

## **Submission in response to Treasury**

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## **Development of Governance Standards Consultation Paper**

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### **BOARD MATTERS PTY LTD**

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## 1. Executive Summary

- 1.1 This submission is made on behalf of Board Matters Pty Ltd and associated legal practice, Board Matters Legal. Board Matters is a specialist corporate governance consulting practice established in 2002 in Queensland and now, 11 years later, with clients around Australia. We have consulted to hundreds of not-for-profit organisations including in the religious, educational, health and other charitable arenas as well as industry organisations, member mutuals and other not-for-profit entities without charitable status. More information about our relevant experience and services can be found at our website at [www.boardmatters.com.au](http://www.boardmatters.com.au).
- 1.2 In making this submission we also draw upon Board Matters' extensive experience consulting to for-profit boards and organisations, including public companies and family-owned and other private businesses as well as public sector entities and organisations.
- 1.3 Our consultants also have a vast array of personal experiences sitting on the boards of a range of not-for-profit organisations. Accordingly, our experience is extensive and directly relevant to this submission.
- 1.4 To our mind, the stated purpose and the principles-based approach put forward in the Consultation Paper is generally correct and achievable, the draft governance standards are materially inadequate to achieve the stated purpose. That purpose is set out in section 2.1 of the Consultation Paper as follows:

*The governance standards are intended to reflect a minimum set of outcomes for registered charities, rather than mandate 'best practice governance' or detailed procedures and requirements necessary for effective not-for-profit (NFP) governance. The purpose of these standards is to ensure all stakeholders can be confident that a minimum standard of governance is being met across all charities, whilst providing entities with sufficient flexibility to determine how they go about managing the charity and how to advance the charity's purposes and achieve its objectives. These stakeholders include the broader Australian community, those who benefit from the important services provided by NFPs and those who work or volunteer for a charity.<sup>1</sup>*

- 1.5 In summary it is our submission that the standards in the present form require a number of material enhancements if they are to achieve the above purpose. In brief our reasons for this conclusion are as follows and are explained in more detail in the following pages and sections of this submission:
- (a) There is insufficient detail in any of the standards to enable a registered charity to understand what is intended or required to meet the standard;
  - (b) In many respects the standards would encourage a reversion to the undeveloped governance and in some cases even poor governance practices of the era prior to the *National Safety*

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<sup>1</sup>Section 2.1, paragraph 3 (p6) Consultation Paper

*Council of Australia (Victoria) case*<sup>2</sup> in so far as they would, in our opinion, promote reduced requirements for accountability to members and the broader community;

- (c) In consultations with our clients and interested organisations in preparation for this submission, we have heard expressions such as 'patronising' and 'dumbed down' used to describe the manner in which the standards seemingly encourage far less governance accountability than most reputable charities (by which we do not mean 'large' charities) today think to be acceptable to their own stakeholders and the community at large;
  - (d) Whilst purporting to be "governance" standards, there are many important instances throughout the draft standards in which the critical and separate roles of board (namely governance) and management (namely managing) are dangerously and interchangeably used<sup>3</sup>, with the effect that they do not set a positive standard for the governance role of the board to act as the high level oversight body keeping management accountable, which is a function of all incorporated bodies, large or small, that have any employees whatsoever;
  - (e) Many parts of the standards draw upon but modify slightly the provisions of the *Corporations Act 2001* leading to confusion and the prospect of endless legal debate as to how to interpret the instances of departure;
  - (f) There is in some instances an inappropriate level of power given to the ACNC as regulator, e.g. to unilaterally disqualify persons from acting as directors responsible entities of NFPs<sup>4</sup> and, moreover, to determine a breach of the law where no legal proceedings have been instituted<sup>5</sup>; and
  - (g) Many governance practices which have been successfully encouraged in other sectors, through a range of other governance codes and standards (e.g. the *ASX Corporate Governance Principles and Recommendations*<sup>6</sup>), have been overlooked as well tried and accepted framework for a principles-based governance approach, and they would deliver genuine accountability and public confidence.
- 1.6 In short, it is our submission that the document does not in fact contain what can be properly classified as "governance standards" but instead states a range of unrelated concepts, ideas, duties and only in some instances "standards".
- 1.7 We do, however, in this submission propose a range of alternative "standards" with, we submit, more useful detailed "principles" given to

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<sup>2</sup> *Commonwealth Bank of Australia v Friedrich* (1991) 9 ACLC 946

<sup>3</sup> See especially draft standard 4 which purportedly sets as a governance standard that the "registered entity must take reasonable steps to **manage** its financial affairs in a responsible manner" giving no recognition whatsoever to the separate, distinct and critical difference between financial governance and financial management.

<sup>4</sup> See draft standard 5

<sup>5</sup> See draft standard 2

<sup>6</sup> The Australian Securities Exchange Governance Council's *Corporate Governance Principles and Recommendations* 2012

guide the application of each "standard", clearly articulating what is expected under each of the current "standards". We do not support the notion espoused by Treasury and ACNC speakers at the Brisbane "roadshow" on Tuesday 5 February 2013 that this could be done by including more details in guidance notes. If there are clear "outcomes" and "principles" to be applied, they ought be stated in the standards as contemplated by section 45-10(2) of the Act and not left to mere guidance notes.

- 1.8 In section 4 of this submission we have also addressed in more detail a range of other matters including:
- (a) Various matters that are not addressed at all by the draft "standards" which we submit ought to be addressed in order to achieve the stated purpose;
  - (b) The confusion being caused by the use of the expression "responsible entities" to mean persons who sit on the governing body of the organisation when "registered entities" is the expression used for charities (and NFP organisations), confusing the responsibilities of the organisation with the responsibilities of its governors; and
  - (c) The need to include in the standards an expression such as "governing body" or "board" as distinct from the individual "responsible entities" in order to make clear that the board or other governing body, as it is constituted from time to time, has responsibility for the governance of the organisation without the need for each and every "responsible entity" to separately approve every action of the organisation.

## 2. Terms used in this paper

- 2.1 The terms used in this paper have the same meaning as the terms used in the Consultation Paper as defined in section 1 of the Consultation Paper.

**Consultation Paper** means the consultation paper dated December 2012 titled 'Development of governance standards' issued by The Treasury on behalf of the Australian Government.

**governing body** means the board, management committee or equivalent governing body, by whatever name it is known, of a registered entity.

**submission** means this Board Matters submission provided in response to the Consultation Paper.

### 3. Possible Governance Standards

#### **Draft Governance Standard 1**

3.1 With reference to draft standard 1 (Purposes and NFP nature of a registered entity) and the questions set out at the end of section 3.1.1 of the Consultation Paper, our answers to those questions are as follows:

(a) *Does the draft standard one establish the appropriate principles?*

Yes although we believe that it leaves much room for debate as to what is meant by the concept of a charity being able to demonstrate "its purposes and its character as a not-for-profit entity" when there is no guidance in the Act or the draft standards to clarify what will be expected in order to demonstrate the 'character' of a 'not-for-profit entity'

(b) *Is the wording of draft governance standard one appropriate?*

Yes, subject to the comment above

3.2 In relation to draft governance standard 2 (accountability to members), and the 2 questions set out at the end of section 3.2 of the Consultation Paper, our answers are as follows:

(a) *Does the draft standard two establish the appropriate principles?*  
No, for the reasons set out in paragraph 3.3.

(b) *Is the wording of draft governance standard two appropriate?*  
No, for the reasons set out in paragraph 3.3.

#### **Draft Governance Standard 2**

3.3 Addressing our responses to the above 2 questions more specifically, our concerns with draft governance standard 3 are as follows:

(a) Whilst the stated object in relation to draft standard 2 is commendable, draft governance standard 2 is inadequate to achieve the stated object, as it gives no certainty to registered charities and their directors (responsible entities) in terms of what it means to "ensure the accountability and transparency of a registered entity";

(b) The responsibility of directors of companies has long been accepted in Australia as extending beyond the purely legal primary accountability to 'members' such that, in order to discharge that primary accountability properly, directors must understand and accept a range of other accountabilities to a broader range of stakeholders, particularly given the importance of donors, volunteers, clients, not to mention the Australian public as funders through the Australian taxation and transfer system;

(c) "Accountability" is a concept which can be interpreted in a vast range of ways, and for this standard to have real meaning demands greater clarity through inclusion of more useful principles, rather than merely providing a glancing reference to already widely accepted and very basic practices (which may well be outdated before long) in the form of annual general meetings and annual reports;

- (d) Whilst the word “transparency” appears in the object clause, nothing is provided to explain what is meant and expected by “transparency” as distinct from “accountability” which we would suggest are equally important, but quite different, concepts; and
- (e) The explicit provision in standard 2(b) that a “registered entity’s members have an adequate opportunity to raise concerns” leaves silent the responsibility of the registered entity or its responsible entities to address or answer those concerns in any manner, which we would have expected should be the explicit accountability if such a right for members is made explicit.

3.4 Our recommended solution to the above is to revise draft governance standard 2 with the following marked up changes:

Draft governance standard 2: Accountability to ~~stakeholders~~ members

45.10 Standard 2—accountability to ~~members~~ stakeholders

Object

- 1) The object of this governance standard is to ensure the accountability and transparency of a registered entity to its members and, as appropriate, to other stakeholders.

Standard

- 2) The governing body of a ~~A~~ registered entity that has members must ensure that the registered entity remains accountable to its key stakeholders and is transparent as appropriate in all dealings with key stakeholders.

Principles

In order to achieve this standard:

~~take reasonable steps to ensure that:~~

- (a) The governing body of the registered entity must account directly to its members at least annually for the governance of the registered entity and the general allocation and use of its resources;
- (b) The governing body must ensure that the registered entity accounts to other key stakeholders of the registered entity as appropriate, relative to their respective interests in the organisation, for the governance of the registered entity and the general allocation and use of relevant resources; and
- (c) The registered entity’s members and other key stakeholders must have, relative to their interest in the organisation, adequate means and opportunity to communicate with the governing body of the registered entity to raise concerns or questions about the governance of the registered entity and the general allocation and use of its resources.
- ~~a) the registered entity is accountable to its members; and~~
- ~~b) the registered entity’s members have an adequate opportunity to raise concerns about the governance of the~~

~~registered entity.~~

Note 1 The steps that a registered entity may take to ensure it is accountable to its members could include holding annual general meetings, providing members with an annual report (including financial information and achievements towards its purpose) and providing for elections for its responsible entities.

### **Draft Governance Standard 3**

- 3.5 Having regard to draft governance standard 3 (compliance with Australian laws), and the questions set out at the end section 3.3 of the Consultation Paper, our answers are as follows:
- (a) *Does draft governance standard three establish the appropriate principles?*  
No, for the reasons set out in paragraph 3.6.
  - (b) *Is the wording of draft governance standard three appropriate?*  
No, for the reasons set out in paragraph 3.6.
- 3.6 Addressing our responses to the above 2 questions more specifically, our concerns with draft governance standard 3 are as follows:
- (a) We respectfully submit that it is unnecessary, and something of a legal absurdity, to impose a standard which requires compliance with Australian law when Australian law in and of itself requires compliance as the base minimum standard for charities, NFP organisations and, for that matter, citizens and organisations throughout Australia;
  - (b) If the intent is to extend the application of Australian laws to the activities of charities outside Australia, as some have suggested is one of the real aims of this standard, then this ought properly and explicitly be addressed by the Parliament of Australia and not via the back door through purported establishment of governance standards by regulation;
  - (c) In view of the real and stated intent of this standard being to give the Commissioner the ability to deal with infringements and perceived infringements as relevant to the continuing registered status of the charity<sup>7</sup>, it is submitted that it is also inappropriate that this matter be addressed via the back door through purported establishment of governance standards by regulation; and
  - (d) It is, we respectfully submit, offensive to the Australian legal and governance system, and in particular the bedrock notion of separation of powers, to give the regulator the power to impose any type of action or sanction when the Commissioner merely “reasonably believes” that a charity has engaged in some illegal or offensive behaviour<sup>8</sup> arguably seeking to circumvent the roles and powers of courts of law in Australia.

<sup>7</sup> See paragraph 2 in section 3.3 on page 14 of the Consultation Paper

<sup>8</sup> See the final paragraph on page 15 in section 3.3 of the Consultation Paper

- 3.7 However conversely we also note that curiously there is nothing in the governance standards to address the real and valid contemporary governance expectation that charities and NFP organisations large and small ought to be able to demonstrate that they have processes and systems (which do not need to be expensive software-based systems) that aid in striving to ensure compliance with laws. This is contrasted with the *ASX Corporate Governance Principles and Recommendations* whereby the board of a company is responsible for the risk management (and therefore legal compliance) framework of the organisation.
- 3.8 Our recommended solution to the above is to revise draft governance standard 3 with the following marked up changes:

Draft governance standard 3: Compliance with Australian laws

45.15 Standard 3—compliance with Australian laws

Object

- 1) The object of this governance standard is to give the public (including members, donors, employees, volunteers and benefit recipients of a registered entity) trust and confidence that a registered entity is governed in a way that ensures its on-going operations and the safety of its assets, through compliance with Australian laws (including preventing the misuse of its assets).

Standard

- 2) A registered entity must actively strive to ensure that the registered entity and its officers and employees comply with applicable Australian laws.

Principles

In order to achieve this standard, the governing body of the registered entity must:

- (a) ensure that the registered entity adopts and maintains demonstrable legal compliance processes that are appropriate relative to the assets and resources of the registered entity; and
- (b) in cases where the implementation of legal compliance processes is delegated by the governing body to employees of the registered entity, monitor and supervise the implementation of the legal compliance processes, to the registered entity and its officers and employees with Australian Laws.

A registered entity must not engage in conduct, or omit to engage in conduct, that may be dealt with:

- a) as an indictable offence under an Australian law (even if it may, in some circumstances, be dealt with as a summary offence); or
- b) by way of a civil penalty of 60 penalty units or more.

Note 1 See section 4AA of the Crimes Act 1914 for the current value of a penalty unit.

Note 2 While a registered entity must comply with all Australian laws, a serious infringement of an Australian law covered by this standard may allow the

~~Commissioner to exercise his or her enforcement powers under Part 4-2 of the Act, following consideration of the matters mentioned in subsection 35-10 (2) of the Act.~~

#### **Draft Governance Standard 4**

3.9 Having reference to draft governance standard 4 (responsible management of financial affairs), and the questions set out at section 3.4 of the Consultation Paper, our answers are as follows:

- (a) *Does draft standard four establish the appropriate principles?*  
No, for the reasons set out in paragraph 3.10 below.
- (b) *Is the wording of draft governance standard four appropriate?*  
No, for the reasons set out in paragraph 3.10 below.

3.10 To explain our objections to draft governance standard in more detail:

- (a) We respectfully submit that this standard is completely inadequate to give guidance to the governing bodies of charities and NFP organisations as to what is expected in relation to this most critical matter of the expectations of the financial governance of an NFP organisation, where by contrast the existing state of the law is extremely clear, well-developed and well understood; and
- (b) The text currently set out under this draft governance standard (at page 17 of the Consultation Paper) indeed could give some users the misguided and mischievous impression that, for instance, it may be sufficient to manage the financial affairs of an organisation solely "by having appropriate insurance". In our consultations with clients and other interested organisations in the preparation of this Submission, we found a very strong negative response to this statement in the Consultation Paper given the extreme danger inherent in such a suggestion.

3.11 We do not advocate for the other extreme of the overly prescriptive details down to 'cheque-signing' authorities and delegations<sup>9</sup> set out in the respective *Associations Incorporation Acts* in some of the States and Territories in Australia. However, we do advocate strongly for giving greater clarity in relation to this important aspect of the governance of charities and NFP organisations.

3.12 Our recommended solution to the above is to revise draft governance standard 4 with the following marked up changes:

Draft governance standard 4: Responsible management of financial affairs

45.20 Standard 4—responsible management of financial affairs

Object

1) The object of this governance standard is to ensure that a

<sup>9</sup> See s.7 *Associations Incorporation Regulation 1999* (Qld)

registered entity governs and manages its resources responsibly, in a way that effectively furthers its purposes and protects its resources from misuse.

#### Standard

(2) The governing body of the registered entity must actively monitor and supervise the management of the financial affairs of the registered entity to ensure that the above stated object is achieved.

#### Principles

In order to achieve this standard, the governing body must:

- (a) ensure that, in cases where management of financial affairs is delegated to any employee/s there is a clear and explicit statement by the governing body of the registered entity making clear the manner in which financial governance and management authorities and delegations are allocated;
- (b) ensure that all delegations of financial management authorities are appropriate relative to the size and nature of the registered entity;
- (c) put in place financial governance processes and arrangements that are appropriate, relative to the size and nature of the registered entity, to ensure that the governing body retains an active role in monitoring and supervising the financial management of the registered entity; and
- (d) ensure that the registered entity keeps reasonable written financial records which enable the registered entity to meet its responsibilities under Standard 2 (accountability to stakeholders) in respect of the general use and allocation of resources of the registered entity.

A registered entity must take reasonable steps to manage its financial affairs in a responsible manner.

**Draft Governance Standard 5**

- 3.13 Having regard to draft governance standard 5 (suitability of responsible entities) and the questions set out at the end of section 3.5.2 of the Consultation Paper our answers are as follows:
- (a) *Does draft standard five establish the appropriate principles?*  
No, for the reasons set out in paragraph 3.15 below.
  - (b) *Is the wording of draft governance standard five appropriate?*  
No, for the reasons set out in paragraph 3.15 below.
- 3.14 Also addressing the questions set out at section 3.5.3 of the Consultation Paper our answer is as follows:
- (c) *Are there concerns with allowing the ACNC to disqualify responsible entities and maintain a disqualified responsible entities register?*  
Yes, for the reasons set out in paragraph 3.15 below.
- 3.15 We support the introduction of a standard which encourages concepts of "suitability" expectations for responsible entities, provided it does not become a costly administrative burden which many such regimes have proven over time to be. However, this draft governance standard is so negatively framed that we fail to see how it helps to encourage true governance suitability of responsible entities. To explain our objections to draft governance standard 5 in more detail:
- (a) Instead of setting a standard which would support and foster good governance attributes amongst the governors of charities, this draft standard merely states the existing 'lowest common denominator' test under the *Corporations Act 2001*, namely that a disqualified person cannot be a director (or in this case 'responsible entity');
  - (b) In order to frame the standard in such a way as to aid in the attainment of the stated object, we submit that it ought instead to involve concepts akin to, although not as administratively prescriptive as, the 'Fit and Proper' regime applicable to regulated financial services entities under the *Corporations Act 2001*;
  - (c) Governance standards are not the appropriate instrument through which to confer powers on the ACNC to disqualify responsible entities and to maintain a disqualified responsible entities register (which we note is already and more appropriately dealt with in the Act itself<sup>10</sup>); and
  - (d) The ACNC and ASIC both maintain similar registers is likely to lead to significant confusion for the public and for registered entities seeking to ensure compliance with these provisions (particularly given that the ACNC is stated only to be able to suspend or remove responsible entities where the registered charity is a federally regulated entity<sup>11</sup>).

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<sup>10</sup> See Division 100 of the Act

<sup>11</sup> See page 21 in section 3.5.3 of the Consultation paper

- 3.16 Our recommended solution to the above is to revise draft governance standard 5 with the following marked up changes:

Draft governance standard 5: Suitability of responsible entities

45.25 Standard 5—suitability of responsible entities

Object

- 1) The object of this governance standard is to maintain, protect and enhance public trust and confidence in the governance and operation of a registered entity.

Standard

- 2) The governing body of the registered entity must actively strive for the continuous development of the governance capacity of the governing body, and of its individual responsible entities, to optimise the governance of the registered entity.

Principles

In order to achieve this standard, the governing body must:

A registered entity must:

- (a) adopt and maintain transparent and rigorous processes that encourage and support the nomination and selection of persons with appropriate skills, experience, backgrounds and other competencies for election or appointment to the governing body (i.e. as responsible entities);
- (b) actively strive to support the relevant professional development of the members of the governing body (i.e. the responsible entities);
- (c) take reasonable steps, prior to the election or appointment of any person to the governing body, to satisfy itself, to the extent reasonably practicable, that the responsible entity meets the following conditions, namely that it is not:
  - (i) disqualified from managing a corporation, within the meaning of the Corporations Act 2001; or
  - (ii) disqualified by the Commissioner, at any time during the preceding 12 months, from being a responsible entity of a registered entity under subsection (4);
- (d) take reasonable steps to monitor the extent to which its responsible entities continue to fulfil the requirements of the preceding paragraph (c); and ~~ies~~ after taking those steps:
  - ~~i) be, and remain, satisfied that each responsible entity meets the conditions; or~~
- (e) ~~ii)~~ if it is unable to be, or remain, satisfied that a responsible entity meets the conditions, take reasonable steps to remove that responsible entity.

Note Other Australian laws may require responsible entities to be replaced, if removed, because a registered entity may need to have a minimum number of responsible entities.

### **Examples of reasonable steps**

Reasonable steps may include obtaining declarations from responsible entities and the searching of public registers.

3) Subject to subsection (5), the conditions for each responsible entity are that it is not:

a) disqualified from managing a corporation, within the meaning of the Corporations Act 2001; or

b) disqualified by the Commissioner, at any time during the preceding 12 months, from being a responsible entity of a registered entity under subsection (4).

4) The Commissioner may disqualify an entity from being eligible to be a responsible entity for the purpose of this standard if:

a) the entity has been previously suspended or removed as a responsible entity of any registered entity, under Division 100 of the Act; and

b) the entity has been given notice of its disqualification by the Commissioner; and

c) the Commissioner reasonably believes that the disqualification is justified having regard to the objects of the Act.

5) Despite subsection (3), the Commissioner may allow an individual to be a responsible entity for a particular registered entity if the Commissioner believes it is reasonable to do so in the circumstances.

6) An entity that is dissatisfied with a decision of the Commissioner to disqualify the entity under subsection (4) may object to the decision in the manner set out in Part 7-2 of the Act.

### Subdivision 45-D Register

#### 45.150 Register of disqualified responsible entities

1) The Commissioner must maintain a register, to be known as the Disqualified Responsible Entities Register, in which the Commissioner must include the following information:

a) the name of the entity disqualified by the Commissioner from being a responsible entity of a registered entity, under subsection 45.25 (4);

b) the date that the entity was disqualified by the Commissioner;

c) whether the disqualification remains subject to review, under Part 7-2 of the Act.

2) The Register must be maintained by electronic means.

3) The Register must be made available for public inspection, on

a website maintained by the Commissioner.

### **Draft Governance Standard 6**

- 3.17 Having regard to draft governance standard 6 (duties of responsible entities), and the questions set out at the end of section 3.6.2 of the Consultation Paper, our answers are as follows:
- (a) *Does draft standard six establish the appropriate principles?*  
No, for the reasons set out in paragraph 3.19 below.
  - (b) *Is the wording of draft governance standard six and the draft protections appropriate?*  
No, for the reasons set out in paragraph 3.19 below.
- 3.18 Also addressing the questions at the end of section 3.6.3 of the Consultation Paper our answers are as follows:
- (a) *Are there any additional protections which should only be provided to volunteer responsible entities.*  
No, for the reasons set out in paragraph 3.19 below.
  - (b) *If so, what would these protections be?*  
Not applicable.
- 3.19 Specifically addressing our concerns with draft governance standard 6:
- (a) It is objectionable to include fiduciary duties of directors in a governance standard when the point of "governance standards" ought to be to deal more broadly with the responsibilities of those who govern the organisation in order to attain the required standard rather than simply defaulting to the legal duties which were previously applicable under ss180-183 of the *Corporations Act 2001* and which, in respect of those registered entities formed under the *Corporations Act*, are now 'turned off' by virtue of the Act;
  - (b) Moreover, inherent in the assertion that the object of the standard is to require responsible entities to act in the manner that would be necessary if "the relationship between them and the entity were a fiduciary relationship" is the suggestion that those responsible entities who are directors of companies and members of management committees of associations may no longer to be regarded as being in a fiduciary relationship which the general law recognises that they are and which, we submit with all due respect, is solely within the power of the courts of law (or Parliament) in Australia, and not a regulator, to determine;
  - (c) As this standard adopts but modifies slightly the language of the previously applicable (and now 'turned off') duties contained in ss180-183 of the *Corporations Act 2001* it leaves open for endless, costly and unproductive legal debate the question as to the way in which courts of law ought to interpret those provisions;

- (d) The provisions relating to “material conflicts of interest” contain technical errors in so far as they confuse general law fiduciary duty to ‘avoid conflicts of interest and interest and conflicts of interest and duty’ with the ‘material personal interest’ provisions of the *Corporations Act 2001*, which will only exacerbate the already extensive confusion in relation to the management of conflicts of interest within organisations;
  - (e) It is curious to expect directors to disclose “perceived” conflicts of interest when the nature of perceived conflicts of interest is such that it is a matter of the perception of a third party, not that of the director in question, and hence we suspect that the reference ought to be “potential” conflicts of interest;
  - (f) The requirement to disclose a “related party transaction” under note 3 to standard 2 of draft governance standard 6 will require a detailed technical understanding of the related party transaction of the *Corporations Act 2001* (apparently making this additional obligation apply to charities that have not previously been subject to the *Corporations Act 2001*) which further obfuscates the issue of the management of conflicts of interest; and
  - (g) The requirement that “a registered entity must take reasonable steps to ensure that its responsible entities are subject to” the stated duties begs the question whether this is an obligation of the ‘registered entity’ acting through the mechanism of a general meeting of members (which would be unworkable) or whether it is in fact the responsibility of the governing body (which we suggest it ought to be).
- 3.20 We submit that draft governance standard 6 is entirely inappropriate as a “standard” and ought to be deleted in its entirety. It ought instead to be subject to much deeper and broader consultation and engagement within the sector to identify the true principles at the heart of the present draft standard 6, leaving legal duties to the general law of fiduciaries to be determined appropriately by the courts. After all, in any case, the general law will continue to apply the fiduciary duties to the directors and governors of most ‘registered entities’ irrespective of what is contained in this standard, so little is lost by deleting it from the standard and taking time to develop the standards appropriately and much is gained by removing the scope for endless legal challenge and debate.
- 3.21 In relation to the question about the additional protections for volunteer responsible entities, we strenuously oppose any such additional protection.
- 3.22 The state of the law prior to the *Commonwealth Bank of Australia v Friedrich (1991) 9 ACLC 946* was uncertain in this regard. Since that legal decision there has been over 20 years of concerted action within the sector to raise the level of understanding amongst directors of charities about the critical responsibilities that come with the role of director. This is now widely understood by directors within the sector to be an extremely high level of responsibility and accountability for the governance and stewardship of assets and resources that do not belong to the directors.

- 3.23 If a person is not suitable to discharge the duties of a director or governor, they ought not to be given the position of responsibility irrespective of whether they are paid for the role or not. We believe that any further protections for volunteer directors would fly in the face of the Act and the standards, since it would seriously and immediately diminish public confidence in the sector in spite of the efforts of the many volunteer directors who have worked so hard for over 2 decades to 'raise the bar', and thus public confidence, in this respect.

#### 4. Other matters

- 4.1 We also take this opportunity to strenuously object to the use of the terminology 'responsible entity' which is used in the draft governance standards. Whilst we appreciate that the draft governance standards simply mirror the Act in this regard, we request that this point be addressed as urgently as possible by the ACNC, since it is already causing manifest confusion in the broader NFP community when discussing the Act and the draft governance standards.
- 4.2 We submit that the language ought to be consistent with now long-used and understood terminology such as "directors", "governors" or even by referring to these people as "responsible persons" and defining that term to include the limited cases of a corporate trustee (which is, we understand, to be the reason for the use of the word "entity").
- 4.3 In seeking to explain these provisions to our clients, we have already encountered significant confusion about the "registered entity" (legal entity) as distinct from the "responsible entities" (people governing the legal entity). It is also curious to use the expression "responsible entity" when the same expression is used in the *Corporations Act* to refer to the company generally responsible for a managed investment scheme (see s9 *Corporations Act*). If one of the purposes of the regime is to simplify the governance of charities, it is submitted that this very simple matter is significantly hindering that purpose.
- 4.4 The draft governance standards set out in the Consultation Paper also fail to recognise one of the central and essential truisms of the corporate form at law, namely that directors are individually accountable (and can be individually liable) for their actions but only ever act as a collective. In their collective mode they are referred to as the 'board', 'council', 'management committee' or other such title. The 'governing body' as we refer to them here has the decision-making authority and responsibility for the 'registered entity'.
- 4.5 We submit that by failing to distinguish between the 'registered entity' as a whole, the 'governing body' (by whatever title it is known) and the individual directors (responsible entities) the standards create extreme confusion and ambiguity about who or what body precisely is responsible for achievement of the standards.
- 4.6 For instance consider draft standard 4 which presently states that:

*A registered entity must take reasonable steps to manage its financial affairs in a responsible manner.*

By stating that the "registered entity" has this responsibility, the standard begs the question whether this is an obligation of the registered entity acting through the mechanism of a general meeting of

members (which would be unworkable) or whether it is in fact the responsibility of the governing body (which we suggest it ought to be). If part of the purpose of these standards is to help to increase the sense of accountability within the sector, it is critical to ensure that there is abundant clarity about such responsibilities.

- 4.7 Moreover, in this standard and various others, by referring only to the task of 'managing' (as distinct from the separate role of 'governing') the financial affairs of the organisation, the standard fails to be a governance standard at all.
- 4.8 We submit that the confusion in this respect can be avoided simply by using an expression such as 'governing body' or board to refer to the collective group of responsible entities in any registered entity, and spelling out when the standards require action by the registered entity itself, the individual responsible entities or the governing body as the collective of the responsible entities. We have endeavoured to take this approach throughout this Submission when proposing amendments to the draft governance standards.
- 4.9 We also submit that, in general, the draft governance standards do not truly represent "standards", but represent a range of concepts, duties and in some cases only, standards. We strongly support the development of a much more detailed set of standards along the lines of the *ASX Corporate Governance Principles and Recommendations* which give real clarity, but are principle-based, around the types of matters that are required for the better governance of listed public companies. We have endeavoured to take this type of approach throughout this Submission.
- 4.10 The standards as presently drafted will provide extensive opportunities for consultancies like our own to help the sector understand and adjust to them when they are already governed, in many cases, extremely well and to a high standard. Whilst this is obviously desirable from the commercial point of view of consultants, it is not desirable from the point of view of charities that have already worked extremely hard to develop governance and other arrangements to a high level and will now be left wondering about the application of their present practices under these standards. It is our submission that by promulgating a set of standards that is more akin to the recommendations and principles under the ASX guidelines, containing much more useful guidance through explicit principles to support each standard, such a problem would be alleviated.

**Dated: 14 February 2013**



Elizabeth Jameson  
Managing Director