

# Key competencies for directors

## *Board composition*

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? In *Directors at Work*<sup>1</sup>, Kiel et al. talk about the competencies of a director being the experience, knowledge, skills, attitudes, values and beliefs of the person. They provide the following framework for considering these competencies:

- **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.
- **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 (ASXCGC) third edition of the *Corporate Governance Principles and Recommendations* touches on 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.

Firstly, Recommendation 1.2 states that:

*"A listed entity should:*

- (a) undertake appropriate checks before appointing a person, or putting forward to security holders a candidate 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."*

<sup>1</sup> Kiel G, Nicholson G, Tunny J A, Beck J, *Directors at Work: A Practical Guide for Boards*, Thomson Reuters Australia, 2012, p 203-4.

In the commentary to this recommendation, the ASXCGC states 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.”*

Secondly, 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.

Thirdly, 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.”*

Fourthly, Recommendation 2.2 states that:

*“A listed entity should have and disclose a board skills matrix setting out the mix of skills and diversity 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 competencies the board sees as important in the selection of directors. The Corporations Act 2001 (Cth) 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.”*

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Finally, Recommendation 2.6 states:

*“A listed entity should have a program for inducting new directors and provide appropriate professional development opportunities for directors to develop and 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:

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

However, there is one competency that following the *Centro* case<sup>2</sup> 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.<sup>3</sup>

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;
- **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.

## 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.

<sup>2</sup> *ASIC v Healey* (2011) 196 FCR 291; [2011] FCA 717.

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

*“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.”*

### 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’ (August 2014).

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