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**Commercial Policy Framework:
Guidelines for Boards of Government Businesses**

OFFICE OF FINANCIAL MANAGEMENT

Policy & Guidelines Paper

Preface

The *Commercial Policy Framework* is a suite of policies that seeks to replicate within NSW government businesses appropriate disciplines and incentives that lead private sector businesses towards efficient commercial practices.

The purpose of these *Guidelines for Boards of Government Businesses* is to outline the key private sector standards of corporate governance which are most appropriate to the practices and procedures for boards of government businesses.

These Guidelines are aimed at government businesses (and their subsidiaries) with a governing board. Some principles may also be relevant for advisory boards.

This publication includes recent amendments to the *State Owned Corporations Act (NSW) 1989* and replaces the first edition of this publication issued in November 2007 (TPP07-8). An updated edition will be issued in response to any future changes to the Act.

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Note

General inquiries concerning this document should be initially directed to the Commercial Policy Branch (Tel: 9228 5813) of Treasury.

This publication can be accessed from the Treasury's Office of Financial Management Internet site [<http://www.treasury.nsw.gov.au/>].

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Executive Summary

These Guidelines regarding the practices and procedures of boards of government businesses are based on applying private sector standards in the context of government ownership. As a guide to optimising board performance and accountability, they should be applied taking into account the specific circumstances of the government business rather than as a tightly prescriptive set of rules.

These Guidelines are primarily aimed at governing boards but many principles outlined may also be applicable to advisory boards. Advisory boards are encouraged to consider the extent to which they should adopt the recommendations in this paper, given their specific circumstances.

The recommendations contained in the executive summary are not mandatory, however, where a governing board of a government business considers that a recommendation is inappropriate to its particular circumstances, the government business has the option of not adopting it, but must explain why in its annual report.¹ This is consistent with the requirement imposed on Australian listed companies to disclose the extent to which they have followed the recommendations set by the Australian Stock Exchange (ASX) in the reporting period².

The ASX recommends a three step method for effective “if not, why not” reporting:

- Identify the Recommendations the business has not followed.
- Explain why the business has not followed the Recommendations.
- Explain how its practices are consistent with the “spirit” of the relevant section of the Guidelines to demonstrate that the business understands the relevant issues and has considered the impact of its alternative approach³.

Recommendations for corporate governance for boards:

- Boards should develop, comply with and publish a charter setting out roles, powers and responsibilities of the board, identifying key stakeholders and the board’s responsibilities to each stakeholder. The charter should complement any legislative charter and should be regularly reviewed.
- Boards should develop and comply with a board code of conduct to ensure integrity and accountability. The board should publish the code of conduct or a summary on the corporate governance section of the website.
- The board should require management to report to it on its design and implementation of risk management and internal control systems. The board should require management to report whether material business risks are being managed effectively and the board should disclose whether such a report has been provided.

¹ It is recognised that some recommendations may be more a matter for shareholding ministers than the board, for example, limiting the number of directorships to no more than three government boards. However, this does not preclude businesses from disclosing departures from the recommendations in their annual report.

² ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 5

³ *Ibid*, p. 7

- Boards should form an audit committee and if a State Owned Corporation (SOC), a remuneration committee if relevant and applicable. Businesses without committees should have board processes in place to consider issues that would otherwise be addressed by a committee.
- Where possible, boards should follow the experience and composition recommendations for committees outlined in section 2.3.
- The audit and remuneration committees should have charters.
- The chair of the board should be independent.
- The roles of the chair and the chief executive officer (CEO) should not be exercised by the same individual and the CEO should not go on to become chair of the same business.
- Businesses should recognise and disclose the functions reserved to the board and those delegated to senior executives.
- Where possible, the majority of the board should be independent.
- In relation to related interests:
 - Directors are to disclose to Treasury any interests or changes in interest in relation to the business or the board position where the director may receive, or appear to receive, any benefits (besides the payment of director's remuneration).
 - For individual decisions being made by the board, directors must disclose any interests in relation to any individual matter being considered by the board and, unless approved otherwise by the board as not being a conflict, must not vote in relation to the matter or be present while the board considers the matter.
- Directors should not hold directorships of more than three government boards.
- Directors should be provided with sufficient information upon appointment in order to clearly understand the expectations of their role.
- Induction and continuing education should be provided to directors to enhance their understanding of the role of boards of government businesses, corporate governance generally and government policy developments.
- There should be regular performance evaluation of the board, committees and individual directors. The board must disclose whether performance evaluation has been conducted and how in the annual report.

1. Introduction

1.1 Background

The *Guidelines for Boards of Government Businesses* are a component of the NSW Government's *Commercial Policy Framework*. The Framework aims to replicate within government businesses the appropriate disciplines and incentives that lead private sector businesses towards efficient commercial practices. This includes corporate governance standards relating to the procedures and practices of boards of government businesses.

The term corporate governance refers to "the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations"⁴. For SOCs, the board of directors is charged with governance of the entity⁵.

The principles of good corporate governance can also be relevant to government businesses that are not SOCs. Non-corporatised businesses may also have an advisory board.

The function of a board will depend upon whether it is an advisory board or a governing board.

An advisory board provides expert advice to the shareholding ministers⁶ and senior executives of the business but generally does not have decision-making power over the business.

A governing board is empowered to govern the management of the organisation and plays a critical role in setting the strategic and operational direction of a business and in appointing the chief executive officer or managing director. Governing boards have absolute responsibility for the performance of the SOC and must ensure that SOCs are managed in the best interests of the shareholding ministers.

At common law, directors are obliged to act in the interests of the company as a whole⁷. This phrase has been interpreted to mean the "financial well-being of the shareholders as a general body."⁸ This principle is applicable to government businesses and boards are fully accountable to the shareholding ministers.

⁴ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 3

⁵ Under section 20L of the *State Owned Corporations Act 1989*, all decisions relating to the operation of a statutory SOC are to be made by or under the authority of the board.

⁶ For the purpose of these Guidelines, shareholding ministers are defined as:

- for State Owned Corporations, the voting shareholders
- for other government businesses, the Treasurer and the portfolio minister.

⁷ Similarly, the *Corporations Act (Cth) 2001* requires that directors "must exercise their powers and discharge their duties in good faith in the best interests of the corporation". SOCs are however governed by the *State Owned Corporations Act 1989* rather than the *Corporations Act 2001*.

⁸ Corporations and Markets Advisory Committee, *The social responsibility of corporations*, December 2006, p. 84

These Guidelines complement other government guidelines relating to boards⁹ of government agencies with additional guidance specifically for boards of government businesses. The Guidelines largely mirror standards that are recommended for private sector businesses to minimise risks concerning corporate governance and optimise performance and accountability of boards.

The recommendations in these Guidelines are not mandatory and an “if not, why not” approach has been adopted, mirroring private sector standards with the emphasis on disclosure rather than prescription.

1.2 Application

These Guidelines apply to the boards of government businesses covered by the *Commercial Policy Framework*. They are primarily aimed at governing boards but many principles outlined may also be applicable to advisory boards. Advisory boards are encouraged to consider the extent to which they should adopt the recommendations in this paper, given their specific circumstances.

Government businesses for the purpose of this policy are:

- Public Trading Enterprises (or Public Non-Financial Corporations under ABS classifications). State Owned Corporations (SOCs) are included in this classification, and are distinguished by their corporatised status.
- Public Financial Enterprises (or Public Financial Corporations under ABS classifications).
- General Government businesses (or General Government agencies under ABS classifications) which are also non-Budget dependent and to which the *Commercial Policy Framework* applies.

1.3 Relationship to Other Policies within the Commercial Policy Framework

CEO Contract Guidelines for Government Businesses¹⁰

These Guidelines provide guidance to governing boards in relation to the appointment and contractual terms, including remuneration, for CEOs or managing directors not covered under the *Public Sector Employment and Management Act (NSW) 2002*, primarily SOCs. The Guidelines include a model termination clause and suggested contractual provisions for performance agreements and performance payments.

State Owned Corporations Indemnity Policy¹¹

The *State Owned Corporations Act 1989* permits statutory SOCs to indemnify their officers only with voting shareholder approval. The Policy contains a pro forma Deed of Indemnity which provides an indemnity to directors against certain liabilities incurred in the course of their duties where conduct is not held to involve a lack of good faith, gross negligence or recklessness. This gives directors appropriate protection against risks related to diligent performance of duties.

⁹ For example:

- Department of Premier and Cabinet, *Boards and Committees Handbook Template*
- Department of Premier and Cabinet, *Conduct Guidelines for Members of NSW Government Boards and Committees*, Version 2, April 2008
- Department of Premier and Cabinet, *An Introduction to Board and Committee Membership*, Version 2, April 2008
- Department of Premier and Cabinet, *Guidelines for NSW Board and Committee Members: Appointment and Remuneration*, October 2004

¹⁰ NSW Treasury, *CEO Contract Guidelines for Government Businesses*, TPP 06-1, January 2006

¹¹ NSW Treasury, *State Owned Corporations Indemnity Policy*, TPP 03-6, October 2003

Reporting and Monitoring Policy¹²

The monitoring and accountability regime for government businesses is an important backdrop for these Guidelines.

The regime requires an annual agreement between the senior executives, board and shareholding ministers known as the Statement of Corporate Intent (SCI) for a SOC, or a Statement of Business Intent (SBI) for non-SOC government businesses. The SCI/SBI sets out performance objectives and targets for the business, taking into account the strategic concerns and preferences of the shareholding ministers. Where the business has a board, the SCI/SBI must be signed by the chair on behalf of the board. As well as providing certainty as to the expectations of the business' performance, the SCI and SBI contain certain representations from the board to the shareholders.

The regime also provides guidance to government businesses on how to comply with their continuous disclosure requirements.

As government businesses are required to apply all applicable policies under the *Commercial Policy Framework*, other policies which are relevant to board members include:

- *Financial Distribution Policy for Government Businesses*¹³
- *Capital Structure Policy for Government Businesses*¹⁴
- *Government Guarantee Fee Policy for Government Businesses*¹⁵;
- *Treasury Management Policy*¹⁶
- *Tax Equivalent Regime for Government Businesses*¹⁷ and the *Manual for the National Tax Equivalent Regime*¹⁸
- *Social Program Policy for NSW GTEs*¹⁹
- *Guidelines for Assessment of Projects of State Significance*²⁰.

¹² NSW Treasury, *Reporting and Monitoring Policy*, TPP 05-2, November 2005

¹³ NSW Treasury, *Financial Distribution Policy for Government Businesses*, TPP 02-3, June 2002

¹⁴ NSW Treasury, *Capital Structure Policy for Government Businesses*, TPP 02-7, September 2002

¹⁵ NSW Treasury, *Government Guarantee Fee Policy for Government Businesses*, TPP 04-2, July 2004.

¹⁶ NSW Treasury, *Treasury Management Policy*, TPP 07-7, July 2007

¹⁷ NSW Treasury, *Tax Equivalent Regime for Government Businesses*, TPP 03-4, June 2003

¹⁸ Australian Taxation Office, *Manual for the National Tax Equivalent Regime*, Version 5, January 2006

¹⁹ NSW Treasury, *Social Program Policy for NSW GTEs*, July 1994

²⁰ NSW Treasury, *Guidelines for Assessment of Projects of State Significance*, TPP 02-4, June 2002

2. Recommendations

2.1 The Board Charter

Each board should have a board charter which:

- Outlines the roles, powers and specific responsibilities of the board.
- Details the key stakeholders, such as the voting shareholders and/or the Treasurer, the portfolio minister, Treasury, regulators, employees, customers and the general community and the board's responsibility towards each.
- Outlines board operations such as conduct of meetings, committees and assessment of board performance including appropriate procedures for resolving and recording concerns by individual directors.

The charter should be written by the board in consultation with the shareholding ministers, the portfolio minister (if not a shareholding minister) and Treasury and should complement any board charter that exists under legislation. For SOCs, this includes the *Constitution and Procedures of Board* contained in schedule 8 of the *State Owned Corporations Act 1989*.

For a governing board of a government business, responsibilities of the board for inclusion in the charter are generally²¹:

- Overseeing the business, including the control and accountability systems.
- Setting the business' strategic aims and ensuring that its obligations to the government and other relevant stakeholders are met.
- Appointing and removing the CEO (or equivalent), in some cases requiring ministerial consultation or approval.
- Where appropriate, ratifying the appointment and removal of senior executives.
- Providing input into and final approval of the senior executives' development of the SCI or SBI, including the performance objectives, and the underlying corporate strategy.
- Reviewing and endorsing risk management and internal control systems, conduct guidelines and legal compliance.
- Monitoring performance of senior executives' and strategy implementation.
- Ensuring senior executives have access to appropriate resources.
- Approving and reviewing the progress of major capital expenditure, capital management, and acquisitions and divestitures.
- Approving and monitoring financial and other reporting, including provision of information to the government under the *Reporting and Monitoring Policy for Government Businesses*.
- Generally ensuring compliance with relevant government policies.

²¹ These responsibilities are based on the suggested board responsibilities for private sector organisations. Refer to ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 13

The charter should be periodically reviewed by the board to ensure it remains relevant and up to date with developments within the organisation and general corporate governance. The charter should be made publicly available, preferably by making it available on the business' website in a clearly marked corporate governance section.

2.2 Code of Conduct

In addition to a board charter, boards should develop and comply with a code of conduct. The code of conduct for the board may be the same as for senior executives and/or may be part of the government business' code of conduct. The code of conduct or a summary should be made publicly available, ideally by posting it to the business' website in a clearly marked corporate governance section.

*Conduct Guidelines for Members of NSW Government Board and Committees*²² applies to all non-SOC government boards and committees. They require each board to have a code of conduct and include guidance on conduct relating to personal and professional behaviour, accountability, gifts and benefits, managing conflicts of interest and reporting suspect corrupt behaviour. This document is linked with a Model Code of Conduct²³. As a statement of good practice, SOCs are recommended to follow the *Conduct Guidelines for Members of NSW Government Board and Committees*.

In any case, the Code of Conduct applicable to the board should cover the following minimal areas:

- commitment by the board and senior executives (if applicable) to the code of conduct
- responsibilities to shareholders and the financial community
- responsibilities to employees, customers, suppliers, creditors, consumers and the broader community
- approach to the community
- responsibilities to the individual
- the corporation's employment practices
- the corporation's policies on business courtesies, bribes, facilitation payments, inducements and commissions
- compliance with legislation
- conflicts of interest and misuse of position
- reporting of unlawful, corrupt or unethical behaviour and the promotion of ethical behaviour
- how the business monitors compliance with the code²⁴.

For SOCs, schedule 10 of the *State Owned Corporations Act 1989* contains minimum legislative directors' duties such as disclosure of conflicts of interests and abstaining from voting where such interests exist, acting honestly, performing duties with care and diligence and not making improper use of information or use of the position of board member²⁵. Schedule 10 also details liabilities for contravention of these duties.

²² Department of Premier and Cabinet, *Conduct Guidelines for Members of NSW Government Boards and Committees*, Version 2, April 2008

²³ Premier's Department NSW, *A Model Code of Conduct for NSW public agencies: Policy and Guidelines*, 1997

²⁴ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 22

²⁵ See sections 1 to 4 and section 7 of schedule 10 which should be read in conjunction with section 33A

2.3 Board Committees

Board committees increasingly have an important role to play in the governance of corporations. It is in committees that independent directors can exercise oversight of the board²⁶. Board committees enable detailed analysis by a sub-group of directors of important matters to report to the board. They can be especially important where specific skills are required to undertake detailed review of specialised areas such as an audit committee to review issues relating to areas of finance and risk. The use of a board committee, however, does not impinge on the responsibilities of the board as a whole in that specific area. Committees should have a written charter outlining their key purpose and procedures and their performance should be periodically reviewed by the board.

At a minimum, governing boards should establish an audit committee and, if a SOC, a remuneration committee²⁷ if relevant and applicable. For smaller boards, the same benefits may not be derived from a formal committee structure. Companies without board committees should have board processes in place which consider the issues that would otherwise be considered by the committee.

Audit and Risk Management

Risk / Audit Committee

Businesses should develop a sound system of risk oversight and management and internal control. The board is responsible for regularly reviewing the business' policies on risk oversight and management and satisfying itself that management has created and put into practice a good system of risk management and internal control. The *Treasury Management Policy* or *Risk Management and Internal Control*²⁸ provide further guidance.

The board should require management to report to it on whether material business risks are being managed effectively and the board should disclose whether such a report has been provided. The board may find it appropriate to make additional enquiries and to request assurances regarding the management of material business risks.

A risk management or audit committee may be an appropriate way to focus the business on appropriate risk oversight, risk management and internal control. The audit committee can also be an effective way of focussing on issues relevant to the integrity of the business' financial reporting and their related controls and procedures including compliance with legal and regulatory requirements, assessing internal audit functions and assisting with external auditing.²⁹ Whether or not a separate audit committee exists, ultimate responsibility for the integrity of financial reporting rests with the board.

²⁶ Independent Audit Limited (UK), *Better Corporate Governance Reporting – A practical framework*, January 2006, page 7

²⁷ This is unnecessary for non-SOC government businesses as executives are remunerated under the *Public Sector Employment and Management Act 2002*

²⁸ NSW Treasury, *Risk Management and Internal Control: Guidelines and Strategies for Improvement*, TPP97-3.

²⁹ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 25

Members of the audit committee should be financially literate (that is, can read and understand financial statements); and where possible at least one member should have relevant qualifications and experience (that is, a qualified accountant or other finance professional with experience of financial and accounting matters); and some members should have an understanding of the industry in which the entity operates. To the extent possible, the audit committee should consist only of non-executive directors, a majority of independent directors, be chaired by an independent chair that is not chair of the board and have at least three members.³⁰ The audit committee should have a charter and this should be made available on the business' website.

Remuneration Committee

The remuneration committee determines the remuneration, recruitment, retention, superannuation and termination policies and procedures for senior executives of the business, including, if applicable, the amount of performance payments³¹. The remuneration committee should ensure that reward is linked to strategic performance. When setting the level and structure of remuneration, the business must balance the competing interests of attracting and retaining senior executives against not paying excessive remuneration. In the annual report, the remuneration committee should disclose what it did during the year to provide oversight of remuneration policy³².

Where possible, the committee should consist of a majority of independent directors, be chaired by an independent director and have at least three members.³³ This committee should take into account decisions made by the Statutory and Other Offices Remuneration Tribunal (SOORT) and any other relevant available benchmarks when determining appropriate remuneration for executives. The remuneration committee should develop a charter setting out its roles and responsibilities, composition, structure and membership requirements and the procedures for when non committee members attend meetings. A summary of the charter or the charter itself, including the roles, rights and responsibilities and membership requirements of that committee should be published in the corporate governance section of the business' website.

³⁰ For further guidance on the establishment, composition and operations of Audit Committees refer "*Compliance Review of the Operations of Audit Committees*", Auditor-General's 2002 Report to Parliament, Volume 3 and ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 25

³¹ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 35. Refer NSW Treasury, *CEO Contract Guidelines for Government Businesses*, TPP 06-1, January 2006, for principles on determining the level of remuneration for the CEO

³² Independent Audit Limited (UK), *Better Corporate Governance Reporting – A practical framework*, January 2006, page 7

³³ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 35

2.4 Board Membership, Independence and Conflicts of Interest

Depending on applicable legislation or founding documentation of the government business, government boards may have certain membership requirements such as having the CEO on the board, a Unions NSW nominee, a staff director or other reserved board positions. Appendix 1 contains summary details for the board composition of SOCs.

Chair

The chair is responsible for leadership of the board and for the effective organisation and conduct of the board's functioning. The chair should facilitate the contribution of all directors and promote productive and respectful relations between directors and between board and management. The chair should commit the time necessary to discharge the role effectively, and regularly review the time commitment required of all directorships. Although these Guidelines do not prescribe a maximum number of chairmanships that an individual may hold, the chair's other positions should not be such that they are likely to hinder effective performance in the role³⁴. The chair should also be an independent director (see below).

Executive Directors

For many SOCs, the CEO is on the board either under the enabling legislation or because he or she has been separately appointed. The responsibilities of chair and the CEO should not be exercised by the same person. The breakdown of responsibilities between the chair and the CEO should be agreed by the board and set out in a statement of position or authority. The chair should not be subsequently appointed as CEO of the same business. A former CEO should not be considered an independent director unless there has been a period of three years between ending that employment and serving on the board.³⁵ Executive directors are not considered to be independent.

Reserved board positions

The annual report should clearly identify board members filling reserved positions such as a staff director, Unions NSW nominee or other ex officio members from other bodies.³⁶

Independent decision making

All directors should exercise independent judgement when making board decisions.

To facilitate this there should be an agreed process for directors to access in appropriate circumstances independent professional advice at the business' expense. A statement as to whether there is a procedure agreed by the board for directors to take such advice should be included in the corporate governance section of the annual report.³⁷

Non-executive directors should consider the benefits of meeting without senior executives present.

³⁴ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 17

³⁵ *Ibid*, p. 17

³⁶ Refer Appendix 1 for a list of SOCs who have a Unions NSW Nominee or a staff director. As an example for non-SOCs, the board of NSW Treasury Corporation includes two ex-officio Treasury officers as per the *Treasury Corporation Act (NSW) 1983*, section 4A

³⁷ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 16

Independent Directors

A director is considered independent if he or she is independent in character and judgement and there are no relationships or circumstances which could materially interfere with, or appear to materially interfere with, the exercise of the independent exercise of their judgement³⁸. An independent director is a non-executive director (i.e. is not a senior executive). Relationships which may impact a director's independent status include where a director:

- Is employed, or has been employed in a senior management position by the business, and there has not been a period of at least three years between ceasing that employment and serving on the board.
- Has within the last three years been a principal of a material professional adviser or consultant to the business, or an employee materially associated with the service provided.
- Is a material supplier or customer of the business, or an officer of or otherwise associated directly or indirectly with a material supplier or customer.
- Has a material contractual relationship with the business other than as a director of the business³⁹.

Directors should disclose to the board family relationships and cross ties which may impact on independence. The majority of the board should be independent directors. Directors who have been appointed under legislation as nominees by external bodies or ex officio members cannot be considered "independent directors".

Directors who the board considers to be independent should be identified in the corporate governance section of the annual report. The board should disclose why it considers a director to be independent particularly where the relationships listed above exist. Materiality thresholds should also be disclosed, both from the perspective of the business and its directors.

Regular assessments

The board should regularly assess whether each non-executive director is independent. Directors should provide to the board all relevant information that is required to make the assessment.

If a director's independent status changes, this should be disclosed and explained to the shareholders in a timely fashion.⁴⁰

Conflict of interest

Directors are required to disclose to the business and to its shareholders, represented by Treasury, any interests in relation to the business or the board position and any changes to these interests where the director may receive, or appear to receive, any benefits (besides the payment of director's remuneration). This includes where interests exist directly, or due to personal ties or business interests.

³⁸ Department of Trade and Industry UK, *Review of the Role and Effectiveness of Non-executive Directors*, ('the Higgs Report') at page 37, ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 16

³⁹ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 17

⁴⁰ *Ibid*, p. 17

Government businesses are required to maintain a register of conflicts of interest, including membership of other boards. Treasury may periodically request access to the register. Directors are expected to ensure that there is no conflict between the membership of the government board and other non-government boards. After initial disclosures are made upon appointment, board members should update this as soon as practicable for any new significant interests or significant changes to existing interests and at least once a year for minor changes or new interests.

For individual decisions being made by the board, directors must disclose to the board any interests in relation to any matter being considered. Unless the board passes a resolution that the interest does not disqualify the director, the director must not vote on or in relation to the matter or be present or otherwise take part while the board considers the matter⁴¹. The board should not pass a resolution allowing the director to vote, unless it is satisfied that the interest does not represent a conflict which could materially affect or appear to materially affect the judgment of the director. A precise definition of when such a conflict exists should be clearly stated in writing in the board's code of conduct.

Details of any transactions between the government business and the director or a director-related entity should be disclosed in the annual report as a related party disclosure.

Other board memberships

Directors should not hold directorships of more than three government boards, and should inform the chair before accepting new appointments. Any changes to membership of other non-government boards should be disclosed to Treasury. As long as there is no conflict, family companies and not-for profit chairmanships and board memberships are excluded from these limitations.

Access to information

The board should be provided with the information it requires to effectively discharge its responsibilities.

Senior executives should supply the board with information in a form and timeframe, and of a quality that enables the board to discharge its duties effectively. Directors should be able to request additional information where they consider such information necessary to make informed decisions.⁴²

Corporate Secretary

The corporate secretary plays an important role in ensuring that board policy and procedures are followed, and coordinating the completion and despatch of agenda and briefing materials.

All directors should have access to the corporate secretary.

The corporate secretary's appointment and removal should be decided by the full board.

The corporate secretary should be accountable to the board, through the chair, on all governance matters⁴³.

⁴¹ See schedule 10, *State Owned Corporations Act 1989*, sections 1 and 2

⁴² ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 19

⁴³ *Ibid*, p. 20

2.5 Information for Directors upon Appointment

The content and quality of information provided to directors is fundamental to the quality of corporate governance. To enable directors to clearly understand the expectations and requirements of the board, directors should ensure that on appointment, they obtain the following:

- the letter of appointment specifying the term of the appointment and the level of remuneration (see below)
- a deed of indemnity, if a SOC
- a copy of the enabling legislation of the government business
- a copy of either the *State Owned Corporations Act 1989*, if a SOC; or the *Public Sector Employment and Management Act 2002* if not a SOC
- a list of fellow directors and the chair
- a copy of the business' constitution
- a copy of the board's code of conduct
- copies of the board's and committee's charters
- a copy of the most recent business plan and related SCI or SBI
- a set of applicable policies under the *Commercial Policy Framework*
- the board and committee meeting schedule
- the most recent annual report
- organisation charts
- statutory history of the business
- meeting minutes and/or papers from the previous board meeting.

The templates in the *Board and Committee Handbook*⁴⁴ contain further guidance on information which board members may find useful both at induction and as an ongoing reference.

Remuneration

For SOCs, remuneration for directors is determined by the voting shareholders⁴⁵. The voting shareholders generally review director remuneration levels each year and may consider recommendations from SOORT. SOORT annually reviews and recommends remuneration levels for the chair, directors and committee positions for each individual SOC. The SOORT review takes into account factors such as the size of the business (as measured by assets, revenues, profit and number of employees) as well as other relevant considerations, including factors identified by Treasury.

SOORT also recommends fee increases for all non-SOC boards, with the Premier retaining the power to approve, reject or vary requests.

It should be noted that for all government businesses, CEOs and other public sector employees who also sit on the board should not receive the remuneration payable to non-executive board members (that is, they should not be "double dipping")⁴⁶.

⁴⁴ Department of Premier and Cabinet, *Boards and Committees Handbook Template*

⁴⁵ *State Owned Corporations Act 1989*, schedule 8, clause 6

⁴⁶ Department of Premier and Cabinet, *Guidelines for NSW Board and Committee Members: Appointment and Remuneration*, October 2004, at section 2.3. This section of the Guidelines applies to all employees of NSW public service departments, statutory bodies outside the public service and State Owned Corporations. Also refer NSW Treasury, *CEO Contract Guidelines for Government Businesses*, TPP 06-1, January 2006

2.6 Induction and Continuous Education

Newly appointed directors should undergo an induction program to allow them to engage in decision-making at the earliest opportunity. To be effective new directors should have a good understanding of the business and its industry. An induction program should be available to enable directors to gain an understanding of the:

- business' financial, strategic, operational and risk management positions and policies
- rights, duties and responsibilities of directors and senior executives
- roles and responsibilities of senior executives
- role of board committees.

All directors should undertake relevant continuous education programs during their tenure, either in-house or through external consultants and should include education concerning key developments in the business and in the industry and environment within which it operates.⁴⁷ Directors may wish to disclose in the annual report the training they have undertaken during the year.

Both induction and on-going education should include sessions on developments in corporate governance, ethics and government policy. Input by Treasury in relation to government policies and applying commercial principles in the context of government ownership is highly recommended. On request, the Commercial Policy Branch of Treasury may assist in helping to organise relevant material.

2.7 Performance Evaluation

All boards and board members should have their performance evaluated regularly against appropriate measures.⁴⁸ Conducted properly, board evaluations can contribute to performance improvements at organisational, board and individual director levels. Boards who perform regular performance evaluations find improvements at these levels in terms of improved leadership, increased clarity of roles and responsibilities, improved teamwork, greater accountability, better decision making, improved communication and more efficient board operations.⁴⁹

It is recognised that performance evaluation is not a one size fits all approach. Boards differ in the severity of their potential performance problems, their competitive environment and the range of performance problems they face. Accordingly, board evaluations can vary in terms of their range, difficulty and cost.⁵⁰ Types of performance evaluation include self assessment, peer evaluation and external evaluation.

For non-SOCs, individual evaluation is a matter for the portfolio minister but Treasury will monitor the board's overall performance through the SBI process. Self evaluations should also be performed on an annual basis.

⁴⁷ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd Edition, August 2007, p. 19

⁴⁸ *Ibid*, p. 19

⁴⁹ Kiel, Geoffrey C and Nicholson, Gavin J (2005) "Evaluating Boards and Directors", *Corporate Governance: An International Review* 13(5) p. 8

⁵⁰ *Ibid*, p. 8

For SOCs, the method of performance evaluation should be determined by the board. Evaluation should be performed on a regular basis, i.e. at least annually. Treasury also reserves the right to “audit” the performance of boards, by appointing an external consultant to make an assessment of the board’s operations.

The following framework suggested by Kiel and Nicholson may be useful for boards in determining the most appropriate method of performance evaluation:

- what are the objectives of the evaluation
- who will be evaluated
- what will be evaluated
- who will be asked
- what techniques will be used
- who will perform the evaluation
- what will be done with the results⁵¹.

Performance evaluation has two components: the performance of the board as a whole and the performance of individual directors.

The following provides guidance as to what individual performance evaluation may be based on:

- attendance at and contributions to board meetings and committees
- attendance at training sessions
- stakeholder feedback including, where relevant, the portfolio minister
- willingness to question, probe and challenge senior executives as appropriate.

The board’s overall performance should be evaluated using the following indicators based on targets and objectives outlined in the SCI/SBI where applicable:

- alignment of the business’ strategic direction with objectives set by the government
- management of senior executives
- short term and long term financial results of the business
- achievement of non-financial objectives such as reform milestones and service delivery levels
- management of risk and compliance issues
- adherence to corporate governance standards including promoting and adhering to the board charter and code of conduct
- adherence to government policies including those within the *Commercial Policy Framework*
- stakeholder feedback including, where relevant, the portfolio minister.

The board should disclose the process for evaluating the performance of the board, its committees and its directors in the annual report.

⁵¹ Kiel, Geoffrey C and Nicholson, Gavin J (2005) “Evaluating Boards and Directors”, *Corporate Governance: An International Review* 13(5) p. 41

3. Annual Report Disclosure

Disclosures related to boards required under legislation include⁵²:

- *Annual Report*
 - names, title and appropriate qualification of directors
 - method and term of appointment of directors (including whether they hold a reserved position – refer section 2.4)
 - frequency of meetings of the board and attendance by directors
 - the names of significant board committees, their function and membership.
- *Financial Statements*⁵³
 - emoluments or other benefits paid to directors (excluding amounts paid to full-time directors)
 - a description and amount of any loans, advances or other moneys made to directors or related parties to directors, but not including loans, advances or money otherwise due for the purpose of carrying out official duties, such as travelling allowances and the like⁵⁴.

In addition to the legislative requirements, the annual report should disclose:

- Any recommendations in the executive summary of these Guidelines that have not been followed and an explanation as to why⁵⁵.
- For each of the significant board committees, the name of the chair, frequency of meetings and attendance by directors.
- Which directors are independent and whether there are any factors that may impact on their independence as well as materiality thresholds.
- Whether there is a procedure agreed by the board for directors to take independent professional advice at the expense of the government business.
- Any transactions between the government business and the director or a director-related entity, whether these transactions were at “arms-length” commercial terms and whether the director derived any direct personal benefit from the transactions (that is, related party disclosures).
- The process for evaluating the performance of the board, its committees and its directors.

Information of a commercially sensitive nature is not required to be disclosed.

It should be noted that annual reporting requirements are reviewed regularly. For the most up-to-date requirements refer to the Treasury annual reporting section on the website.

4. Further Information

General inquiries concerning this document should be initially directed to:

Commercial Policy, Treasury

Telephone: (02) 9228 5813

Internet: www.treasury.nsw.gov.au

⁵² *Annual Reports (Statutory Bodies) Regulation (NSW) 2005*, schedule 1

⁵³ *Public Finance and Audit Regulation (NSW) 2005* schedule 1, part 1 - clause 1, part 2 - clause 3

⁵⁴ It should be noted that loans to a directors, a spouse of a director or a relative of a director or spouse is prohibited under part 4, schedule 10 of the *State Owned Corporation Act 1989*.

⁵⁵ This is analogous to the “if not, why not” approach to good practice recommendations adopted by the Australian Stock Exchange Corporate Governance Council which gives companies flexibility to not adopt its recommendations but tempers this flexibility with the requirement to explain why in the annual report.

Appendix 1: Legislative Requirements for SOC Board Appointments

Section 20J and schedule 8 of the *State Owned Corporations Act (NSW) 1989* regulates the membership, appointment of directors and the procedure of boards for SOCs. Provisions relating to appointment of directors, board composition and skill requirements of the board have been modified by enabling legislation of individual SOCs as detailed below.

Legislation	State Owned Corporation	Board appointment	Board composition	Specified requirements of the directors/ the board
<i>State Owned Corporation Act 1989</i> section 20J and schedule 8. <i>Ports and Maritime Administration Act 1995</i> , section 18	Newcastle Port Corporation Port Kembla Port Corporation Sydney Ports Corporation	Appointed by the Governor on the recommendation of the voting shareholders	1 staff director 2 to 6 other directors	2 to 6 other directors who, in the opinion of the voting shareholders, will assist the SOC to achieve principal objectives
<i>Hunter Water Act 1991</i> section 4B	Hunter Water Corporation	Appointed by the voting shareholders	Chair CEO 1 Unions NSW nominee 6 other directors	6 other directors appointed for relevant expertise
<i>State Water Corporation Act 2004</i> section 7	State Water	Appointed by the voting shareholders after consultation with the portfolio minister	CEO 1 Unions NSW nominee 1 to 6 other directors	The directors must have the necessary skills, expertise and knowledge to enable State Water to meet its objectives
<i>Sydney Water Act 1994</i> section 5A	Sydney Water Corporation	Appointed by the voting shareholders	Chair 9 directors	Must publicly advertise for nominations board to have specified expertise
<i>Energy Services Corporations Act 1995</i> schedule 2	Country Energy EnergyAustralia Integral Energy Eraring Energy Delta Electricity Macquarie Generation TransGrid	Appointed by the voting shareholders	CEO 1 Unions NSW nominee 2 to 5 other directors	
<i>NSW Lotteries Corporatisation Act 1996</i> section 11A	NSW Lotteries Corporation	Appointed by the voting shareholders	CEO 1 Unions NSW nominee 2 to 5 other directors	
<i>Superannuation Administration Authority Corporatisation Act 1999</i> schedule 3	Superannuation Administration Corp (Pillar)	Appointed by the voting shareholders	CEO 1 Unions NSW nominee 2 to 5 other directors	Directors cannot be on the boards of FSS Trustee Corp or SAS Trustee Corp

Legislation	State Owned Corporation	Board appointment	Board composition	Specified requirements of the directors/ the board
<i>Waste Recycling and Processing Corp Act 2001</i> section 7	Waste Recycling and Processing Corporation	Appointed by the voting shareholders after consultation with the portfolio minister	1 Unions NSW nominee 3 to 6 other directors	
<i>Landcom Corporation Act 2001</i> section 8	Landcom	Appointed by the Governor on the recommendation of the voting shareholders in consultation with the portfolio minister	7 directors	
<i>Transport Administration Act 1988</i> section 18H	Transport Infrastructure Development Corporation	Appointed by the voting shareholders after consultation with the portfolio minister	CEO RailCorp CEO TIDC 1 to 5 other directors	The board must have the necessary expertise (including engineering and rail safety expertise) as the voting shareholders, after consultation with the portfolio minister, consider necessary to realise TIDC's objectives
<i>Transport Administration Act 1988</i> section 19NA	Rail Infrastructure Corporation	Appointed by the Governor on the recommendation of the voting shareholders after consultation with the portfolio minister	1 Unions NSW nominee 2 to 6 other directors	The board must have the necessary expertise (including engineering and rail safety expertise) as the voting shareholders consider necessary to realise RIC's objectives

Notes:

- Where the CEO is not specifically on the board under the enabling legislation, the *State Owned Corporations Act 1989* permits the CEO to be appointed as a director.
- Where the chair is not separately listed as a board member under the enabling legislation, the *State Owned Corporations Act 1989* requires a chair to be appointed from the directors.

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Legislation

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Corporations Act (Cth) 2001

Public Finance and Audit Act Regulation (NSW) 2005

Public Sector Employment and Management Act (NSW) 2002

State Owned Corporations Act (NSW) 1989