

Role of Directors

Background

1 of 5

The purpose of this Guidance Sheet is to outline the key legal duties and obligations of Directors and set out clear principles and guidelines for the ethical and professional conduct of Directors in effectively carrying out their responsibilities.

Directors owe certain duties to the NSO and its members. The duties require Directors to act competently, honestly, in good faith and in the best interests of the organisation. When determining the best interests of the organisation, this means in the interests of the members of the organisation as a whole.

This Guidance Sheet covers both common law duties (those duties imposed by the courts), the duties imposed on Directors under the Corporations Act and the moral duties of the role. It is not an exhaustive summary of a Directors' legal obligations. It summarises some of the key obligations imposed on Directors of companies, from which minimum standards of ethical conduct can be drawn.

The Constitution is the other key document governing the appropriate legal and ethical behaviour of Directors in the performance of their duties. The Constitution constitutes a contract, and therefore a legally binding document, between the company and each Director and Company Secretary.

The Primary Role of the Board and Directors

The Board is ultimately accountable for the performance of the organisation.

As such the role of the Board and its Directors is to give direction to the organisation and to accept responsibility for its performance. In addition, the Board is responsible for setting the ethical framework for the organisation and defining and nurturing the organisation's fundamental values.

In order to carry out this primary role Directors are regarded as owing a fiduciary duty to the organisation. This means that a Director has special obligations to the sport because he or she occupies a position of trust. Accordingly, Directors share a common duty on behalf of stakeholders for:

- the achievement of appropriate outcomes
- the financial security of the organisation

As a result of the fiduciary relationship between the Directors and the organisation, the Directors are bound to exercise their rights and powers in good faith and for the benefit of the organisation. When exercising their powers, Directors should consider their moral and social responsibility to the members and community at large.

In exercising this fiduciary duty each Director is responsible for all decisions taken by the Board. This means that in most instances, Board members share a common liability and except in limited circumstances, they can be sued individually or collectively (jointly or severally) in the event of a determination that the Board failed to properly exercise its duty of care or knowingly acted in breach of the law.

In achieving its primary function and exercising its fiduciary duty, the Board's responsibilities can be broken down into the following key areas:

- Strategic responsibilities
- Governance responsibilities
- Legal responsibilities



- Financial responsibilities
- Organisational performance responsibilities
- Organisational risk responsibilities
- Chief Executive Officer appointment, delegation and performance review
- Stakeholder responsibility
- Moral and ethical responsibilities, including culture of the organisation

Legal Responsibilities

Directors are required to understand the needs of the organisation and their legal responsibilities as Directors.

The principal statutory and common law duties imposed upon Directors may be summarised as follows:

a) to act honestly and in good faith in the interests of the organisation as a whole

Directors are given broad discretion to oversee the activities under the Constitution. The duty of good faith applies to all discretions and decisions of Directors.

The duty of good faith and honesty arises at common law partly (as with most of the other common law duties of Directors) because Directors are regarded as being in a position of trust with respect to the organisation.

This duty is also reflected in the Corporations Act, which requires that an officer of the company at all times act honestly in the exercising of his or her powers and the discharge of his or her duties.

In this context, the duty of honesty is similar to the duty to act for a proper purpose. If a Director's purpose is misguided or improper, the Director will breach the duty even though there is no question of personal gain or dishonesty. Accordingly, a Director can be dishonest without being fraudulent.

Principally, therefore, this duty requires Directors to consider the interests of the members of the organisation as a whole. This may involve considering whether the short term or long-term interests of members should be paramount.

In circumstances of insolvency or near insolvency, the duty to act in the best interests of members is overridden by a duty to act in the best interests of creditors.

b) to exercise the degree of care, skill and diligence that a reasonable person in a like position would exercise in the same circumstances

The duty of care, skill and diligence is an objective duty, in that the question is what an ordinary person, with the knowledge and experience of the Director, might be expected to have done in the circumstances if he or she was acting on their own behalf.

The following are key principles that are to be applied in determining whether or not a Director is fulfilling his or her duty of care, skill and diligence to the organisation. Although the list is not exhaustive, the common law requires that Directors shall at least:

- take reasonable steps to place themselves in a position to oversee and monitor the performance of the organisation
- acquire a working knowledge of the fundamentals of the activities of the organisation
- generally monitor affairs and policies, although a detailed inspection of day-to-day activities need not be undertaken
- maintain a familiarity of the financial status by regularly reviewing the financial statements
- make enquiry into matters revealed by the financial statements which call for enquiry

The common law duty to act with care, skill and diligence is also reflected in the Corporations Act which provides that in exercise of powers, a Director must exercise "the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation's circumstances".



- c) to exercise powers granted honestly and for the purposes for which they were conferred and not for collateral purposes

Since Directors of the organisation are fiduciary agents, powers given to Directors may only be exercised for the purposes for which they are given. In particular, those powers must not be exercised in order for the Directors to obtain a private advantage.

Whether a particular act by a Director as a fiduciary, is a genuine exercise of their power for the benefit of the organisation as a whole is generally determined by ascertaining the substantial motivating purpose for which the power is exercised and then by determining whether that purpose was proper or not.

- d) to avoid any actual or potential conflict between the obligations owed to the organisation and a Director's personal interest or other duties

One of the clear rules of the common law is that neither a Director nor responsible officer should allow a conflict of interest to compromise their position with the organisation. Accordingly, Directors' personal interests and their duty to the organisation must not be brought into conflict.

This overlaps with the duty to act in good faith and for a proper purpose.

Categories of situation which likely give rise to conflicts of interest are:

i. Directors or officers taking advantage of opportunity

The general rule is that a Director must not use his or her position as a Director of the organisation to make a personal profit or for their own benefit. If he or she does, then he or she must account to the organisation for the profit made. The Corporations Act provides for similar rules.

ii. Directors taking advantage of an opportunity where the organisation is unable

A Director has an obligation not to profit personally from his or her position as a Director, and not to allow a conflict to arise between his or her duty as Director and his or her own self-interest.

A Director is disqualified from diverting for his or her own benefit, a business opportunity which the organisation is actively pursuing.

A Director's liability to account to the organisation depends upon the facts of the case. It is a defence that the profits were made with the informed consent of the organisation.

iii. Directors' contracts with the organisation

The Corporations Act contains prescribed measures that must be complied with where the organisation wishes to give a financial benefit to a related party such as a Director. This includes circumstances where the organisation contracts with the Director personally or an entity in which a Director has a material personal interest. These 'related party' provisions mandate member approval at a general meeting.

The general rule is that contracts made by a Director with the organisation are voidable at the option of the organisation. This includes contracts in which Directors have an indirect interest. The fairness of the contract is irrelevant, and this is applied as a strict rule.

In addition, the Corporations Act requires a Director to declare the nature of any direct or indirect material personal interest he or she has in a matter that relates to the affairs of the organisation.

iv. Conflict of external duties with Directors' duties

Where a Director holds an office or property which creates or could create duties in conflict with his or her duties as Director of the organisation, they should declare the interest at the next Board meeting after they become aware of the interest.

Where a Director has a material personal interest or direct or indirect pecuniary interest in a matter being considered by the Board he or she must, as soon as possible after the relevant facts have come to the Director's knowledge, make full disclosure of the nature of the interest at the next meeting of the Board.

Such a disclosure will be recorded in the minutes of the meeting of the Board and the Director must not, with respect to that matter:



- be present during any deliberations of the Board, or
- take any part in any decision of the Board.

e) to keep confidential information that is obtained through their position

Directors have a duty not to make unauthorised disclosure or use of the organisation's information and a duty not to disclose or exploit confidential information, such as commercially or price sensitive information or information which is confidential by virtue of a contractual arrangement.

Information is commercially sensitive where it has specific value to the organisation, particularly where its disclosure would allow others to "reap without sowing" or would otherwise be detrimental to the organisation. In the context of the organisation, this would involve any information that is of value to the organisation in the sense that its disclosure might cause damage to the organisation's reputation or disclose plans which the organisation would not want revealed to its competitors or third parties. It would also involve any information determined to be confidential by the Board or senior staff of the organisation.

Directors of the organisation should not reveal any discussions or meetings or documents relating to policies or plans in their initial stages.

The Board should at the very least be informing its members of the major decisions which it has made and report on the reasons for these decisions. The Board is justified in not disclosing all its activities on the basis that in doing so it is acting in the interests of the organisation, by preventing information which may be detrimental to it from being revealed and potentially distorted.

Directors must remember that they have a duty to act in the interests of the organisation as a whole, which includes the interests of all members and not select members or groups of members.

The Corporations Act imposes a statutory duty on a Director not to make improper use of the information acquired by virtue of their office to gain, directly or indirectly, an advantage for themselves or for any other person or to cause detriment to the company.

f) To disclose advantages or business opportunities acquired in the course of their office

Misuse by a Director of the organisation's property so as to make a personal gain or gain for any other person (for example, a company in which the Director is interested) without the authority of the organisation is a clear breach of a Director's fiduciary obligation. In particular, a Director must only exploit corporate opportunities arising through their position as a Director for the benefit of the organisation. A Director who breaches this duty may be liable to account for any gain or profit made.

This duty is also reflected in the Corporations Act which requires a Director not to make improper use of their position to gain, directly or indirectly, an advantage for themselves or any other person or to cause detriment to the company.

Breach of this duty may also involve a breach of a Director's duty of honesty imposed by the common law and by the Corporations Act.

g) to prevent insolvent trading by the organisation

The Corporations Act imposes a duty on Directors to prevent insolvent trading.

A Director will be personally liable for a company's debt if:

i. the person is a Director of the company when the company incurs a debt and:

- A. the company is insolvent at the time or becomes insolvent by incurring the debt or other debts incurred at that time; or
- B. there are reasonable grounds for suspecting that the company is or will become insolvent; or



- C. either the person is aware of grounds for suspecting insolvency, or a reasonable person in a like position in the company's circumstances would be aware; and
- ii. **the person fails to prevent the company from incurring the debt.**

A company is insolvent if it is not able to pay its debts as and when they become due and payable.

As a practical matter, a Director should ensure that they are provided with sufficient financial information on a regular basis to ascertain whether the company can pay its debts. If there is any doubt, the views of the company's auditor should be obtained.

Strategic Responsibilities

It is the Board's job to establish the organisation's strategic direction. This should be reflected in the strategic plan.

The Board is to develop the strategic direction and strategic plan in partnership with the CEO and the sport's key stakeholders.

The strategic direction and strategic plan must ultimately be 'owned' by the Board.

Time should be set aside annually for the Board to:

- develop and refine the strategic direction and strategic plan if required; and
- monitor and assess performance against the strategic plan

All operational plans should be consistent with the strategic direction and strategic plan.

Development and implementation of operational plans designed to achieve the strategic priorities should be primarily the responsibility of the CEO, except where the practical support of Directors is required.

Financial and Organisational Risk Responsibilities

The Board's financial governance needs to address the following issues as a minimum requirement:

- budgeting and financial planning
- reserves and investments
- CEO remuneration and benefits
- protection of assets
- financial reporting
- oversee and monitor the financial performance of the organisation

To ensure appropriate financial governance procedures the Board may establish a Finance Audit and Risk Committee that will work on behalf of the Board to:

- make recommendations to the Board on financial policies
- ensure that the annual budget reflects the organisation's strategic plan and key priorities
- provide assurance of the integrity of the organisation's financial systems
- oversee and advise on board financial reporting
- carry out financial and other risk assessments
- ensure appropriate reporting to stakeholders at end of financial year and other relevant times.

For additional information or assistance, please contact the Governance and Organisational Enhancement team of Sport Australia via email at SportsGovernance@sportaus.gov.au.

