity Commission has been asked to report within 9 months (by 19 December 2009) on the framework and structures around the remuneration of Directors and executives of those companies (known as disclosing entities) regulated under the *Corporations Act 2001* (Commonwealth).”

The purpose of this submission is to assist the Productivity Commission to achieve as the end-result, the creation of a regulatory framework where corporations in Australia can flourish and achieve Best-In-Class status at a global level thus strengthening the Australian economy and the community as a whole.

The key for us at *SIMMETHOD*TM is not the level of Director’s and CEO’s remuneration but the degree of alignment between their remuneration and long term value creation for all stakeholders and the strength of the corporation, short and long term, measured through a basket of indicators at the end of their tenure. In other words, the degree of long term value created as measured by a basket of leading operational and financial performance indicators.

Many years ago, delivering a speech at the University in Argentina (where I grew up) I was asked by one of the students if Argentina was a first or a third world country? My answer was that the moment that graduates of Argentinean Universities did not have to leave the country in order to look for a better future, Argentina would become a first world country.

In the same spirit, I consider the ideal outcome of the Productivity Commission “Executive Remuneration in Australia” Final Report, the creation of a the regulatory framework where Australian Corporations can prosper at a global scale with a measurable level of risk, world class opportunities for Australian employees with adequate levels of protection and rewards for every stakeholder, large or small.

This shared purpose, to facilitate the creation of Best-In-Class global corporations in order to strengthen the economy of Australia as a whole, was the driving force behind the creation of the *SIMMETHOD*TM performance measurement and improvement methodology and it is the reason for this submission based on:

- **A lifetime of experience measuring and improving the performance of Australian and global corporations**

- **The creation of a comprehensive performance measurement and improvement methodology based on the 7 Laws of Growth and Value Creation.**
- **The analysis of 2000 global corporations in order to create:**
 - * **Best-In-Class performance templates for each industry sector.**
 - * **A Best Practices Performance Index that enables comparison of businesses from different industry sectors such as trading partners across the supply chain.**
 - * **Risk minimisation alerts based on pre-specified management targets.**

2 Terms of reference

“The terms of reference require the Commission to consider the relationship between remuneration and corporate performance — that is, the degree to which incentives have been built into the remuneration structure to align the interests of directors and executives with those of shareholders. As well as this relationship, there is also a question as to the links between remuneration and individual performance — that is, there may often be a distinction between individual performance of a director or executive and corporate performance.”

“There is no universally accepted standard for performance (whether individual or corporate), particularly in setting benchmarks for incentive payments. Measures of performance could include profit, share price performance and total shareholder returns, return on equity and other measures of investment return. Many businesses will target ‘Key Performance Indicators’ (KPIs). While ideally these should be easily quantifiable — for instance, unit sales — some KPIs can be harder to measure, such as product quality.”

“Each industry is likely to have a different mix of KPIs and companies within an industry will typically highlight different sets of indicators from their peers. Further, there are no established rules for how any of these indicators can be applied in the context of remuneration, especially where a long-term view of performance is sought.”

How should ‘corporate performance’ and ‘individual performance’ be defined? Is it possible to define them in general terms that are applicable across most businesses?

2.1 The new business landscape

In assessing the

- **Effectiveness of a business model,**
- **Strategy or execution of a strategy,**

- Degree of alignment between resources and business objectives,
- Quality of management or
- Efficient use of information within the business.

Special attention must be given to Best Practices developed across a range of global industries.

In the past, there were defined lines between industries sectors and business models did not cross industry lines and tangible assets generated most of the income. However, with the advent of the internet, smart phones, smart cards, new payment methods and a new generation of savvy Internet users, geographical limitations have been removed and intangible assets (such as intellectual property, R&D, human capital, brands, client relationship and databases) have been growing in importance as the lever of growth and value creation.

As a result, businesses all around the world have been either searching for new business models or adapting their existing business models in order to:

- Protect or expand their client base and brands,
- Transfer their costs, services and products to the most cost-effective distribution channels,
- Identify hidden or unutilised intangible assets that are able to maximise the value of the tangible assets or
- Take advantage of new technology and market changes and leverage brands and assets to build a new business model with new income producing streams.

In some industries, barriers to entry have collapsed. In others product delivery and distribution have been turned upside down. These significant changes have occurred because of the creation of new business models using lower cost structures or multiple income streams coordinated across channels. These business models are less reliant on traditional physical assets and more reliant on intangible assets such as client interaction and engagement via the web or mobile channels.

Today's marketplace is interlinked and the performance of a business or industry sector is impacted by the performance of all other sectors. Efficiency initiatives and their benefits are shared across supply chains and a common set of business processes is required to fully take advantage of E-commerce.

All this has made necessary the creation of new strategies and business processes supported by new performance metrics that could be used as a yardstick to assess business strategies,

organisational structures, business processes, human capital and management effectiveness. Today more than ever the question to be asked is: How long would it take for senior executives to realise that their business strategy is not being followed?

Speed and interactivity is now more important than ever with professional workforces used to instant feedback and responsiveness in the way they shop, play and work. As a result, there is a need for an interactive and flexible performance measurement and improvement methodology. It must be able to keep pace with constantly changing business environment, focus their performance in the key profit drivers of the business and provide instant feedback and training to the workforce.

There is a new generation of consumers and workforce. They do not respond to traditional media advertising, they crave interactivity and instant responses. They must be measured, trained, motivated, managed and led interactively via new self-measured methodologies that empower every resource to maximise their contribution to business objectives.

2.2 In the new business landscape the way you measure determines your result!

The **SIM**METHOD™ Best Practice performance measurement and improvement methodology fills a gap in the marketplace offering a fast and cost effective yardstick and business insight to motivate employees to a Best Practice level of performance.

SIMMETHOD™ reports, Best Practice Management Index and metrics are based on a proprietary database of global companies which is constantly updated with the latest available public domain information. This information is filtered, calculated and sorted through the 7 Laws of Performance Improvement and Value Creation to create the **SIM**METHOD™ metrics, reports, templates, Best Practice Management Index and alerts.

The power of the **SIM**METHOD™ methodology and metrics lie in their ability to provide in simple terms a window into a company business model and management effectiveness and the ability to find a common language across industries. This factor is a source of competitive advantage in the quest for new and optimised business models that are able to leverage intangible assets in order to improve the return and value of tangible assets with reduced cost structures and new income streams.

The **SIM**METHOD™ has proven across different business cycles that a basket of operational and financial indicators compared across a group of industries is less open to manipulation and provides a clear indication of future trends.

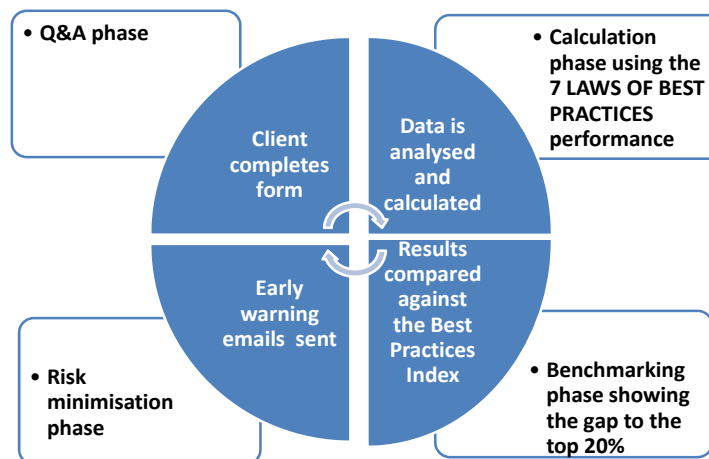
In particular, the analysis of the data using the 7 Laws of Performance Improvement, the search of Best Practices and value creation metrics, the search for leading operational

indicators has been proven to be a good predictor of future trends, financial performance and value creation. The **SIMMETHOD™** can also be used to create Best Practice templates and produce early warning web-based alerts.

3 How the **SIMMETHOD™** addresses the issues highlighted in the terms of reference.

3.1 **SIMMETHOD™** database and benchmarking process

The 4 Phases of the **SIMMETHOD™** Value Creation Cycle



The database contains thousands of global businesses covering every industry and is updated on a periodical basis. As a result, the Best Practice Management Index and the industry metrics keep changing as new information becomes available.

All **SIMMETHOD™** data is management rather than financial information and its objective is to provide a reference point, a new insight, uncover performance obstacles and lead the way towards improved performance. The interactivity of the benchmarking process enables any business to establish a cost effective starting point and monitor either positive or negative trends.

Global business data sources includes sales, profit, assets, market values, information technology, channel utilisation such as internet or mobile, transaction costs, research and development and human resources.

SIMMETHOD™ indicators do not seek to be exact but rather serve as a conduit to ask better questions and seek better answers in the performance improvement and value creation journey.

Sometimes, the value of a metric in itself does not provide the greatest of insights, but valuable actionable knowledge is gained by its ability to provide a trend or a common comparison yardstick with similar companies.

The methodology uses the independent metrics to search and group potential top performers. **Businesses that show extreme values in a basket of indicators are likely to show a positive or a negative operational trend that will ultimately be translated into corresponding financial performance.**

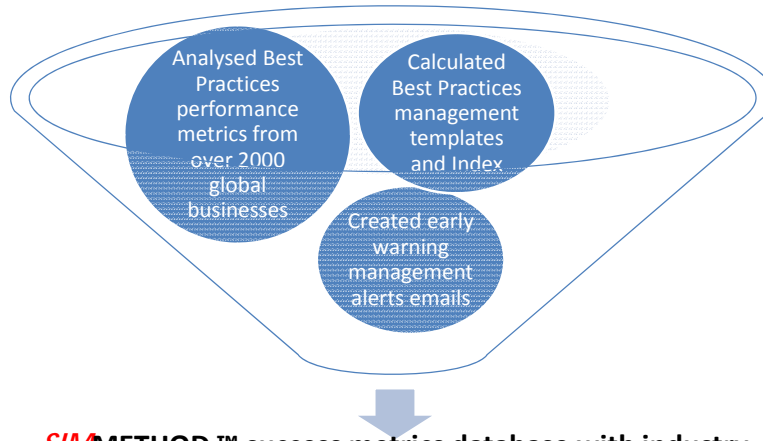
Metrics used to compile the Best Practice Management Index include:

- Metrics unusual in value (top or bottom 20%)
- Metrics above or below averages for the industry
- Metrics that highlight a positive or negative trend
- Value creation (or destroying) metrics
- Alignment of execution to strategy metrics
- Metrics showing the value extracted from human capital (or knowledge)
- Metrics showing the contribution of information technology and overheads to the business

In order to build the Best Practice Management Templates, a score is assigned based on the aggregation of all the metric values plus a particular weight to highlight trends either positive or negative.

SIMMETHOD™

How was the Best Practices performance database created?



SIMMETHOD™ success metrics database with industry templates highlighting the metrics of the top performers and the gap between them and industry laggards.

3.2 SIMMETHOD™ web-based services include:

- 1) **SIMMETHOD™ industry profile reports:** a summary of strategies, business models, benchmarks and Best Practice Management Index scores grouping the companies into potential winners and losers.
- 2) **SIMMETHOD™ early warning reports:** highlighting specific performance issues for a given industry or group of industries
- 3) **SIMMETHOD™ email alerts:** to notify users of specific targets met for a given business or industry (either positive or negative)
- 4) Access and benchmark against the **SIMMETHOD™** industry database
- 5) Cost-effective employee performance management and Best Practices interactive training

3.3 Compelling SIMMETHOD™ value protection for Australian corporations and shareholders alike

SIMMETHOD™ offers clients compelling value and insight into management effectiveness and analysis of future performance:

- 1) **Business executives, strategy teams, Board members:**

- Obtain objective analysis and benchmarks in order to measure and improve performance and to support quality decision making
- Assess the impact of a new strategy, to align execution to strategy, to motivate employees to a Best Practice level of performance and to focus resources in the key profit drivers of the business
- To identify hidden or unutilised intangible assets able to reduce cost structures or generate new income streams
- Empower sale professionals and leverage brands and client relationships to become a trusted adviser to your clients and improve your profit per employee

2) Independent business consultants, accountants and auditors:

- Sometimes it is difficult as an outsider to get objective insight into the effectiveness of a strategy or execution of the strategy and the likely impact on future financial performance. Most available benchmarks focus on process metrics or in sections of a given business and makes evaluation and comparisons of a whole business difficult. **SIMMETHOD™** provides objective comparison across industries of resource management, resource contribution to business objectives and business strategy and management's ability to execute the strategy.
- As part of a change management program, a business reorganisation or a training program. **SIMMETHOD™** supports business professionals in their performance improvement, cost optimisation and change management initiatives.

3) Investors:

- In search of business performance yardsticks as potential predictors of future financial performance.

3.3 Testimonials and awards

- “At AM Corporation as a direct result of using the **SIMMETHOD™** we achieved over \$4 million dollars of cost savings”. John Clark, COO, AM Corporation.
- “The **SIMMETHOD™** methodology added real dollars to our bottom line”. Edmund Khalaf, CFO and Group Vice President Randstad (Select Appointments).

- “The **SIMMETHOD™** performance measurement and improvement methodology provided a powerful analytical basis for our decision making process”. David Hendler, Director, Reebok.
- Awarded a "Top Ten Innovation Prize" by the NSW Department of Trade, Australia in August 2008.

JORGE TABACMAN

SIMMETHOD™

Measuring and improving corporate performance since 1990

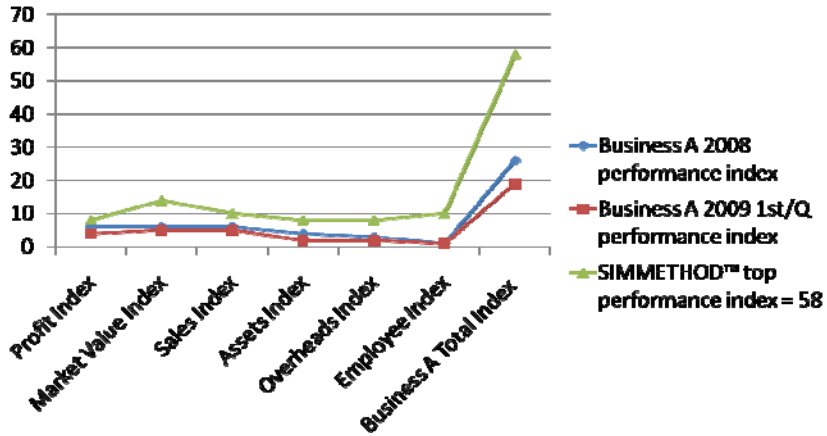
www.simmeth.com

3.4

Examples

SIMMETHOD™

Developing Trend Example



SIMMETHOD™

HR Industry Sector Example

