

**2 July 2018**

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Dear Lucas

## **Good governance principles and guidance for NFP organisations**

Governance Institute of Australia (Governance Institute) is the only independent professional association with a sole focus on whole-of-organisation governance. Our education, support and networking opportunities for directors, company secretaries, governance professionals and risk managers are unrivalled.

Our members have primary responsibility to develop and implement governance frameworks in public listed, unlisted and private companies, as well as not-for-profit organisations (NFPs) and the public sector.

Governance Institute welcomes the opportunity to comment on the Australian Institute of Company Directors (AICD) *Good governance principles and guidance for NFP organisations* (the Principles).

We commend the AICD for developing the Principles, which will assist in improving governance in the not-for-profit sector. We consider that the Principles are consistent with the elements of good governance. The AICD is also to be commended for developing the supporting practices to help organisations interpret and apply the Principles to their unique circumstances.

Governance Institute makes the following general comments in relation to the consultation questions.

### **Question 1 Do you support the approach of providing supporting practices? If not, what alternative do you recommend?**

Governance Institute supports the approach of providing supporting practices.

### **Question 2 What resources would be most valuable in supporting users of the Principles to apply them in their organisations?**

There is a significant volume of publicly available material from organisations such as Governance Institute, ACNC and ATO which would be a valuable resource for not-for-profit organisations. A guide to accessing these resources by including links to the relevant webpages would be useful.

Governance Institute has a range of good governance guides aimed at the not-for-profit sector including a publicly available not-for-profit starter pack which includes guidance on the following topics:

- Board structure
- Conflicts of interest in not-for-profit organisations
- Issues to consider when developing a communications policy
- Issues to consider for a chief executive officer who is also appointed as the company secretary
- Issues to consider when developing a policy for managing related party transactions in NFP organisations
- Risk management policy
- Separation of authority between board and management
- Stewardship
- Volunteer management

The link to this material which is located on Governance Institute's website is:

<https://www.governanceinstitute.com.au/resources/good-governance-guides-free-starter-packs/nfp-starter-pack/>

**Question 3 Do the proposed 10 principles adequately capture the high level principles of good governance in the NFP context?**

**Question 4: Do the proposed supporting practices appropriately capture the features of good governance to each principle? Should any be changed, added or removed?**

Governance Institute agrees with the proposal to restructure the principles and the revision in priority order. In particular we agree with the promotion of 'Purpose and Strategy' to Principle 1.

### **Good Governance Principles and Guidance for Not-for-Profit Organisations**

We have carefully reviewed the current Principles and provide our detailed comments as follows:

#### **Principle 1: Roles and responsibilities**

##### **Clarity concerning the role of the board**

The Commentary refers to the problems that can arise in some NFP's when directors serve in a volunteer capacity and step in to fill operational gaps thereby 'wearing two hats', as a key operational contributor and as a board member. We agree that this is an issue which affects many NFP's, particularly smaller organisations where volunteer board members may be keen to get involved in the day-to-day decision making of the organisation, or, as highlighted in the Commentary, are required to fill operational gaps during periods of crisis or change. In addition, directors with personal connections with donors may often get involved in fundraising activities. As the Commentary points out, this gives rise to governance issues such as the blurring of the differing responsibilities of the board and management. Moreover, staff and management may not appreciate board members 'looking over their shoulder' which can damage trust. It is important for directors to understand that when they are acting in an operational role, they are wearing a very different 'hat' to when they are acting as a director and that during those periods, their accountability is to management. It is tempting for directors of NFP's who step into operational roles to retain their directorial persona and issue directions to staff members in a manner that usurps the role of management. Directors need to be vigilant that they have a clear differentiation between the two roles. We recommend that the Commentary be expanded to deal with this point in more detail and that additional guidance be provided, perhaps by adding an additional 'question for consideration' which deals with accountabilities and behaviours of directors who 'wear two hats'.

##### **Boards should not function like parliaments**

We note that the obligation of directors to act in the best interests of the company, even when they are nominated by a particular stakeholder group, is contained in a footnote at the bottom of page 15. We agree that where individual directors regard themselves as representatives of a particular group, factions and boardroom infighting can arise which reduces the ability of boards to operate effectively. This can also cause directors to breach their legal duties which they owe to the organisation. We recommend elevating the reference to this potential breach of duty to the main text.

## **Principle 2: Board composition**

### **Getting an appropriate mix of skills, knowledge and experience**

Governance Institute is of the view, that in addition to the appropriate mix of skills, knowledge and experience, it may be important for not-for-profit organisations pursuing a cause or mission to have a board containing people with the appropriate mix of stakeholder perspectives and experiences. By way of example, an organisation which has as its purpose the provision of services to children with autism may benefit from having people who deal with autistic children on a day to day basis or parents of autistic children to whom these services are provided, on its board. These people can provide a valuable perspective to the board on the needs which the organisation is striving to meet. We recommend that a reference to stakeholder perspectives and experiences be included in this section. In the context of the previous paragraph, this is quite different to having directors who are appointed to represent those stakeholder groups.

### **The size of the board**

We refer to the suggestion in the Commentary that it may be sensible for a small not-for-profit organisation to begin with a relatively small board of say four or five directors. There are risks that a board of such size is too small to have the capabilities and perspectives needed around the board table to make effective decisions. It may be preferable for such a small board to act on an interim basis until additional members can be recruited.

### **Terms of board appointment**

Some not-for-profit organisations will have their board terms prescribed by legislation. We recommend that a reference be included in the Commentary to that effect to serve as a reminder to relevant organisations to check their founding statute.

## **Principle 3: Purpose and strategy**

We agree that it is critical for an organisation to define clearly why it exists, what it does etc,. The constitution of a not-for-profit organisation (and the objects in it) does much more than set out things a board must do and take into account when it is considering these questions. The objects in the constitution are the reason why the organisation exists. We suggest that the Commentary be amended to emphasise the importance of the objects clause of the not-for-profit organisation's constitution.

An exploration of the management of strategic risk in a not-for-profit organisation would be valuable in this section. Not-for-profit organisations are particularly susceptible to 'mission creep,' where they operate in areas outside of their purpose or objects. This may occur because a need arises which the organisation wants to address. Currently, not-for-profit organisations are increasingly engaged by Government to provide social services to the public. This can result in organisations entering into government contracts which generate valuable income, but which lead the organisation into areas outside of their area of skill or expertise or that they are not best placed to service.

## **Financial performance indicators**

We consider that care needs to be taken when selecting measures for the performance of not-for-profit organisations. By way of example, when selecting an efficiency measure, reducing the cost of meals produced in a nursing home may make the service more profitable but may also reduce the nutritional content and be counter-productive. We refer you to the index researched by Professor Mark Lyons (and Alan Bridges) of UTS as a method of measuring the sustainability of a not-for-profit organisation discussed in the paper *Factors associated with fundraising dependency among non-profit organisations in Australia*, Gianni Zappala and Mark Lyons, Australian Journal of Social Issues Volume 41, No 4 Summer 2006, which you may find of interest.

## **Principle 6: Board effectiveness**

### **Board meetings**

It can be good practice to include an in-camera session of non-executive directors as a matter of governance hygiene and as a safety valve to ensure that non-executive directors have an opportunity to raise appropriate queries or concerns.

### **Factors that contribute to poor meetings**

We consider that an additional factor that contributes to poor meetings in not-for-profit organisations that can be included in the list is the practice of board members working through the detail of reports rather than by assuming that reports have been read and asking relevant questions. A way to improve the running of a board meeting to enable boards to add value is to provide for reports to be taken as read.

### **Some questions for consideration**

We agree that one of the factors that contributes to poor meetings includes conflict of interest issues not being dealt with appropriately. This is an issue with which small not-for-profit organisations typically struggle. We recommend including in this section a question on how conflicts of interest are being handled, to focus the minds of board members on this important issue.

## **Principle 8: Organisation building**

### **Use of volunteers**

We consider it good governance for boards of not-for-profit organisations to develop an appropriate set of policies governing volunteer management. We recommend the addition of a reference to effective board oversight of volunteers in this section.

## **Principle 9: Culture and ethics**

### **Board culture**

Due to the importance of a board dealing appropriately with conflicts of interest, we recommend including a reference to the legal obligations contained in the Corporations Act concerning conflicts of interest and related party transactions in this section which will be of relevance to not-for-profit organisations which are companies limited by guarantee.

Yours sincerely

A handwritten signature in black ink, appearing to read "Burrell", with a horizontal line extending from the end of the signature.

Steven Burrell  
Chief Executive