



SETSCoP Governance Training

What is the role of a Director?

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SETSCoP Governance Training

- Webinar 1 – What is a Board ?
- Webinar 2 – What is the role of a Director?
- Webinar 3 – Tone from the top – the culture and mechanics of Boards



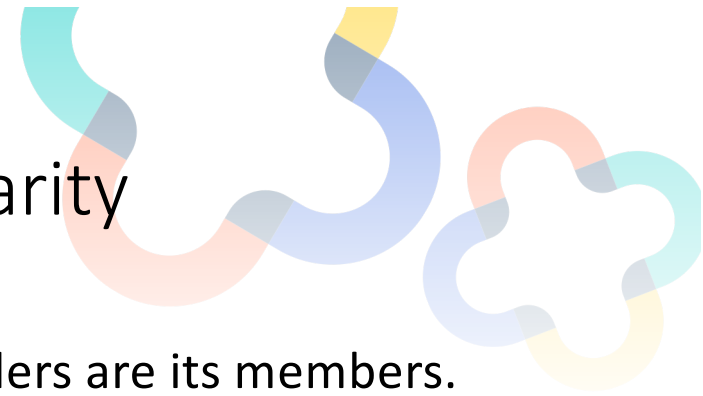
Before we begin...some clarity



We will simplify the interchangeable terms

Board and Management Committee = Board
Directors and Committee Members = Directors

We will discuss this later...some more clarity



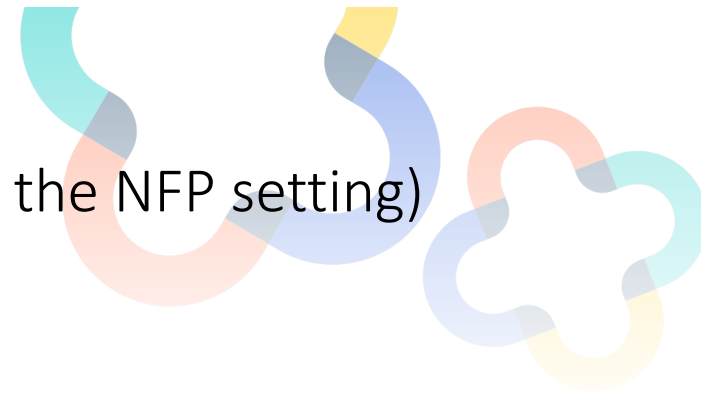
The NFP equivalent of the commercial company's shareholders are its members.

- NFP organisations cannot be owned
- They don't have shareholders (owners)
- They have members

From a governance perspective members play the role of shareholders

What is the role of a Director? – (specifically, in the NFP setting)

- ✓ The 'Fiduciary Relationship'
- ✓ Who is a Director?
- ✓ Director duties – (a couple of case studies)
- ✓ How to fulfill Director duties
- ✓ Director competencies
- ✓ The size & composition of a Board



The “Fiduciary Relationship” ...



- It is where a person has undertaken to act in the best interest of the another and not in her or his own interests.
- It is the legal relationship between the Director and the Company.
- “The duty to act with fidelity and trust”.
- The obligation of undivided loyalty.
- It obliges the Director to act honestly, in good faith and to the best of their ability in the interests of the company.
- It derives from common law, regardless of commonwealth or state legislation, it applies equally to Companies, Associations, Board members and to managers.
- Personal interest, or personal advantage must not override the interest of the company.

Who is a Director?



- A Director is (could be):
 - A person validly appointed - **Director**
 - A person not validly appointed but acts as if they are – **De facto Director**
 - A person who influences or instructs Directors to act – **Shadow Director**
 - A person validly appointed to act in the capacity of a director who is absent – **Alternate Director**
- There are no formal qualifications or minimum standards of competencies to be Director
- Must be over 18 years of age
- There are some restrictions (ASIC/ACNC):
 - May not be company
 - Cannot be insolvent (undischarged bankrupt)
 - Disqualified from being a Director by law
 - Convicted of an indictable offense involving the operations of a company
 - If they were a former auditor of the company in the previous two years.

Director duties...



- Director duties are defined in the Corporations Act for Companies limited by guarantee (ASIC) and the ACNC Governance Principles for Associations.
- Duties are the same under common law for Companies and Associations.
- Duties are in three areas:
 1. Loyalty and good faith and;
 2. Care and diligence and;
 3. Specific statutory duties
- Remember the separation of duties between Directors and Managers:
 - “Fingers out, nose in”.

Duties of loyalty and good faith



These include:

- To act at all times in the best interests of the company.
 - This can be complex when balancing the short- and long-term pain/gain vs benefit to all stakeholders vs sustainability.
 - Global trend towards environmental, social and governance (ESG) responsibility considers the companies impact on the community and the environment.
 - Duty to the company and not the group of companies.
- Acting for proper purpose.
 - Improper use of position – e.g. entering into an agreement that provides a personal benefit to a Director.
 - Improper use of information – e.g. not use information to gain personal advantage (applies after a Director has left the Board). Keeping confidential information confidential.
 - Phoenix activities – manipulation of ASIC processes etc, to avoid penalties or payments.

Duties of loyalty and good faith



Conflicts of interest

- Material Personal Interest (MPI) – must be determined by unconflicted directors
- Disclosure – notice must be given as soon as practical after the director becomes aware.
- Must be recorded in the minutes
- In companies limited by guarantee, Directors with MPI must not be present in the discussions.
- Should be a Board meeting agenda item at every Board meeting.
- Every organisation should have a 'Conflict of Interest Policy'.

Example: ACME Settlement Inc is an incorporated association with seven directors. Julie is one of the Directors and who has proposed at a Board meeting that ACME should pursue DGR status registration. Julie has previously given ACME a sizable amount of money as a donation.

What should Julie do or have done? Should ACME receive DGR status she will receive a substantial personal tax deduction. Julie, should declare her interest as soon as she was aware i.e. at the time she made the proposal to the Board.

What should the Board do? – it should be discussed by the other Directors (ideally with Julie out of the room) . This should be recorded in the minutes. They must consider the following:

- to decide if there exists a material personal interest. (Yes it is material)
- has Julie complied with the COI policy? (If she declared this at the time then she probably has)
- Is Julie's interest inconsistent with the interests of ACME? (probably not as all donors would also be entitled to a tax deduction)
- Should Julie be allowed to be present and vote on the DGR decision? (depends on the status of other Directors)

Duties of care and diligence



- It is an objective assessment against what a reasonable Director would do.
- It examines decision-making.
- Balances foreseeable risk vs potential benefit that could be reasonably expected.
- Core obligations of Directors are:
 - ✓ Become familiar with the operations of the business.
 - ✓ Stay informed (ask questions) re the activities of the company.
 - ✓ Monitor generally the company's affairs and policies.
 - ✓ Maintain a familiarity with the company's financial position.
 - ✓ This includes reading the financial statements, board papers, asking questions, making own enquiries where appropriate. This demands a level of financial literacy.
 - ✓ Have a reasonable informed opinion of the company's solvency positions and its financial capacity.

This requires directors to critically analyse and employ detailed attention to matters before them and not rely on "others" or simply "follow the crowd"

An important point...

- Boards have the power to act.
- Directors don't have the power to act as individuals.
- Boards act as a group.

However....

Director's duties, responsibilities and liabilities are on the individual.



Specific statutory duties



Statutory duties include:

1. Duty to prevent insolvent trading
 - Applies only to Directors (not managers).
 - Applies when the company is insolvent or there are reasonable grounds for suspecting the company is or would become insolvent.
 - Solvent = Able to pay all of its debts as and when they become due and payable.
 - Protected to some extent by the 'Safe Harbour Provisions' (not applicable to Associations).
2. Duty for continuous disclosure
3. Disclosure of related party transactions

Other regulatory areas include:

WHS, privacy act, environmental law, competition law, FWA, anti-discrimination, modern slavery

The Centro case



- Centro is a large property company listed on the ASX.
- Centro 2007 annual report did not disclose properly the companies short term liabilities (\$1.5B). There was an accounting error. It was also missed by Centro's auditors.
- The Directors defence was:
 1. That the Directors were overloaded by a large Board pack they can't be expected to read all of it.
 2. They aren't accountants and relied on the processes and advisors (auditors).
- The courts saw it differently:
 - That the Directors breached their responsibilities as to Duty and Care by certifying the truth and fairness of the financial statements and annual reports.
 - Directors are entitled to delegate their responsibilities, but Directors are expected to take a diligent and intelligent interest in the information that is available to them, to understand that information and apply an enquiring mind to their responsibilities.
 - Directors must have a basic level of financial literacy and should have noted the "obvious errors".
 - Boards must carefully manage the information flow process from management. In any event it is no excuse for not reading the Board pack.

Directors in NFPs...

- NFP Directors are often not paid or paid only nominal amounts.
- This is in a quite stark comparison to Directors of commercial companies.
- NFP Directors volunteer as they are passionate about the purpose.
- It is important to note that Director duties are equally applicable regardless of the level of payment of any Director fees.



What NFP Directors need to do...

Being a NFP Director should not be scary

NFP Directors serve for purpose and are wonderful people

To be a Director you should:

1. Keep informed – financial and non-financial position, risk and issues.
2. Be inquisitive – must inquire, must ask questions (healthy skepticism).
3. Be aware of their duties and responsibilities. Eyes open.
4. Develop their governance skills.
5. Have the time. It is a serious commitment of time and attention.



Director competencies



Competencies refers to skills, experience and knowledge

Generally, there are two groups of competencies:

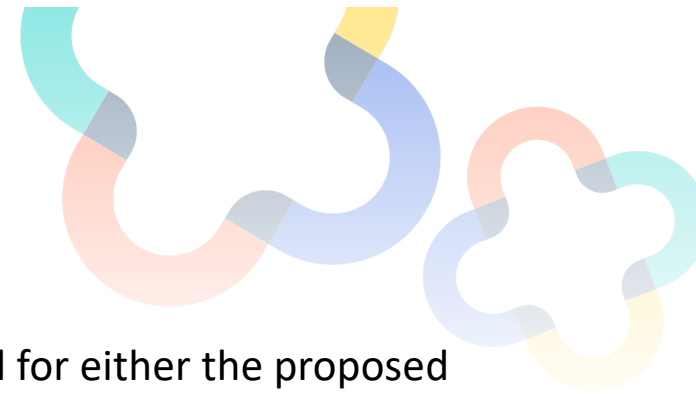
1. Technical – qualifications, education, experience, industry knowledge in :

- strategy, accounting , finance, law, fundraising , settlement, housing, social enterprises, employment, community, corporate governance, clinical governance, human resources, marketing, IT, government policy, etc

2. Behavioural – director personal attributes and behaviours.

- Influence skills, communications, interpersonal, commitment, decision-making, biases, ethical standards, social skills, emotional intelligence, etc

Director recruitment – skills matrix



- Before recruiting Board members, a skills matrix should be developed for either the proposed new board or across the existing directors. (see next slide)
- The skills matrix should be reviewed annually against the purpose and strategy of the organisation.
- As well as skills and behaviours, attention should be given to the following attributes of candidates:
 - ✓ Big picture thinking
 - ✓ Ability to be coherent and develop an argument
 - ✓ Imagination and curiosity
 - ✓ Ability to understand complexity
 - ✓ Being open minded
 - ✓ Self-awareness, listening skills, respect for other people
- Before accepting a directorship, you should complete your own due diligence on the organisation.

Director recruitment – skills matrix

Competency	Director 1	Director 2	Director 3	Director 4	Director 5
<u>Technical</u>					
Accounting	5	1	1	2	3
Finance	5	1	1	2	2
Legal	4	1	1	5	2
Strategy	2	3	1	2	1
Human Resources	1	4	1	3	5
Humanitarian Settlement	1	5	5	1	3
Marketing/PR	1	2	1	1	1
Risk Management	4	3	1	5	2
<u>Industry Experience</u>					
Settlement	3	5	5	1	5
Public Policy	2	3	1	2	4
Government	2	3	1	2	3
<u>Behavioural</u>					
Collaborative	4	5	5	4	5
Listening	4	4	4	4	4
Time and availability	5	5	1	3	4
Ability to challenge	4	2	1	5	2
Interpersonal skills	3	5	5	2	5

Scale
 1 = none
 2 = low
 3 = medium
 4 = good
 5 = high

Note: use a scale rather than a tick or cross

Board composition – (size & makeup)

- Board diversity – diversity of thinking
- Balance vs independence
 - Ratio of Executive and Non-Executive Directors
 - Experience, skills, knowledge vs Independence of mind
 - A Non-executive director does not necessarily mean independence.
 - Current and former employees
 - Tenure
 - Major supplier or competitor
 - Being a secured creditor



Board composition – (size & makeup)



Size

- Large enough to benefit from diversity and small enough to be effective.
- 7 to 9 is the Australian optimum size
- NFP Boards are often larger
- Beware of board size creep.

The next webinar (5th April) ...



What is the role of the board in establishing the tone from the top?

Here we discuss such issue as...

Culture of the Board and the organisation

The mechanics of operating a Board effectively including the role of committees

Future webinars will focus on Director skills:

- | | |
|---------------------------------------|----------------------|
| • Finance for non-financial directors | 10 th May |
| • The legal issues in governance | 25 th May |
| • Strategy & Risk | 7 th June |

Further information...

Australian Institute of Company Directors (AICD)

www.aicd.companydirectors.com.au

Governance Institute of Australia

www.governanceinstitute.com.au

SETSCoP Business Guides Governance Series

<https://setscop.org.au/resource-type/governance-of-not-for-profits/>

Australian Charities and Not-for-profit Commission (ACNC)

www.acnc.gov.au

Your local state government office

- Victoria – Consumer Affairs Victoria
- Queensland – Office of Fair Trading
- New South Wales – NSW Fair Trading
- South Australia – Family and Community
- Tasmania – Consumer Building and Occupational Services
- West Australia – Consumer Protection
- Australian Capital Territory – Access Canberra
- Northern Territory – Licensing NT



Questions?