

For the love and/or for the money - good governance remuneration practice for NFP non-executive directors –

Steven Cole Lib (Hons) FAICD
Cole Corporate
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Precis of Paper

- (a) Historically the provision of board or management committee services by non-executive directors to NFP organisations has largely been on a voluntary, gratuitous and non-remunerated basis.
- (b) This paper analyses the suitability of this approach in a contemporary context given emerging needs and demands for the NFP sector and the ability of NFP organisations to recruit the best talent to their boards or management committees.
- (c) The paper goes on to discuss good governance practice and different bases for award, or otherwise, of non-executive director remuneration depending on the needs and circumstances of the particular NFP organisation.

(*) About the Author

Steven Cole has over 40 years of experience on ASX, commercial, proprietary, public sector and NFP boards. Relevantly Steven's board and committee experience in the NFP sector has covered sporting and community associations, educational institutions (secondary and tertiary), business and professional associations, philanthropic fundraising causes, and charitable organisations in the aged/disability care, youth at risk and welfare sectors.

1 Introduction

In one form or another, and whether registered as companies limited by guarantee under the Corporations Act (Cwlth) or as associations incorporated under State/Territory legislation, there are hundreds of thousands of entities comprising the not-for-profit (“NFP” or “for purpose”) sector of the Australian economy.

Based on official Australian National Accounts: Non-Profit Institutions Satellite Account (2012 – 2013 released in August 2015) drawing on ATO data from around 57,000 “economically significant” NFPs (revenue base in excess of \$50,000 p.a – so as to exclude the vast majority of small community, sporting and other NFPs) these 57,000 NFPs accounted for:

- \$79 billion p.a value added to the Australian economy;
- 1,081,000 employed persons;
- 3,882,000 volunteers contributing between them 521 million hours p.a. (or approximately 265,000 FTEs).

Principal industry sectors covered by these economically significant NFPs included:

- | | | | |
|---------------------------|----------|---------------|---------|
| • education and research | (c. 30%) | • environment | (c. 7%) |
| • social services | (c. 20%) | • unions | (c. 3%) |
| • health (incl hospitals) | (c. 19%) | • religion | (c. 3%) |
| • culture/recreation | (c. 14%) | • other | (c. 4%) |

All incorporated NFP organisations, whether “economically significant” or otherwise are governed by a board or management committee typically of between 5-10 people, the vast majority of whom act in a non-executive capacity to help guide, direct and support the organisation to which they are appointed towards the achievement of the organisation’s strategic mission and operational goals.

The performance expectations upon NFP organisations, and those in charge of them, are ever growing with:

- more and more traditional government welfare services being outsourced to NFP organisations with resultant “responsibility transfer” from the government to the NFP sector;
- greater regulatory and compliance requirements and expectations with potential liability consequences for those falling short of prescribed standards;
- high community and social expectations for organisational outcomes and probity standards of those in charge of NFP organisations;
- reputational risks for NFP organisations, and those in charge of them, in an age of heightened information awareness and social media activism.

This growth in performance expectations prevails notwithstanding increasing funding challenges for NFP organisations both from competition between NFP organisations for limited or relatively limited government grant funding and private philanthropy, and also tensions as to funding responsibility between government, private philanthropy and “user pay” advocates.

These drivers in turn have lead to the need for:

- greater economies of scale for NFP operations in order to deliver the required standard and level of service delivery, especially within funding constraints;
- strategic outcomes to be delivered through more sophisticated business and commercial models than traditionally have been the case;
- more developed governance and management frameworks, practices and responsibilities for NFP organisations.

As a consequence, those in charge of NFP organisations need to have greater and more refined skills, acumen, experience and personal commitment to bring to the benefit of the organisation and its purpose or cause, to address these expectations and drivers.

This paper draws upon a number of key findings from the Australian Institute of Company Directors “Not-for-Profit Governance and Performance Study” 10th Edition 2019 including:

- “NFP board workloads are rising as regulatory and community expectations of boards increase and as governance becomes more complex”
- “... some NFP boards have found it hard to recruit younger directors ...”
- “ there has been little change [over recent years] in the proportion of NFPs that pay board fees, despite rising workloads and risks”

A quote from one respondent to that study succinctly summarises the matter:

“The responsibilities of NFP directors are increasing and we need more of their time, which may be beyond reasonable volunteer expectations.”

Traditionally in Australia, despite some exceptions to the norm, the services of non-executive board and management committee members of NFP organisations have predominantly been on a voluntary, gratuitous and non-remunerated basis.

A purpose of this paper is to examine whether or not this approach should remain the norm or whether, depending on the needs and circumstances of the case, the continuation of such an approach may not be in the best interests of the NFP organisation – after all, the ultimate test against which to benchmark.

For the sake of clarity, this paper is not directed towards large multi-million/billion dollar co-operative and mutual based corporations commonly operating on commercial principles in the agricultural, health insurance, insurance or financial sectors, notwithstanding their technical not-for-profit status. It is the author’s understanding and experience that such enterprises rightly remunerate their directors at commercial rates benchmarked against their for-profit counterparts.

2 Overarching Principles

- (a) From the perspective of the best interests of the NFP organisation, or for any organisation, remuneration of directors, officers and/or employees is largely a means to an end, with the “end” being the procurement of the services of an appropriately skilled, experienced and committed human resource to add value to the organisation in the pursuit of its strategic and/or operational goals.
- (b) Remuneration is but a tangible and financially liquid form of benefit exchanged in return for services rendered. It is not an end in itself especially in the context of the NFP sector where:
 - a relatively high level of volunteer labour traditionally has been available; and
 - depending on the sector in which the NFP organisation operates, other non-monetary less tangible benefits may be available by way of reward to incentivise the provision of services (refer sections 2(e)(ii) and 5(b) following);
- (c) In purely economic terms, to justify remuneration, which by necessity results in a depletion of financial resource to the NFP organisation, there must at least be a compensating factor or benefit flow to the organisation to warrant that financial resource depletion. That compensating factor or benefit flow might be accountable against the question.

Were it not for the remuneration, or the relevant level of remuneration:

- *the relevant services or the specific nature of the relevant services (including political, business and/or social influence);*
- *the standard or quality of provision of the relevant services;*

- *the level of commitment and/or longevity of the assurance of timely availability of the provision of the relevant services;*
- *the competitive pool and diversity of prospectively available suitable personnel from which to choose to provide the relevant services,*
would not be available to the NFP organisation in furtherance of its strategic and/or operational objectives?

(d) The corollary to that question, in purely economic or financial terms, is the statement that *“unless that compensating factor or benefit flow for the NFP organisation is present, and exceeds in assessed value the remuneration (at the level) to be paid, then remuneration, or remuneration at the relevant level, should not be paid.”*

(e) However, matters must be considered not merely in pure economic or financial terms. Other factors also need to be taken into consideration:

(i) [Social and cultural considerations for the organisation]

Practices of an NFP organisation should be reflective of the organisation’s ethos and culture which typically might include concepts of fairness, equity, doing-the-right-thing, integrity, community, support, inclusion etc. The manner in which the organisation deals with its personnel who contribute to its mission outcomes should be consistent with these values. On the one hand this lends itself to principles of fair reward for effort and skills contributed, responsibilities assumed and risks undertaken. Yet on the other hand, in practice, typically the organisation may pay some staff yet call upon other “volunteers” to provide their services gratuitously without remuneration.

Perhaps “volunteering” in such organisations is highly respected and revered, with that respect and knowing contribution to the cause (or organisational mission) being the “benefit” sought by the volunteer in exchange for the services. But how does the organisation culturally reconcile a material change in treatment for one group of volunteers, i.e. its board or management committee members, if they were to move to a remunerated basis for their services, compared with another group e.g. the op-shop or front-line service volunteers to whom a move to remunerated basis for their services is not to be offered?

The attitudes of the organisation’s grant funders and philanthropic benefactors should also be considered in the event that the payment of board member remuneration be a negative to the availability of their continuing support to the organisation.

(ii) [Benefits accruing to a volunteer board member other than financial remuneration]

Financial remuneration is but one form of benefit or reward available to a non-executive director/volunteer on an NFP organisation board or management committee. Other benefits, depending on the NFP organisation and the individual volunteer, may include:

- personal ethical alignment and wish to support the cause or “give back” to society;
- for a person with surplus “time on their hands”, helping to give them a useful purpose in life;
- practical board experience and skill development and possible board career training and enhancement;
- attendance at board member professional development and educational courses funded by the NFP organisation, from which the board member may also derive personal benefit;

- business and social networking and association with other board/committee members or with profiled celebrities with whom the NFP organisation may associate from time to time in support of the organisation's cause;
 - depending on the NFP organisation, complimentary or privileged seating/entertainment at events in which the NFP organisation is involved (perhaps more relevant for profile arts and sporting NFP organisations);
 - paid travel and accommodation expenses for interstate and/or overseas meetings or events or conference attendance (e.g. in a representative capacity for the organisation at a peak industry body meeting, sporting event or conference).
- (iii) [Ensuring a diverse and competitive pool of prospectively suitable personnel]

If service on an NFP organisation's board or management committee is to be on a voluntary, gratuitous and non-remunerated basis, then logically the members of a broad section of the population who cannot afford to gratuitously offer their time on such a basis, through personal economic need for themselves and their families, are implicitly excluded from providing their services. If financial remuneration was offered for their services, then the pool of prospective candidates for the role, and the diverse nature of that pool, is likely to increase. Within this increased more diverse pool of candidates might be the person who best suits and can best contribute to the NFP organisation's needs and goals.

- (f) It is only the NFP organisation and its board, in conjunction with the approval of the members of the organisation (as applicable) and in compliance with any relevant constraints:
- in the organisation's constitution and/or governance charter (as applicable); and
 - in the terms of the legislation or regulatory framework governing the organisation,

that a decision concerning the remuneration of the organisation's non-executive directors, and if so in what manner and to what extent, can be made. It is an important decision and one which must be made in good faith for a proper purpose in the organisation's best interests having regard to all relevant circumstances, be they economic, financial, social, cultural or otherwise.

3 Legal and regulatory considerations

- (a) Constituent legislation.
- (i) Most Australian NFP organisations are typically constituted either as:
- companies limited by guarantee under the Corporations Act (Cwlth) – commonly larger NFP organisations, those with international or multi-State/Territory activity, and those with more commercial service offerings (even if for charitable causes);
 - associations incorporated under the various associations incorporation legislation of the applicable State or Territory in which the organisation primarily operates or had its origins.
- (ii) In the case of companies limited by guarantee under the Corporations Act, and given that such companies are regarded as “public companies” for the purposes of that legislation, there are a number of legislative provisions that may be relevant in the context of non-executive director remuneration (subject to some exceptions) including:

- [S.150(1)(c)] – Concerning the need for approval by the board for payments to directors:

The organisation having the obligation to disclose the remuneration paid to each of its directors, or those of a subsidiary or entity controlled by the organisation:

(A) [S.202B] If directed to do so by:

- members holding 5% or more of votes able to be cast at a general meeting; or
- 100 voting members (or more).

(B) [S.300A] In the Remuneration Report comprised within the Directors' Report section of the organisation's Annual Report.

- [S.208] The remuneration of a director (a "related party" of the organisation) is a "financial benefit" which may only be given if:

(A) it is approved by members in general meeting [refer Ss 217-227] and is paid/given within 15 months of that approval; or

(B) an exception applies [refer Ss.210-216].

The principal relevant exceptions are:

- [S.211] The remuneration is reasonable given the circumstances of the organisation, and the circumstances of the director (including the responsibilities involved in the office or employment of the director);
- [S.212] The remuneration is by way of D&O indemnity or insurance premium payment (or related relevant legal costs), and to give it is reasonable in the circumstances of the organisation.

- [S. 180, 181, 182, 183, 184 and Common Law] Directors owe fiduciary duties to the organisation on which they serve. These duties temper a director's ability to act in their own best interests, to "work to rule", or possibly even withhold their services (other than to resign), if they are dissatisfied with the risk/exertion/reward relationships of their appointment in the circumstances of the corporation that may arise from time to time.

- [s.195] Directors who have a material personal interest in a matter being considered at a board meeting must not be present during deliberations and must not vote on the matter (subject to certain exceptions). However these legislative constraints do not apply with respect to a matter in relation to a director's remuneration as a director of the organisation [refer S.195(1A)(b) and S.191(2)(a)(ii)] even if good governance practice may recommend such practices be observed.

(iii) In the case of organisations incorporated under State/Territory associations incorporation legislation, regard should be had to the specific provisions of each piece of legislation applicable to the organisation. By way of example the following provisions of the Western Australian Association Incorporations Act 2015 (with comparable provisions applying under the relevant legislation in most other jurisdictions) are relevant to non-executive director remuneration:

- [s.5(3)(c) and (d)] An association does not lose its eligibility for incorporation under that legislation merely because a member

derives remuneration or salary paid in good faith as an employee or member of the management committee of the organisation.

- [s.26(2)(b) and Schedule 1 Division 2 paragraph 1] Constitutions and rules of association must provide that payments to be made to members of the board/management committee out of funds of the organisation (other than for proper out-of-pocket travel/accommodation expenses) must be authorised by resolution of members of the organisation.
 - [fiduciary duties and conflict of interest] Generally, comparable requirements as those mentioned above for companies limited by guarantee – refer Corporations Act ss180-184 and 195.
- (iv) Regard should also be had to the Australian Charities and Not-for-Profit Commission Act 2012 (as applicable) including for organisational registration, reporting and compliance requirements as well as responsibilities and liabilities of directors and officers. However the regulatory remuneration of board members, other than for proper accounting and financial reporting purposes, does not appear to be a matter within the current scope of that legislation.

(b) Constitution, Articles or Rules of the Organisation

The constitution, articles or rules of the organisation may also contain constraints concerning the payment of remuneration to board/management committee members. By way of example:

- Rule 15 of the “Model Rules” for association incorporated under the WA Associations Incorporation Act 2015 prohibit the payment of such remuneration (other than travel and other expenses properly incurred in attending meetings and business on behalf of the organisation) although such “Model Rules” may be amended by the organisation by special resolution of members – such a required provision may be typical in other jurisdictions as well;
- although there are no prescribed constitutional restraints concerning board/management committee member remuneration for companies limited by guarantee, the following example from the constitution of a prominent sporting organisation provides a prudential constraint to assure members of the organisation against the “agency risk” of those in charge of the organisation unduly favouring themselves with remuneration without prior reference to the members:

“5.9 Payment to Directors prohibited

(a) *Subject to Article 5.9(b), the Organisation must not pay any fees to a Director for performing his or her duties and responsibilities as a Director unless the Members in general meeting have approved the payment or the Members in general meeting have approved payment of fees to Directors, at the discretion of the Board, with a maximum annual pool or cap amount for all Directors in any one year, and the payment is within that annual pool or cap amount.*

(b) *A payment of the kind referred to in Article 1.5(b) may be made to a Director if that payment has been approved by the Board.*

[Article 1.5(b) refers, as relevant, to remuneration that complies with Article 5.9(a) and out-of-pocket expenses properly incurred by the Director in connection with the affairs of the Organisation]”

(c) Governance or Board Charter and/or Policies

Contemporary accepted good governance practice by the organisation may also have resulted in a governance or board Charter, and/or a range of governance related policies, having been adopted by the organisation’s board concerning

certain governance related structures, policies and procedures that are to apply to the organisation and its governance.

If such a Charter and/or policies have been adopted, then due regard should be had to any provisions or constraints relating to board/management committee member remuneration that may be contained therein.

(d) Legislation protecting volunteers from civil liability

All States and Territories have passed legislation which provides a modicum of protection and exclusion of liability for those providing or being engaged in “community work” in a voluntary, gratuitous and non-remunerated capacity for community/charitable based organisations. Relevant legislative provisions are as follows:

- Volunteer Protection Act 2001 (SA);
- Volunteer Protection Act 2002 (VIC);
- Civil Liability Act 2003 (Qld);
- Civil Liability Act 2002 (NSW);
- Volunteer (Protection from Liability) Act 2002 (WA);
- Personal Injuries (Liabilities and Damages) Act 2003 (NT);
- Civil Law (Wrongs) Act 2002 (ACT);
- Civil Liability Act 2002 (TAS).

If remuneration is to be paid to a non-executive director, then whatever protection from and exclusion of liability afforded by those legislative provisions will be lost to the non-executive director.

However with respect to the protection of liability afforded by those legislative provisions, the following aspects should be more fully considered with professional advice taken having regard to the relevant jurisdiction involved:

- (i) Any exclusion is for civil liability only, not criminal liability.
- (ii) The relevant State/Territory legislation will be subordinate to Federal legislation, including under the Corporations Act which prescribes duties (and liability for breach of those duties) of directors of companies limited by guarantee. The Corporations Act contains no comparable provisions concerning limitation or exclusion of liability for volunteer directors. Accordingly at best, subject to the below comments, the legislation may be effective to limit or exclude liability (subject to exceptions described in the relevant legislation) of voluntary non-remunerated board/management committee members of NFP organisations incorporated under the associations incorporation legislation of the relevant State/Territory.
- (iii) The legislation in some States/Territories expressly provides that the performance of responsibilities of office of a board/management committee member of an NFP organisation is to be regarded as “community work”, so as to attract the exclusion of liability (to the extent provided) for volunteer non-remunerated directors and officers. The legislation in a number of other States/Territories does not so expressly provide, and accordingly in those other States/Territories the availability of such protection is either unlikely, or is moot, pending clarification or judicial interpretation of the relevant provisions. Specific legal advice should be sought if protection under these legislative enactments is to be relied upon.

4 Remuneration structure

4.1 Flexibility of approach

Properly managed and structured, existing legislative, constitutional and “good practice” requirements allow significant flexibility and discretion to a board/management committee to determine whether, and if so the manner in which, its non-executive board/management committee members are remunerated. However, if proceeding in this respect, the following prudential practices are strongly recommended for NFP organisations:

- (a) prior approval by members of the organisation as to the structure and process by which the remuneration is to be set;
- (b) clear limitations on the extent of the aggregate of non-executive director remuneration, without prior informed member approval; and
- (c) reasonable transparency and accountability of non-executive director remuneration outcomes.

The balance of this section 4 proceeds on the assumption that remuneration of non-executive board/management committee members is warranted having regard to the various factors discussed in section 2 of this paper and that any relevant legislative, constitutional or governance charter/policy constraints discussed in section 3 of this paper have been addressed. This assumption should not necessarily be taken as endorsement to the appropriateness of such an approach for all NFP organisations, in all circumstances.

4.2 Differing nature of approaches to remuneration

- (a) Non-executive director remuneration policies of different organisations may vary significantly:
 - (i) from the “egalitarian” approach (i.e. all non-executive directors are treated as of equal value and are rewarded accordingly) to a “differential reward” approach (i.e. recognising that the contribution of some non-executive directors may be more significant and valuable than others, or that to attract a particular non-executive director of perceived value to the organisation, a higher fee may need to be paid than is paid to other non-executive directors);
 - (ii) from the “swings and roundabouts” approach (i.e. sometimes the work of boards/management committees and their members is busier and more demanding than other times) with non-executive directors’ fees set as a relatively flat or constant reward irrespective of the complexity, duration or scope of exertion required from time to time, to a variable “fee for service” approach (i.e. which may see a relatively lower base fee, but with incremental extra fees payable to non-executive directors for extra responsibilities, committee work and exertion from time to time).

- (b) This variation is perceived to be healthy in an open competitive market for services, and may well also respond to the diversity of NFP organisations from large trans-national organisations, to national multi-million dollar enterprises, to small project or cause specific or local community based organisations.
- (c) Without detailed research, any commentary on industry norms as to non-executive director remuneration policies for NFP sector organisations is anecdotal only, especially given the historical pre-disposition for non-executive board/management committee members not to be remunerated, and for their services to be provided on a gratuitous voluntary basis. However, it is perceived that amongst those NFP organisations that do remunerate their non-executive officers, their policies have tended towards an egalitarian/swings and roundabouts bias, with contemporary practices trending towards an egalitarian/fee for service bias. Such an outcome is perceived to be consistent with trends and practices in commercial or for-profit sector corporations with respect to their own directors.
- (d) Further areas for consideration by NFP organisations include whether:
 - (i) the “headline amount” of remuneration payable is to be inclusive or exclusive of superannuation paid by the organisation on behalf of the non-executive director;
 - (ii) further remuneration may be paid to the non-executive director on account of “extra-ordinary exertion” at times of organisational crisis where the demands of office may well exceed any reasonable contemplation of the continued provision of services without extra reward being paid over and above usual base remuneration allowances;
 - (iii) payment by the organisation of:
 - premiums for D&O insurance, inter alia for the benefit of the non-executive director, at least to the extent permissible at law;
 - professional advice taken by a non-executive director, in accordance with organisational policy, concerning matters arising in the performance of his/her duties of office,
 should be considered within the scope of non-executive director remuneration (although generally the commonly accepted approach is that such items are not regarded as “remuneration”).
- (e) For the purposes of this analysis it is assumed that payment or reimbursement of out-of-pocket expenses properly incurred in the performance of a non-executive director’s responsibilities of office is an “entitlement”, and is not regarded as “remuneration”.

4.3 Differing nature of approaches to the quantum of remuneration and how it is shared among non-executive directors

- (a) Anecdotal evidence suggests material diversity in approach to non-executive director remuneration especially between:
 - different industry sectors;
 - larger more complex and sophisticated NFP organisations compared with smaller less sophisticated community based NFP organisations,
 although sometimes also between comparable organisations in the same or similar industry sector, but with different philosophies of approach and organisational culture as to non-executive director remuneration.
- (b) Listed below are some of the approaches to non-executive director remuneration commonly taken by different NFP organisations:
 - (i) The determination of an annual maximum remuneration “Pool” approved of by the organisation’s members, giving the board the power to award

remuneration to non-executive directors at the board’s discretion provided that the aggregate of remuneration awarded in any year does not exceed that “Pool”. Such an approach:

- merely provides a “cap” to manage the agency risk of the board’s generosity with respect to board members benefitting themselves in excess of the expectations and authority of the organisation’s members;
 - leaves open to board discretion the amount of remuneration actually awarded to all or any board/management committee members, or the basis of such awards, provided the “Pool” is not exceeded.
- (ii) Non-executive director remuneration benchmarked against that receivable by a non-executive director of a commercial/for-profit corporation of comparable size, revenue, employee base, business complexity and industry sector. Of interest comparable benchmark data of such remuneration of non-executive directors of public listed entities is readily available due to Corporations Act and ASX Listing Rule regulatory disclosure requirements.
- (iii) Non-executive director remuneration benchmarked against that receivable by a non-executive board member of a public sector board or statutory authority of comparable size and operational base and complexity, given that such remuneration is usually objectively set by an independent public sector commission or authority.
- (iv) Non-executive director remuneration being a payment more in the nature of an honorarium or relatively modest payment, either on an annualised basis or on a per meeting/sitting basis.
- (v) In most cases, payment or reimbursement of proper out-of-pocket expenses incurred by the non-executive director in the performance of his/her responsibilities of office in the affairs of the organisation.
- (c) To give some very broad context as to the quantum of “base” non-executive director remuneration that might be paid under some of the approaches referred to in paragraph (b), based on the author’s experience and anecdotal research, the following estimates are provided:
- [paragraph (b)(ii) – commercial/for-profit corporation comparators]
\$50,000 to \$100,000(+) p.a.
 - [paragraph (b)(iii) – public sector boards/statutory authority comparators]
\$20,000 to \$50,000(+) p.a.
 - [paragraph (b)(iv) – relatively modest/remuneration/honorarium style comparators]
\$5,000 to \$20,000 p.a.
- (d) Credible data from the Australian Institute of Company Directors “Not-for-Profit Governance and Performance Study” 10th Edition 2019 shows that there is a strong correlation between the likelihood of remuneration of non-executive directors and the size of the NFP organisation – refer table below.

Size of NFP organisation (revenue p.a. \$m)	% of NFP organisations which remunerate non-executive directors
>\$100m	45%
\$20m to \$100m	≈39%
\$5m to \$20m	19%

\$1m to \$5m	9%
<\$1m	1%

The survey did not also interrogate the amount of remuneration paid to non-executive directors.

4.4 Governance considerations in setting non-executive director remuneration

- (a) Generally the control, direction and management of incorporated organisations is assigned to the board/management committee of the organisation, subject to any reservations of authority retained and determined by the members of the organisation in general meeting.
- (b) In the context of the board/management committee of an NFP organisation having the authority to set, or at least recommend to members of the organisation for approval, the remuneration of members of the board/management committee, the “agency risk” of such authority or recommendation needs to be addressed with risk of conflicts of interest arising.
- (c) Depending on how the board/management committee addresses this issue, questions and concerns may arise as to:
 - the probity of the decision or recommendation;
 - conflicts of interest, and/or
 - the ethics,
of those non-executive directors involved.
- (d) Mitigation of the risks of such concerns arising are more likely to be achieved if:
 - there is transparency and candour of communication between the board/management committee and the members and stakeholders of the NFP organisation concerning such matters;
 - the NFP organisation has adopted a governance policy concerning remuneration of non-executive board/management committee members which has been openly shared with the organisation’s members and stakeholders;
 - usual conflict of interest protocols (disclosure of conflict, abstention from involvement in deliberations and from voting on the matter, with due recording of such matters in the relevant meeting minutes) be observed so that to the greatest extent practicable no board/management committee member is ultimately determinative of their own remuneration;
 - independent and objective professional advice and/or comparative analysis against other NFP organisations (of comparable size, complexity and industry sector) is undertaken to provide base data against which to benchmark the decision taken to pay or recommend remuneration, and the recommended amount of that remuneration.

5 Special Industry Sector Organisational Size and Other Considerations

- (a) NFP organisations cover an extra-ordinary broad array of industry sectors, strength of balance sheets, funding sources (and extent/reliability of that funding), public benevolent v's personal member interest mission outcomes, organisational size and strategic/operational/regulatory compliance complexity.
- (b) Some NFP organisations provide attractive non-financial benefits to their board/management committee members so that financial remuneration is not as relevant in order to attract quality non-executive directors. For example:
- [for some major arts and sporting NFP organisations] Event attendance, seating and celebrity fraternising opportunities;
 - [for many NFP organisations with national or international meeting attendance requirements for certain of its board/management committee members] Travel and accommodation expenses paid for such meeting attendances may well be considered by some non-executive directors as an attractive benefit.
 - [for some profile NFP organisations] The business or community status that comes with being a board/management committee member of that particular NFP organisation.
 - [for many NFP organisations] The preparedness of the organisation to fund relevant professional education and training courses for their board/management committee members (who may derive personal benefit therefrom in addition to the benefit to the NFP organisation by reason of the upskilling of such directors).

Where such benefits are material and attractive to the organisation's board/management committee members, then the question may be asked whether the "Overarching Principles" in section 2 of this paper have been satisfied to warrant the payment of remuneration.

- (c) Many other small community, arts, sporting, religious, educational, humanitarian, charitable or welfare organisations, especially those which provide a community gathering or support more focussed on the individual interests of their members, might not:
- be culturally attuned to the award of remuneration;
 - be sufficiently financially endowed to offer remuneration;
 - have a degree of organisational or business sophistication and challenge that otherwise would warrant the payment of remuneration,
- for their board/management committee members.

- (d) There are also some NFP organisations where material financial or other in kind support from a passionate benefactor to the organisation (in support of its purposes and causes) may be tied (expressly or implicitly) to the expectation of a position being offered on the board/management committee of the organisation. The offer of remuneration to that benefactor would not be relevant to the attraction of that benefactor to the organisation (or its board/management committee).
- (e) These are just a sample of a broad array of considerations that may apply and which warrant reflection.

6 Arguments for and against the payment of remuneration in appropriate cases

- (a) [The “for” case]

This section seeks to summarise the rationale for the purposes of remuneration in appropriate cases, subject to the considerations mentioned elsewhere in this paper.

- (i) Fair reward for the board/management committee members’:

- time commitment;
- expertise, acumen and skill;
- assumption of responsibilities of office;
- assumption of risks (liability and reputational) associated with the responsibilities assumed,

noting that the legal regulatory compliance and overall performance expectations upon non-executive board/management committee members of NFP organisations have increased materially over recent decades.

- (ii) Incentivisation to attract high quality directors who are prepared to commit to the responsibilities of office.
- (iii) Increasing the available pool, and the diversity of that pool, of prospectively suitable directors to include those who might be suitable but, from a personal financial perspective, cannot afford to offer their time and services on a gratuitous basis.
- (iv) Securing the assured time, commitment and prioritisation of workload of board/management committee members through contractual payment for such time, commitment and prioritisation. Although such expectations may be able to be secured culturally even without remuneration, the psyche of the board/management committee member is likely to be more attuned if contractual remuneration is paid, rather than a psyche of “mere gratuitous contribution”.
- (v) The organisation notionally being in a stronger position to “hold to account” the relevant board/management committee member for his/her responsibilities and duties of office and performance outcomes by reason of the contractual “fee for service” paid, rather than a psyche of “mere gratuitous contribution”.
- (vi) Finally and importantly, the payment of remuneration “monetarises” the value of the contribution of the relevant board/management committee member, a contribution the value of which is otherwise reasonably ethereal. For example a benefactor who contributes (say) \$50,000 p.a. to a charitable organisation would be highly regarded, yet a board/management committee member’s voluntary gratuitous non-remunerated contribution may be of comparable commercial value, but not as comparably recognised.

(b) [The “against” case]

This section seeks to summarise the rationale as to why remuneration should not be paid, subject to the considerations mentioned elsewhere in this paper:

- (i) If the services of appropriately skilled, experienced and committed non-executive directors can be secured through non-remunerated volunteers, then it is questionable as to why it is in the best interests of the organisation to deplete its financial resources by paying non-executive director remuneration.
- (ii) Where the NFP organisation significantly enjoys the benefit of a range of services from volunteers, then unless the organisation intends to remunerate all its volunteers for their services, why should the non-executive directors be singled out for special differential treatment?
- (iii) Generally many NFP organisations are “mission” or “for purpose” driven. The underlying culture for those involved in such organisations is typically passion for the mission or purpose of the organisation. There is risk of loss, or dilution, of that culture if those sitting on the ultimate decision making body of the organisation do not necessarily innately share that passion without financial incentivisation. The potential loss or dilution of the NFP organisation’s culture may have longer term unintended consequences.
- (iv) As volunteers, non-executive directors of incorporated associations (i.e. non Corporations Act entities) in at least a number of States/Territories gain the benefit of certain exclusions of personal liability for their endeavours, which exclusions would not apply if they were remunerated (refer Section 3(d) of this paper).
- (v) Even if not financially remunerated, non-executive directors of many NFP organisations derive other compensatory benefits arising from their service (refer section 2(e)(ii) and 5(b) of this paper).
- (vi) Finally and importantly, for many NFP organisations (especially smaller community, charitable, social, arts and sporting NFP organisations), the organisation is not sufficiently financially resourced, or sound, to warrant the payment of such remuneration.

7 A potentially innovative approach especially for NFP organisation with DGR tax status

The reward, or not, of remuneration need not be a binary outcome:

- having common application across all board/management committee members;
- with absolute depletion of the organisation’s financial reserves.

The organisation could pay remuneration so as to deliver the benefits recognised in section 6(a) of this paper (including 6(a)(vi)), yet at the same time, the board/committee member could elect to donate all or part of that remuneration back to the organisation as a financial benefactor.

This approach certainly has greater appeal if the NFP organisation has deductible gift recipient (DGR) status with the Australian Taxation Office as the tax otherwise payable by the non-executive director on the remuneration paid would be offset by the tax deductibility of the donation made.

8 Sample Policy Framework for Non-Executive Board/Management Committee Director Remuneration

For NFP organisations wishing to provide remuneration to their non-executive board/management committee members, Attachment “A” to this paper provides a Sample Policy template that may be of use as a draft to assist the organisation in developing its own policy on such matters.

9 Conclusion

Although board/management committee members of NFP organisations may historically largely have provided their services on a voluntary gratuitous and non-remunerated basis, the environment is changing and there is an increasing trend, in appropriate cases, for that historical approach to be reviewed.

This paper reviews various legal, economic, governance and cultural issues that arise, and which need to be considered, with respect to the remuneration of board/management committee members of NFP organisations.

NFP organisations are encouraged to have due regard to the contents of this paper in the context of their governance framework and their director succession and remuneration policies.

ATTACHMENT “A”

SAMPLE NFP ORGANISATION POLICY FRAMEWORK FOR NON-EXECUTIVE BOARD/MANAGEMENT COMMITTEE MEMBER REMUNERATION

1 Introduction to Framework

(a) Statement of Purpose of Framework

The purpose of this Framework is to describe the organisation’s policies and practices for non-executive director remuneration so as to:

- constitute sound non-executive director remuneration policy and practice within the existing governance, legislative and regulatory requirements and expectations that apply; and
- assure members, stakeholders and the community of integrity of process and outcome.

(b) Principles upon which this Framework is Premised

There are 5 key principles which have guided the development of this Framework:

- (i) Alignment with contemporary accepted good governance standards and principles including:
- remunerate fairly and responsibly;
 - compliance with legislative and regulatory spirit and intent;
 - accountability and oversight by the board.
- (ii) Integrity and probity of process and outcomes;
- (iii) Transparency of process and outcomes
- (iv) Benchmarking against objectively determined market and industry practices and reasonable expectations;
- (v) Periodic review.

(c) Review and amendment of the Framework

The organisation accepts that corporate governance best practice continues to evolve. To this end, the organisation commits to the periodic review of this Framework to maintain alignment with contemporary best practice from time to time.

2 Context of the Framework

(a) Constitution

This Framework is complementary to the organisation’s constitution.

(b) Governance Charter

This Framework constitutes a policy of governance of the organisation adopted by the organisation’s board in the terms of its Governance Charter.

(c) Remuneration Oversight

The board of the organisation itself, or via a relevant committee established by the board in the terms of its Governance Charter, is charged with responsibility for the implementation and oversight of this Framework.

(d) Principles of Sound Practice for Non-executive Director Remuneration Setting and Review

In applying this Framework regard will be had to the following:

- (i) Having in place processes that incorporate market benchmarking and/or independent advice (as appropriate), however NOT overly relying on advisers at the expense of the mature discussion and judgement of the board;
- (ii) Undertaking scenario testing of proposed remuneration arrangements to ensure their reasonableness having regard to cost/benefit/risk analysis in the best interests of the organisation;
- (iii) Ensuring non-executive director remuneration outcomes are fair, reasonable and publicly justifiable;
- (iv) Keeping abreast of stakeholder and general market sentiment on non-executive remuneration issues for like organisations;
- (v) Clearly communicating the organisation's approach to non-executive director remuneration and the policies applying from time to time;
- (vi) Accounting to the members of the organisation the actual remuneration paid from time to time by the organisation to its non-executive directors;
- (vii) Engaging appropriately with members and other relevant stakeholders about the organisation's approach to non-executive director remuneration;
- (viii) Reviewing the organisation's non-executive director remuneration arrangements and policies at least annually.

3 Determination and Approval of Maximum Non-Executive Director Remuneration Pool ("Pool")

- (a) The Pool must be of appropriate value to meet the objectives of the Framework and policy determinations made under it.
- (b) In determining the value of the Pool from time to time the following considerations should apply:
 - (i) The principle of remunerating fairly and responsibly having regard to the relevant work load, time commitments, skills and experience required, business complexity and risks assumed;
 - (ii) The number of non-executive directors required to properly, effectively and efficiently discharge the role, responsibilities and work of the board;
 - (iii) The quality, experience and skills of the non-executive directors;
 - (iv) Market benchmark, with other like NFP organisations, remuneration for non-executive directors of the quality, experience and skills required by the organisation having regard to the organisation's size (revenue and

- employee base), industry sector, regulatory compliance requirements, governance arrangements and business/operational complexity;
- (v) The capacity of the organisation to pay non-executive director remuneration;
 - (vi) Any policy constraints applicable to the organisation's employed personnel generally in accordance with the organisation's HR policies and practices;
 - (vii) Reasonable contingency allowance to give some discretionary flexibility to the board to accommodate the organisation's short to medium term board succession planning and recruitment, strategic development and growth expectations including inflationary pressures, as well as contingency needs for extraordinary exertion circumstances that may arise.
- (c) Only the members of the organisation by resolution in general meeting may set the value of the Pool. It is the responsibility of the board to adequately inform the members of relevant considerations and to recommend to the members in general meeting a resolution as to the value of the Pool to meet the organisation's reasonable needs.
- (d) Directors and key management personnel should not vote on a resolution of the members to approve the value of the Pool.
- (e) When seeking member approval in setting the value of the Pool from time to time, relevant principles of this Framework should be addressed in explanatory notes to the relevant proposed member resolution, including:
- (i) the organisation wishes to attract quality personnel to its board and needs to remunerate those people fairly and responsibly;
 - (ii) the organisation needs to award its non-executive directors appropriate market benchmarked remuneration relative to like NFP organisations;
 - (iii) the organisation has adopted this Framework to ensure that sound and prudential policies and practices are adopted and applied by the organisation and the board;
 - (iv) the following factors are relevant in considering the amount of any reasonable contingency allowance to be priced into the value of the Pool:
 - circumstances may arise where it is in the best interests of the organisation for non-executive directors to be required to provide extraordinary services well outside the predictable norm, or any reasonable tolerance threshold;
 - it is not in the interests of the organisation to price the risk of this contingency into the standard annual non-executive director remuneration;
 - it is at these times when the organisation will need and want its non-executive directors fully engaged, motivated and committed to the cause;
 - it is at these times that non-executive directors often assume additional personal liability risk in the performance of their duties, as well as extra time, effort and exertion inputs; and
 - significant "overtime" which a non-executive director is called upon to provide, warrants fair and reasonable recompense (especially if the

contingency of that overtime has not been priced into the non-executive director's standard annual remuneration entitlement).

4 Structure of Non-Executive Director Remuneration

- (a) Remuneration for the organisation's non-executive directors within the limit of the Pool will be determined by resolution of the board, after consideration of advice from the remuneration committee (as applicable), and will be structured on the following basis:
- (i) "Base Fee"

An annual base fee payable on a monthly or quarterly accruals basis to each non-executive director including by reference to the scope and extent of commitment of the services to which the Base Fee is referable ("Base Services");
 - (ii) "Additional Service Fee(s)" [as applicable]

An annual additional services fee(s) payable on a monthly or quarterly accruals basis to relevant non-executive directors whose responsibilities include additional services of a serial nature for the organisation as well as the nature, scope and extent of commitment of those additional services ("Additional Services"). For administrative convenience, the board may suggest these as a set percentage of the Base Fee. Such Additional Services Fee(s) are to recognise the extra services, over and above Base Services, provided by:

 - the organisation's chair;
 - non-executive directors serving on standing board committees (e.g. Audit, Risk, Governance etc as applicable);
 - chairs of those standing board committees.
 - (iii) "Superannuation Fees"

Determination by the board as to whether or not the Base Fees and Additional Service Fees are exclusive or inclusive of superannuation, including having regard to statutory base superannuation payment obligations for the organisation with respect to non-executive director remuneration.
 - (iv) "Extraordinary Exertion Fees" [as applicable]

The board reserves to itself the discretionary or right to award "Extraordinary Exertion Fees" to non-executive directors, in addition to Base Fees, Additional Service Fees and Superannuation Fees, subject to the following considerations:

 - The aggregate amount of Extraordinary Exertion Fees in any annual financial period may not exceed the difference between the value of the Pool and the aggregate of the Base Fees, Additional Service Fees and Superannuation Fees in that annual financial period without prior approval of the members in general meeting;
 - Conflict of interest protocols will be observed including proposals for Extraordinary Exertion Fees to be considered discretely for each non-executive director (in the absence of that non-executive director) by the remaining directors – also ensuring that there is not an implicit reciprocity understanding between non-executive

directors as to approval of each other's prospective Extraordinary Exertion Fees;

- Due consideration will be given to taking independent consultancy advice as to the appropriateness and quantum of any prospective Extraordinary Exertion Fees to assure objectivity and integrity in decision making. This consideration applies especially if the prospective amount of Extraordinary Exertion Fees is material.
- Without limiting the discretion of the board in awarding Extraordinary Exertion Fees:
 - the nature of the circumstance or criteria that might warrant consideration for the award of such fees is more likely to apply where extraordinary issues arise requiring material and extraordinary exertion by a non-executive director(s) such as dealing with an organisational crisis, major acquisition or divestment, or other demanding event;
 - the quantum of the award of such fees may be based on a an hourly rate, per diem rate, gross award or other reasonable basis having regard to the circumstances.

(b) The board, through and having regard to the role of the relevant board committee with responsibility for such matters (as appropriate), will:

- monitor the implementation of this Framework;
- monitor the market for non-executive director remuneration and good governance practices concerning such matters;
- annually review non-executive director remuneration levels and the value of the Pool approved by members;
- act in such manner to ensure that the principles upon which this Framework is premised continue to be honoured.

5 Expectations and contractual arrangements with non-executive directors

(a) This Framework constitutes a policy determination as part of the organisation's Governance Charter and therefore forms part of the contractual terms between the organisation and its non-executive directors.

(b) Each non-executive director by virtue of his/her appointment to office acknowledge:

- the expected time, commitment and exertion expectations of them;
- there is a reasonable threshold tolerance expectation upon extra exertion and time which the non-executive director may be called upon from time to time without expectation of Extraordinary Exertion Fees;
- the fiduciary duties owed by non-executive directors to the organisation may preclude the non-executive director withholding or limiting his/her services (other than resigning from office) at times of crisis, even if reasonable remuneration and compensation for the extra time, effort, commitment and risk cannot be assured.

6 Generally

- (a) This Framework is to be published as a policy determination under the organisation's Governance Charter.
- (b) Nothing in this Framework in any way limits:
- the entitlement of a non-executive director to be reimbursed out of pocket expenses reasonably and properly incurred by him/her in accordance with organisational policy in that behalf;
 - the organisation properly incurring professional development expenses from which a non-executive director may gain personal benefit;
 - the organisation effecting and paying the premium for a policy of Directors and Officers Indemnity Insurance, to the extent not prohibited by law, under which a non-executive director may incidentally gain benefit as an insured party;
 - the organisation indemnifying a non-executive director, to the extent not prohibited at law, from liabilities incurred by a non-executive director in the proper performance of their duties as a director.