“Tread your own Path”

Designing your organisation’s governance framework to be “fit for purpose” for its own unique needs and circumstances

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1 Introduction

1.1 About corporate governance

Corporate governance has been defined as "…the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled within corporations. It encompasses the mechanisms by which companies, and those in control, are held to account." [Justice Owen in the HIH Royal Commission, The Failure of HIH Insurance Vol 1, April 2003 at page xxxiv].

Governance is the domain or province of the board of the corporation. Boards are the collective group of those appointed in the terms of the corporation's constitution to:

- govern, direct and manage the corporation, including by way of delegated authority to the corporation's executive and management team;
- act in the best interests of the corporation in the pursuit of its goals and objectives; and
- account to the corporation's shareholders and regulators for the performance of:
  - the corporation in the pursuit of those goals and objectives; and
  - the board itself in the discharge of its responsibilities.

Board members are also charged with fiduciary and other duties and must operate within the construct of a body of laws (legislative, regulatory and judicial) which prescribe certain standards of conduct and behaviour designed to protect the corporation and its stakeholders from both malfeasance and misfeasance by those vested with stewardship of the corporation ("**agency risk**").

Typically boards comprise individuals with an array of skills, experience, knowledge, relevant interests and attributes who, as a collective, accept responsibility for the stewardship of the governance of the corporation.

1.2 Governance as a strategic advantage

Effective and sound governance is seen to be a strategic advantage:

(a) from a procedural and defensive perspective, designed to protect the organisation and its members' interests by:

- ensuring standards are maintained;
- ensuring regulatory compliance requirements are met;
- managing risk, including the "agency risk" of those entrusted with the corporation's direction and management;
- minimising the prospect of liability for the corporation and personal liability for its officers;

(b) from a substantive and offensive perspective, designed to enhance organisational performance by:

- assuring the robustness of the organisational platform from which strategic and operational opportunity can be leveraged;
- optimising the most effective marshalling and utilisation of scarce or precious resources (financial, human, physical, IT, intellectual property, management) for strategic and operational gain;

- delivering worthwhile and effective corporate performance and outcomes consistent with the corporation's goals and objectives for the benefit of the corporation and its stakeholders as a whole, having regard to their respective rights and interests.

2 Governance guidelines and standards

2.1 Governance frameworks

Over recent years various industry associations, NGOs and regulatory authorities (local, national and international) have published lists of standards, guidelines and recommendations concerning "good governance" for organisations for consideration, adoption and reporting against (as appropriate) by organisations within their respective domains.

What is broadly acknowledged across all of these standards, guidelines and recommendations is that there is no uniform governance solution which optimises the governance and performance outcomes of every organisation irrespective of its nature, size, purpose and peculiar needs and attributes. What is universally acknowledged is that "**one size does not fit all**" and that whatever governance framework is adopted and applied by a corporation, it has to be "**fit for purpose**" having regard to a number of factors, many of which may be unique to the corporation. These factors include the:

- nature of the organisation (public listed, commercial unlisted, public sector, charitable purpose, co-operative/mutual, university sector, community purpose etc)
- objectives and purposes of the organisation;
- environment and industry in which the organisation exists and operates;
- scale, spread and operational complexity of the organisation;
- maturity of the organisation;
- attributes and experience of the organisation's people;
- culture of the organisation and its people;
- regulatory requirements of the industry in which the organisation operates;
- requirements and demands of those to whom the organisation and its board are accountable.

2.2 Alignment of governance standards

The various standards, guidelines and recommendations concerning "good governance" referred to in paragraph 2.1 have much in common with one another, even though the manner in which they may be expressed may differ.

Commonly they are structured around high level principles such as:

- clarity of organisational objectives and purpose;
- accountability and integrity;
- ethical decision making and dealing;
- organisational culture;
- balanced and timely reporting and disclosure;
- structuring and maintaining the board to add value;
- clarity of roles and responsibilities of board and management;
- strategic focus and risk oversight;

- remunerating key management personnel of the organisation in a fair and responsible manner;
- respecting the rights of members of the organisation.

By way of example the ASX Corporate Governance Council Corporate Governance Principles and Recommendations (3rd Edition – 2014) are structured in a 3-tiered manner around:

- 8 high level Principles
- sets of up to 6 more detailed Recommendations aligned to each high level Principle, with each set directed at governance related structures, mechanisms, practices and behaviours which are believed to promote the relevant Principle, and the presence of which should help assure that the relevant Principle will be met;
- an array of other suggestions and commentary (**"**Commentary**"**) for an organisation to consider, aligned to each of the Principles and Recommendations. The Commentary is designed to give context to its associated Principle and Recommendations, and which, if given due regard by the organisation, is believed to further promote the relevant Principle and/or Recommendations.

The structure of the governance standards, guidelines and recommendations of other credible and respected industry associations, NGOs and regulatory authorities (local, national or international) are in many ways usually quite similar:

- a set of high level governance related principles;
- a series of more detailed "break outs" of recommended structures, mechanisms, practices and behaviours to support the principles;
- background commentary to give context to the principles and recommendations.

There is also considerable convergence of approach for these standards, guidelines and recommendations as to what are the primary governance related mechanisms, structural elements, policies, practices and behaviours that are relevant to an organisation when building an effective governance framework. This convergence of approach is also added to by the writings, studies and works of various acknowledged governance academics, commentators and practitioners.

These governance related mechanisms, structural elements, policies, practices and behaviours are often the observable and/or demonstrable elements of an organisation's governance framework which can be measured or assessed as being compliant with or aligned to accepted good governance standards, guidelines and recommendations.

By proxy and traditionally, it is often the degree of alignment of these elements with published governance standards, guidelines and recommendations that is used to form a judgement as to whether or not an organisation's governance is "good" or "effective", even though more contemporary informed academic and other writings on governance support the propositions that:

- governance is more involved than merely the structure and the workings of the board and its directors, and their interface with management and the organisation's stakeholders, although these are important parts of it;
- governance is a complex construct, the effectiveness of which is dependent upon a dynamic and interacting array of organisational systems and human interfaces;
- at board level, aspects of inter-personnel dynamics and a "healthy team" environment are more important drivers of governance effectiveness and organisational performance than structural and other related aspects, although the importance of these other drivers should not be deprecated.

3 Identifying and considering the observable and/or demonstrable elements of governance

3.1 The table below sets out many of the observable and/or demonstrable elements of governance that are commonly found in the published standards, guidelines and recommendations on good or effective governance. They are also often measured or considered when assessing or benchmarking the purported "quality" of an organisation's governance framework and practices against its alignment with published governance standards, guidelines and recommendations.

3.2 The table below addresses matters under the following headings and columns:

- column 1 – the observable and/or demonstrable element of governance commonly found in the published standards, guidelines and recommendations on good or effective governance;
- column 2 – the philosophical beneficial governance outcome sought to be derived by reason of the presence of that element;
- column 3 – examples of actual governance practices commonly deployed by different leading organisations in their fields depending upon their type, nature, circumstances and needs.

#	Observable and/or Demonstrable Element of Governance	Philosophical beneficial governance outcome sought to be achieved	Examples of actual governance practices by leading organisations in their fields depending on the type, nature, circumstances and needs of the organisation
1.	**Board matters**		
1.1	Board size (consensus optimal recommended size of around 8-10)	• Small enough to be flexible, efficient, foster engaged deliberations and facilitate trust • Large enough to discharge the work load and provide diversity of perspective	• Small/mid cap listed – 4 to 7 is common • University boards – 15 to 20(+) is common • Public sector boards – 8 to 12 is common
1.2	Chair/CEO (segregation of office)	• Objectivity and independence of oversight by the Chair as the leader of the board with respect to the performance of management and the CEO as the leader of the management team	• US public listed major/global corporations – around 50% do not ascribe to this • Early start-up companies – commonly do not ascribe to this • Family companies – commonly do not ascribe to this
1.3	Non-executive board members (majority of board members)	• Objectivity of oversight by non-executive board members without risk of bias possibly arising from an executive board member's employment by the organisation	• UK corporations tend to have a higher % of executive directors than do US or AUS corporations (often up to 30-40%) • Early start-up and family companies tend not to ascribe to this • Subsidiary companies generally do not ascribe to this
1.4	Independent board members (majority of board members)	• Objectivity of oversight by independent board members in the best interests of shareholders/members as a whole • Minimise risk of bias possibly arising from a board member (executive or non-executive) having other extraneous interests or duties	• Joint venture and subsidiary companies generally do not ascribe to this • Family companies tend not to ascribe to this • Charitable and community organisation boards are commonly comprised of those with a special interest in the organisation's cause • Public sector organisations often have statutory prescribed representative boards • Co-operatives often have boards comprised of representatives from member geographies or functional interests

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1.5	Level of board engagement (sufficiently engaged)	• Not so passive so as to be "asleep" at the wheel • Sufficiently engaged to perform its governance functions effectively • Not too engaged so as to surpass or unduly intrude upon the role of management and lose objectivity of perspective	• The appropriate level of engagement of a board may vary from time to time including on account of: - corporate crises or special projects arising - change of CEO/senior management - strength and depth of the executive management (sometimes particularly relevant for smaller public companies and NFP organisations with lean management teams)
1.6	"Closed" board sessions (without executives present)	• Opportunity for non-executive board members to converse concerning management's performance and any other board related issues arising without risk of inhibition through executive management personnel being present	• Some organisations factor these into each board meeting • Other boards undertake these on an as needs basis • The culture of some organisations would find this anathema

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2.	**Board Committee Matters**		
2.1	Number and type of Board Committees (commonly to include at least audit, risk, nominations and remuneration functions)	• Certain regulatory standards (e.g. stock exchange or public sector management) may prescribe minimum expected requirements • Designed to assist the board in: - sharing the work load; - focus on key functional areas of operation or governance requirements; - allow more in depth analysis of issues by those board members with relevant experience/skills in the area	• Larger public listed corporations in Australia tend to have all 4 typical board committees • Smaller public listed corporations in Australia often combine the audit/risk and nominations/remuneration functions into 2 committees • US public listed corporations tend not to have a discrete risk committee • Some NFP corporations combine audit/risk as well as "finance" in one committee and then have another more generic "governance" committee • Public sector organisations may not have nominations or remuneration committees if those functions are retained by the relevant Minister or government department
2.2	Board Committee Charters (detailed remit, terms of reference, authority and accountability expectations)	• To ensure clarity of role, responsibility and accountability • To ensure certainty of membership, scope of role and authority • To prescribe reporting channels	• The terms of reference and procedural rules of board committees differ markedly between organisations in the same sector and especially between organisations in different sectors, although clarity of role, responsibility and accountability is a common benchmark being strived for

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2.3	Board Committee composition - appropriate skills/experience - board Chair/audit Chair segregation of roles on Audit Committee - majority of independent directors on most committees - exclusion of executives from membership of Committees with audit, nominations or remuneration functions	• For relevant experience and skills within the board to be deployed to specialist board functions • To segregate board Chair from audit Chair responsibilities to enhance internal audit control • To ensure objectivity and independence of performance of Committee functions • To exclude executives from membership of certain Committees where their membership may give rise to a likely conflict of interest	• The governance elements under this heading are often at best aspirational for many organisations although larger public listed companies certainly conform more closely to these • Many smaller public listed, NFP and public sector organisations may be less assiduous with their adherence to these governance elements • Family companies – tend not to ascribe to this level of governance prescription

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3.	**Board Member Matters**		
3.1	Board member appointments (suitably skilled and experienced board to govern the organisation)	• Transparency of process • Constitutional observance and regulatory compliance • Getting the best team available for the organisation's needs	• Across most sectors, "word of mouth" and "network" based appointments are common, often at the expense of transparency of process and sometimes even at the expense of getting the best skills/experience • Family companies – often do not ascribe to this with a dominant patriarch/matriarch and with familial association paramount • Public sector appointments - political bias in the selection process is not uncommon
3.2	Board skills matrix tool (use of tool and the disclosure of its outcomes)	• To identify skill/experience gaps • To assist in succession planning and professional development initiatives	• Tools and practices such as this are relatively novel in their application to governance so take up is still emerging, with public listed and large NFP organisations taking the lead • Relatively low take up in a formal manner with smaller organisations and with public sector organisations (where Ministerial discretion may be paramount or a representative board is prescribed)
3.3	Board member induction and ongoing professional development (develop and maintain relevant skills and knowledge of board members)	• To ensure relevant industry/business/organisational information uptake and understanding by new board members • To provide professional development opportunities for board members to: - enhance their performance for the organisation's benefit - maintain their "fitness for purpose" in a dynamic and challenging world	• Material focus on practices such as these is relatively novel so take up is still emerging across all sectors • It is more likely that take up of these practices initially will be amongst larger public listed, NFP and public sector organisations

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3.4	Board member tenure: - set terms of staggered renewable appointments - inferred "best before" maximum tenure around 10 years with "independence" status reviewed thereafter	• To ensure board members' terms of appointment are such that periodically they need to stand for re-election to office • Balancing board refreshment principles with the greater depth of organisational understanding and corporate knowledge that comes with longer tenure of office	• For US public listed corporations, appointment and tenure is usually annually (renewable) with an average board tenure of around 8-9 years, with a material percentage of board members' tenure of 12-15 years (plus) • A number of NFP/community based organisations commonly have some very long standing board members with 12-15 years (plus) service • Family companies tend not to ascribe to this • Some public sector organisations actually prescribe maximum aggregate terms of tenure
3.5	Board member removal from office (only by those appointing the board member)	• Transparency of process • Constitutional observance and regulatory compliance • Governance integrity	• In practice, especially where there is a dominant major shareholder or even dominant board Chair, informal pressures for a board member to retire commonly prevail over formal requirements, irrespective of organisational type and sector
3.6	Board member letter of appointment (formalise terms and conditions of appointment)	• To ensure clarity and certainty of the terms of appointment and expectations upon a board member	• Commonly not adhered to with many NFP/community based organisations and smaller commercial and family corporations • Public sector corporations usually nominally adhere to the practice with minimal content as to the terms and conditions of appointment

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4.	**Policies and Codes**		
4.1	Code of Conduct (ethical behaviour standards)	• To promote a culture of integrity and ethical practices • To mitigate against corruption, legal non-compliance, socially abhorrent behaviour and adverse reputational risks	• Generally present in large public listed and NFP organisations • Not as common in smaller commercial and family companies • For public sector corporations, public sector management codes and principles may apply instead of an organisation's own code
4.2	Conflicts of Interest (assurance of prudential protocols and practices)	• To ensure integrity and mitigate against "agency risk" issues • To ensure perceptions of sound probity • To ensure regulatory compliance	• Generally present in larger public listed and NFP organisations • Many other organisations merely rely on statutory and common law requirements rather than having a discrete policy for the organization • Public sector organisations often have specific requirements in their enabling legislation or under public sector management rules rather than having their own discrete policy
4.3	Segregation of roles and responsibilities between board and management (stipulation and disclosure)	• Clarity and accountability of roles and responsibilities • Encouraging boards and management to focus on their own domains of responsibility	• Many smaller commercial and family corporations do not have specific policies on such matters and largely rely on the organisation's constitution and cultural practices • Many public sector organisations merely rely on the statutory or regulatory provisions by which the organisation is established
4.4	Policies concerning dealing in the organisation's securities by directors and officers (restrictions on dealing in the corporation's shares)	• To ensure integrity of share trading without abuse of inside information • To minimise the risk of "insider trading" breaches	• Usually of no or minimal relevance (or adherence) other than for public companies

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4.5	Policies concerning release/disclosure of market price sensitive information (regulatory/legal compliance protocols)	• To ensure equal and timely access by the market to price sensitive information concerning the organisation and its securities	• Usually of no or minimal relevance (or adherence) other than for public companies
4.6	Risk management policy (governance protocols and procedures to address)	• To address the organisation's appetite or tolerance for risk • To assign responsibility for risk management • To ensure identification and management of material risks	• Strongly featured in public companies, large NFP organisation and large public sector organisations, especially those operating in a highly regulated environment (e.g. health, finance, insurance, utilities, work place safety, those with material consumer protection risks) • Less likely to be part of the policy framework for small and family corporations
4.7	Remuneration policy (governance principles, protocols and disclosure requirements)	• To address the organisation's policy concerning remuneration for: - non-executive board members - executive personnel including base and incentive remuneration, STI and LTI, to align the interests of the executive with the organisation • To mitigate against "agency risk" of those in control of the organisation unduly favouring themselves with remuneration • To align executive incentives with desired organisational outcomes	• Strongly featured in public listed companies • Less likely to be part of the policy framework for small and family corporations • Less likely to be part of the policy framework for public sector organisations whose remuneration structures may be prescribed by public sector management rules and authorities
4.8	Diversity policy (initiatives and targets to promote)	• To promote diversity within the organisation and to set measurable objectives to be	• Strongly featured in large public listed companies • Less likely to be part of the policy framework for smaller and family corporations

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		attained (with special focus on gender diversity) • To deliver to the organisation the perceived benefits of diversity in the organisation's personnel at all levels	• Less likely to be part of the policy framework for NFP organisations where diversity is more common in any event or the lack of diversity is more entrenched (e.g. male dominated sporting organisations)
4.9	Communication policy (members and stakeholders)	• To encourage effective communication and engagement with the organisation's members and stakeholders • To promote transparency and accountability of the organisation's governance and affairs	• Strongly featured in public listed companies with heightened investor demand for information and financial performance accountability • Less likely to be part of the policy framework for small and family corporations • Less likely to be part of the policy framework for public sector organisations whose primary formal accountability may only be to the relevant Government Minister, the Parliament or the relevant government department

3.3 As mentioned, column 3 of the above Table includes examples of common governance practices of a range of organisations of differing size, type and nature relative to the elements of the accepted standards, guidelines and recommendations of various industry associations, NGOs, regulatory authorities and governance academics and practitioners. Many of these actual practices deviate materially from the elements of those accepted standards, guidelines and recommendations.

3.4 Yet notwithstanding that deviation there is no substantive evidence to suggest that overall the governance frameworks of these organisations have material shortcomings, or are not suitable in most material respects for those organisations. Nor is there any clear evidence that the organisational performance of these organisations is materially less than would be the case if those suggested governance practices were adopted.

3.5 On the contrary many organisations adopting these divergent governance practices perform exceptionally well, and may even "outperform" organisations which adopt more mainstream and less divergent governance practices – where "performance" is measured against the degree to which the organisation achieves, or moves towards, its organisational goals and objectives.

4 Fitness for Purpose

4.1 Effective governance has been described to be both an "art and a science".

4.2 As a "science", it lends itself to more prescriptive governance related structures, systems, processes and practices that have been proven by others to be "effective". Other organisations can then benchmark their own governance attributes against such structures, systems, processes and practices. Other organisations can then seek to emulate such structures, systems, processes and practices in the hope or expectation of improved "effectiveness" for themselves. Yet even as a science, and as can be seen by the examples in column 3 of the Table in section 3 above, many of the observable and/or demonstrable elements of governance noted in column 1 of the Table do not have universal application even amongst organisations of relatively common type, size and attributes.

4.3 As an "art", the accepted adage "one size does not fit all", as quoted earlier, could never be more apt. The complexity of interplay between the governance "players" (board members, CEO, executive team, management, shareholders/members, regulators, broader stakeholders) and between the organisation and the environment in which it operates (physical, social, financial, and market related), creates an imponderable array of permutations, each with its own unique needs and challenges.

4.4 The Holy Grail of effective governance is to optimise organisational performance and best manage organisational risk consistent with the organisation's goals and objectives. Good or effective governance has been described by some commentators as a "journey" rather than as a "destination". Accepting this description encourages focus on:

- the "now", or where the organisation currently is at;
- the "destination", or where the organisation intends to get to;
- the "journey", or how it is intended to move from the "now" to the "destination", dealing with all the opportunities, risks and circumstances that may be encountered on the way.

4.5 As with most journeys, rarely do they present as a straight-line or serially based equation. In fact the means and ways of getting from the "now" to the "destination" are many and varied.

4.6 Interestingly the etymology of "governance" is from the Latin "gubernare" meaning to steer a ship, and also to keep good order. The analogy of a "gubernator", Latin for one who steers a ship, setting a course to deliver his/her ship, crew and cargo in good stead and in a timely manner to a destination (i.e. the objective of the voyage), and to deal with the perils of the voyage on the way (including winds, currents, tides, storms etc), as well as any regulatory requirements, is compelling.

4.7 What is important in the context of good or effective governance is not with the benefit of hindsight to determine which course set or which tactics deployed proved to be the best in the circumstances which unfolded, but rather at the commencement of the voyage and with foresight judgement which is the most "sound" approach to take given the complexity and importance of the task (or mission) to be undertaken, the resources available (physical, financial, human etc), the regulatory environment and the perils of the voyage that may be encountered.

4.8 That is the key. That is "effective governance" as it addresses the concept of a proactive and forward looking approach to address "fitness for purpose" and positioning of the organisation's governance framework for the intended journey.

5 Conclusion

5.1 Effective governance is the Holy Grail for all organisations in their endeavours to enhance their organisational performance and outcomes, and better manage their organisation's risks in or towards the achievement of their organisation's goals and objectives.

5.2 Although many industry associations, NGOs and regulatory authorities have published standards, guidelines and recommendations for organisations to benchmark their own governance attributes against, there is no prescriptive set of governance elements that will assure an effective governance outcome for any organisation, even one that strictly ascribes to that set of governance elements.

5.3 Although organisations are well advised to be guided by or at least have due regard to, such standards, guidelines and recommendations, and the governance elements identified within them, essentially each organisation needs to "tread its own path" to ensure its governance is "fit for purpose" for its own needs and circumstances and for its own journey towards its goals and objectives.

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