Australian Institute of Company Directors

INDIVIDUAL

Key competencies for directors

The board is responsible for ensuring that it has represented on it the skills, knowledge and experience needed to effectively steer the company forward. Directors will be appointed to the board because their specific skills, knowledge and experience will fill particular gaps on the board. It is important to acknowledge that not all directors will possess each necessary skill, but the board as a whole must possess them.

What are competencies and why are they important?

What is a competency? Kiel et al. define the competencies of a director as being the experience, knowledge, skills, attitudes, values and beliefs of the person.[1] They provide a framework for considering these competencies as follows:

- **Industry:** Experience in and knowledge of the industry in which the organisation operates;
- **Technical:** Technical/professional skills and specialist knowledge to assist with ongoing aspects of the board's role;
- **Governance:** The essential governance knowledge and understanding all directors should possess or develop if they are to be effective board members. Includes some specific technical competencies as applied at board level; and
- **Behavioural:** The attributes and competencies enabling individual board members to use their knowledge and skills to function well as team members and to interact with key stakeholders.

The ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*[2] (ASX Principles) touches on the competencies of directors in a number of recommendations. These recommendations highlight the importance placed on balancing the competencies of directors in publicly listed companies. The same requirements are also desirable for the boards of many unlisted organisations.

1. G Kiel, G Nicholson, J A Tunny and J Beck, 2012, *Directors at Work: A Practical Guide for Boards*, Thomson Reuters Australia, p 203.
2. ASX Corporate Governance Council, 2019, *Corporate Governance Principles and Recommendations*, 4th edition, February, **https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf**, (accessed 8 May 2019).

First, Recommendation 1.2 states that:

> *A listed entity should:*
>
> *(a) undertake appropriate checks before appointing a director or senior executive or putting someone forward for election as a director; and*
>
> *(b) provide security holders with all material information in its possession relevant to a decision on whether or not to elect or re-elect a director.*

In the commentary to this recommendation, the ASX Principles state that this includes, among other items of information on the director "biographical details, including their relevant qualifications and experience and the skills they bring to the board".

Second, Recommendation 1.5 deals with diversity and encourages boards to promote diversity on the board, its committees and throughout the organisation. By having gender, racial, age and other forms of diversity on a board it can be expected that the board will have a wider range of competencies than having too great a focus on any one background.

Third, Recommendation 2.1 encourages boards to have a nomination committee, among whose functions is reporting to the board on "the process for recruiting a new director, including evaluating the balance of skills, knowledge, experience, independence and diversity on the board".

Fourth, Recommendation 2.2 states: "A listed entity should have and disclose a board skills matrix setting out the mix of skills that the board currently has or is looking to achieve in its membership". This recommendation is to ensure that investors and other stakeholders can review the criteria related to the competencies the board sees as important in the selection of directors. The *Corporations Act 2001* (Cth) (the Corporations Act) also has similar disclosure of competencies in mind in the section dealing with annual directors' reports, which apply to public companies. Section 300 (2A) (10) (a) requires the publication in the annual report of "each director's qualifications, experience and special responsibilities".

Finally, Recommendation 2.6 states:

> *A listed entity should have a program for inducting new directors and for periodically reviewing whether there is a need for existing directors to undertake professional development to maintain the skills and knowledge needed to perform their role as directors effectively.*

This recommendation acknowledges that competencies are not static but need to be continually updated.

What competencies should board members have?

There is no absolute list of competencies which apply to all boards. Each board must review its own special requirements. The competencies required will be impacted by factors such as:

- the size of the board;
- the committee structure of the board;
- whether the organisation is for-profit, not-for-profit or a government instrumentality;
- the size, nature and financial position of the company;
- the complexity of operations such as lines of business, geographic spread of operations;
- the shareholder/member structure;
- the competencies of senior management; and
- the risks and challenges of the business.

However, there is one competency that following the *Centro* case[3] it is considered that all directors should have – sound financial and accounting knowledge. This means the ability to read and comprehend the company's accounts, financial material presented to the board, financial reporting requirements and an understanding of corporate finance. In the Centro case, Justice Middleton made the observation that this is a key requirement that a director cannot delegate to other directors, board committee, advisors or management.[4]

3. *ASIC v Healey* (2011) 196 FCR 291; [2011] FCA 717.
4. *ASIC v Healey* (2011) 196 FCR 291; [2011] FCA 717 at 174-175.

Other competencies considered to be important for many boards include:

- **Strategic expertise** – the ability to understand and review the strategy;
- **Legal** – the board's responsibility involves overseeing compliance with numerous laws as well as understanding an individual director's legal duties and responsibilities;
- **Risk management** – experience in managing areas of major risk to the organisation and the use of risk management systems;
- **Managing people and achieving change** – including experience as either a CEO or senior member of a management team in a similar or larger sized organisation;
- **Industry knowledge** – experience in similar industries.

There is also an argument that for some boards people with international governance experience can bring valued insights to the company.[5]

What personal qualities should board members have?

While different directors can bring different technical skills and knowledge to a board, there are personal qualities that are desirable in all directors:

- **Integrity** – fulfilling a director's duties and responsibilities, putting the organisation's interests before personal interests, acting ethically;
- **Curiosity and courage** – a director must have the curiosity to ask questions and the courage to persist in asking or to challenge management and fellow board members where necessary;
- **Interpersonal skills** – a director must work well in a group, listen well, be tactful but able to communicate their point of view frankly;
- **Genuine interest** in the organisation and its business;
- **Instinct** – good business instincts and acumen, ability to get to the crux of the issue quickly;
- **An active contributor** – there is no room on boards today for those who do not contribute.

Commentators also suggest that directors must ensure they have adequate time to devote to the organisation's affairs.

Are there any special requirements for APRA-regulated entities?

The prudential standards of the Australian Prudential Regulation Authority (APRA) outline special requirements of directors of its regulated entities, such as banks, building societies, insurance companies and superannuation funds. There are 'fit and proper' standards relating to responsible persons who are the directors and senior management of these entities. To be accepted as 'fit and proper', a director must have the necessary skills, knowledge, experience, diligence and soundness of judgment to undertake the duties of the role.

People who have been unwilling to comply with legal obligations, have breached fiduciary duties, been negligent or deceitful, have been disciplined, disqualified or subject to an enforcement action by a professional or regulatory body regarding honesty and integrity, have been 'substantially involved' in a business failure or held in bad repute in a business community are deemed to not be 'fit and proper'. APRA expects an annual review of a person's fitness and propriety. See, for example, Prudential Standard CPS 520 Fit and Proper (September 2018).

Are there any special requirements for ASX-listed entities?

In 2012, the Australian Securities Exchange (ASX) instituted a fit and proper test for all directors of a company seeking admission to the exchange. Listing Rule 1.1 Condition 20 states that "The Entity must satisfy ASX that each director or proposed director of the entity at the date of listing is of good fame and character".[6]

Further, ASX Operating Rules Guidance Note 1 elaborates the requirements for any organisation which is not an authorised deposit-taking institution (ADI) or does not

5. T Featherstone, 2019, "Why international directors will benefit your board", *Company Director*, AICD, **http://aicd.companydirectors.com.au/membership/company-director-magazine/2019-back-editions/february/global-directors**, (accessed 12 April 2019).
6. ASX Listing Rule 1, https://www.asx.com.au/documents/rules/Chapter01.pdf, accessed 12 April 2019

hold an Australian Financial Services Licence concerning the fit and proper test for directors:

> *... in all other cases, it must provide statutory declarations to ASX in relation to itself and from each of its directors confirming that:*
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> - *they have not been the subject of any previous bankruptcy, insolvency, receivership, administration, or similar event;*
> - *they have not been charged with or convicted of any offences relating to dishonesty, fraud, financial markets-related conduct, or money laundering;*
> - *they have not been the subject of any fines, civil penalties, banning, suspension or other disciplinary measures for financial markets-related conduct;*
> - *they have not been the subject of any disciplinary action or adverse mention in a report made by, or at the request of, any government or governmental authority or agency, the Commission, ASX, an approved clearing facility, an approved settlement facility, and any other exchange, market operator or clearing and/or settlement facility;*
> - *they have not been refused membership of any financial markets-related, legal or accounting professional organisation or had such a membership revoked; and*
> - *they have not had an application for participant status (or equivalent status) on another exchange, market, approved clearing facility or approved settlement facility refused,*
>
> *whether in Australia or elsewhere and that they are not aware of any open or pending investigations or threatened proceedings that could lead to any of the above.*[7]

Are there any special requirements for ACNC registered entities?

The Australian Charities and Not-for-profits Commission (ACNC) requires charities to meet Governance Standards. Under Governance Standard 4, charities must make sure its 'responsible persons' are suitable. This means that charities must take reasonable steps to be satisfied that its directors or committee members are not disqualified from:

- managing a corporation under the Corporations Act; or
- being a responsible person by the ACNC Commissioner, within the previous 12 months.

7. ASX Operating Rules Guidance Note 1 (January 2019), p 9, **https://www.asx.com.au/regulation/rules/asx-operating-rules.htm**, (accessed 12 April 2019).

About us

The Australian Institute of Company Directors (AICD) is committed to strengthening society through world-class governance. We aim to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. Our membership includes directors and senior leaders from business, government and the not-for-profit (NFP) sectors.

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