



THE LAW SOCIETY
OF NEW SOUTH WALES

Our ref: BLC:DH1b1549764

25 June 2018

Mr Lucas Ryan GAICD
Australian Institute of Company Directors
Level 30, 20 Bond Street
SYDNEY NSW 2000

By email: nfp@aicd.com.au

Dear Mr Ryan,

Review of the 'Good governance principles and guidance for not-for-profit organisations' ("Principles and Guidance")

The Law Society of NSW appreciates the opportunity to comment on the review of the Principles and Guidance. The Law Society's Business Law Committee has contributed to this submission.

The Law Society applauds the Australian Institute of Company Director's commitment to supporting not-for-profit ("NFP") organisations to achieve better outcomes through good governance.

Background

The original document

The Principles and Guidance was first published in 2013 and introduced ten principles and illustrated these with commentary and questions to provide

A practical, sector driven, non-prescriptive framework that can assist NFP organisations (including, but not limited to, charities) to understand what constitutes good governance practice to adapt as appropriate and apply having regard to their particular circumstances - purpose, structure, size and available resources.¹

It was acknowledged that recognition of the not-for-profit ("NFP") sector's diversity was crucial to the document's success. NFP organisations range from large national organisations with experienced boards, professional management and paid staff through to small community groups, which have very limited resources and rely on committed volunteers. The larger and more sophisticated organisations are more likely to have adopted comprehensive governance practices and processes similar to those used by companies listed on the Australian Securities Exchange ("ASX").²

¹ Australia Institute of Company Directors, *Review: 'Good governance principles and guidance for NFP organisations'*, 6.

² For example, the ASX Corporate Governance Council's *Fourth Edition of Corporate Governance Principles and Recommendations*, which is also currently being reviewed.

Small community organisations, by way of contrast, may not have anyone on the board with corporate experience or exposure to sophisticated governance practices. In this context, the Principles and Guidance is designed to promote and facilitate conversations that enable organisations to implement processes to achieve good governance practices:

The objective is to share with the NFP community some key principles that we believe are a useful starting point for NFP boards when considering what constitutes good governance practice (with regard to their particular circumstances).³

What has changed

This review arises from the high level changes since 2013 in the legal, political, operational and social environment that have affected the NFP sector as a whole. Some of those changes are briefly summarised in the consultation paper.⁴

Most significantly in relation to governance, the NFP sector has undergone substantial regulatory reform since 2013. This reform has been at both the federal⁵ and the state and territory level, including the regulation of incorporated associations and cooperatives.

What is proposed

The consultation paper states that this review aims to:

- 1) refine the ten principles to reflect current practice of good governance, informed by an up-to-date understanding of the operational context of the NFP sector;
- 2) introduce descriptions of good governance in the form of “supporting practices”; and
- 3) identify and provide additional resources to assist NFPs to apply the principles in their own unique circumstances.

General comments

While our answers to the consultation questions relate to the sector as a whole, our focus in considering these issues is the small or micro organisations that will benefit most from guidance on good governance practice and are the most numerous members of this constituency.

The consultation paper recognises that small organisations comprise a significant segment of the NFP sector, with 67% of all charities having “less than \$250,000 in annual revenue and 40% have less than \$50,000. Half of all charities operate with no paid staff and rely entirely on volunteers”.⁶ Of course, not all not-for-profits are charities, but many of them are.

We suggest that to address the needs of these small organisations, it is necessary to either incorporate additional segment-focused guidance or to develop separate but complementary resources. This additional or complementary guidance could address the lack of sophistication that hampers access to the proposed guidance at an early stage of an organisation’s development. For example, many NFPs are incorporated

³ Australian Institute of Company Directors, above n, 4.

⁴ Australian Institute of Company Directors, above n, 5-8. See also, for example, the Royal Commission into Institutional Responses to Child Sexual Abuse – Final Report.

⁵ Notably, the establishment of the Australian Charities and Not-for-profits Commission in 2012 as a specialist charity regulator, and further tax and funding changes are set out in the consultation paper as mentioned above.

⁶ Australian Institute of Company Directors, above n, 5.

associations, which have committees and committee members, not boards or directors. While this may be a matter of terminology only, we suggest that it is important to flag to these committee members of incorporated associations that these governance obligations relate to their roles and that they do in effect, face similar risk management challenges as directors of larger organisations.

The use of terms such as "risk appetite", with which larger organisations are familiar, may require further explanation in the case of the more unsophisticated groups. Obviously, minimising risk and implementing processes aimed at risk management is essential – and this is recognised in Principle 5. Many small organisations may not have a risk management plan and the importance of this should be emphasised.

As you are aware, many small associations struggle to find sufficient volunteers to constitute and maintain their committees, let alone choose officeholders on merit, seek diversity, engage in succession planning or have fixed tenures – in accordance with paragraphs 3.1 to 3.5 of the proposed supporting practices. While these principles will remain aspirational for these groups at an early stage of their evolution, we acknowledge their importance in the context of a set of 'principles' designed to provide a framework to assist NFP organisations to achieve good governance.

Additionally, some small organisations may not initially appreciate the range of interested parties that comprise their "stakeholders". It would be helpful to include an example which sets out a list of the stakeholders of, for example, a local netball association, where stakeholders may include the players, parents, officials and the community at large.

We applaud the proposal to include case studies, charters, checklists and templates. Due to their lack of resources, smaller organisations will greatly benefit from access to a range of resources such as checklists and templates. It is appropriate and very helpful that the proposed case studies will model not only a large mature organisation but also a smaller one, such as a sporting club.

Question 1: Do you support the provision of supporting practices? If not, what alternative do you recommend?

The Law Society supports the provision of supporting practices. The revised Principles and Guidance will be more effective in achieving its objective, and more accessible, particularly for smaller organisations, with the additional guidance provided in the proposed supporting practices.

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

As indicated above, we consider that checklists and templates would be the most valuable resources in supporting users of the revised Principles and Guidance to apply the principles to their organisations. A risk management checklist, for example, (particularly for smaller organisations) would be extremely helpful. Template statements of "matters reserved for the board" and "board delegation of authority policy", would also be useful. Case studies showing the application of the principles in particular scenarios are also very helpful.

Question 3: Do the proposed 10 principles adequately capture the high level principles of good governance in the NFP context? Should any be added, changed or removed?

We support the proposed 10 principles as drafted, subject to the following comments. As a general comment, we suggest that there may be a degree of overlap in the proposed revised principles and too much emphasis on the board itself.

We support the first six principles without any alteration. We also support Principle 7 in relation to accountability, but suggest it should be expressed as applying to the organisation as a whole, and not just to the board.

We also support Principle 8, relating to culture, but query whether in the current climate⁷, it could rank higher than number 8 in a set of 10 principles.

We suggest that integrity and ethics (Principle 9) could be treated as part of "culture", and that stakeholder engagement (Principle 10) could be treated as part of "accountability".

If Principles 9 and 10 are subsumed into other principles, as suggested above, there would be room for a new principle to capture the relationship and interface between the board and management.

We also note that none of the principles appear to deal effectively with complaints procedures (internal and external) and whistleblowers. These would appear to be very important considerations in the light of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry and the Australian Prudential Regulation Authority, *Final Report of the Prudential Inquiry into the Commonwealth Bank of Australia*.⁸

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

In general, we consider that the proposed supporting practices do appropriately capture the features of good governance relevant to each principle. Specific comments which relate to some of the proposed supporting practices are set out below.

Principle 2: Board's role and responsibility

We suggest that in relation to Principle 2, a manual for directors (committee members) would be a very useful resource document for small associations.

Principle 3 - Board composition

As mentioned above, while most small associations would support the aspirational requirements of Principle 3, it may not be feasible to appoint directors based on the prescribed criteria.

Principle 5 – Risk management

Small organisations may find the term "risk appetite" confusing. We suggest that many would appreciate help with a risk management checklist.

⁷ See, for example Australian Prudential Regulation Authority, *Final Report of the Prudential Inquiry into the Commonwealth Bank of Australia*, 81-93.

⁸ Ibid.

Principle 7 - Accountability

We suggest that some small organisations may struggle to identify who are their "stakeholders" and what is meant by and involved in the concept of "appropriate reporting to stakeholders" (7.2).

Principle 8 - Culture

We suggest that many small organisations may struggle with the concept of overseeing "a strategy to achieve meaningful engagement of stakeholders" (8.1).

Principle 9- Integrity and ethics

Many small organisations would appreciate a template "code of conduct" applicable "to the people involved in the organisation including the board" (9.1). A checklist or strategy for identifying and managing director's conflicts of interest (9.2) would also be most helpful.

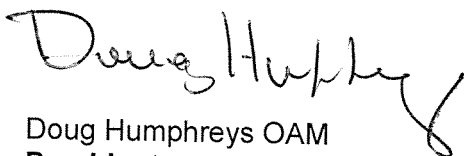
Conclusion

We appreciate that the governance framework established under the Principles and Guidance is designed to be flexible and able to be adapted as appropriate and applied by organisations having regard to their particular circumstances – purpose, structure, size and available resources. The focus is not intended to be on one segment of the NFP sector only. For this reason, it may not be considered appropriate to adapt the terminology to suit the least resourced and sophisticated segment of the sector, if this governance terminology is used by most or many of those organisations at which it is aimed.

We suggest, instead, that complementary guidance and resources aimed at addressing the needs of the very small and less resourced organisations might 'bridge the gap' and better address the needs of those bodies. It may be possible for the Principles and Guidance to be issued together with these additional resources to be used by such organisations to take the first steps in the development of a governance structure.

If you have any questions in relation to this submission, please contact Liza Booth, Principal Policy Lawyer, on (02) 9926 0202 or liza.booth@lawsociety.com.au.

Yours sincerely,



Doug Humphreys OAM
President