

Directors have a duty under common law and under the Corporations Act to act in the best interests of the not-for-profit (NFP) organisation that they serve. Directors should not seek to benefit from the NFP, and should not be influenced by their wider interests when making decisions affecting the NFP.

Conflicts of interest arise when the interests of directors (or those of their families, friends or other organisations with which they are involved) are incompatible or in competition with the interests of the NFP. Such situations present a risk, real or perceived, that directors may make decisions based on these external influences, rather than the best interests of the NFP. Effective boards make good decisions by comparing the range of options available to them. If directors allow factors such as their own interests to influence their decision-making, they may make decisions that are not in the NFP's best interests or contrary to law.

Conflicts can affect the reputation of a NFP, even where no actual conflict exists. It can take a long time for a NFP organisation to build its profile and reputation as an organisation people can trust. This reputation can be destroyed very quickly despite the best intentions of the board and management, if actual or perceived conflicts of interest arise and are not properly managed.

Conflicts of interest will arise — they are part of governing an organisation. The important aspect is identifying and managing them effectively. It is considered **good governance** for a NFP to ensure appropriate mechanisms are in place for disclosing and managing conflicts of interest.

Types of conflicts

The most easily recognisable form of conflict arises when a director obtains direct financial benefit, with an indirect financial conflict also arising when a close relative of a director receives a financial benefit from the NFP. Non-financial or personal conflicts occur where directors receive no financial benefit, but continue to

be influenced by external factors, for example, perhaps because they use the NFP's service themselves or care for someone who does.

Directors may also have a conflict of loyalty, that is they may have competing loyalties between the NFP to which they owe a primary duty and some other person or entity. Many funders, statutory authorities and NFPs nominate members of staff or other representatives to sit on boards as directors, or directors may be elected through a democratic process by a constituency of a NFP. A director may serve on the board of more than one NFP.

Despite the legal principle that the directors' primary obligation is to the NFP, representative directors often feel a strong loyalty to their nominating body or constituency. It is important that any representative directors receive education about their duty to act in the best interests of the NFP and not the organisation that nominated them. When fundraising, directors must maintain independence of judgment regardless of the source of funds and not allow the funder's views to distort the mission of the organisation.

A perceived conflict of interest can be as damaging to the reputation of the NFP as a real conflict.

Duty to disclose

The duty to disclose a conflict applies not only to directors and responsible persons, but also to officers of the NFP. Officers can include employees, volunteers, secretaries, receivers, managers, administrators, liquidators and trustees.

Directors are required by law to declare any interest in contracts unless excluded under S 191 of the Corporations Act. However, employees acting in their own interests may be in breach of their employment contract and subject to disciplinary action or dismissal. Volunteers may serve on the board of the NFP and be subject to directors' duties.

How to disclose?

On appointment, directors should be asked to complete a declaration of interests. This can be attached to the director's consent to act form.

Completed declarations should be returned to the secretary (or other relevant person if there is no secretary), who will be responsible for keeping the register of conflicts of interest up-to-date. The declaration of interests needs to be updated as and when changes occur, and also reviewed annually. This may be recorded on the annual board calendar document.

When a conflict of interest does arise, it is the responsibility of the director in question to declare the conflict to the board. If they fail to do so, the chair of the board or the secretary should declare the conflict if it is known in sufficient detail, such as through the register of interests. It is **good governance** to include declarations of interest as a standing agenda item at board meetings, to ensure that directors have the opportunity to disclose potential conflicts.

Effect of disclosure

Where a NFP is structured as a company limited by guarantee, and as such is a public company, there are specific disclosure requirements in the Corporations Act relating to 'material personal interests' which must be complied with.

While many incorporated NFPs and their subsidiaries are companies limited by guarantee, NFPs can also be incorporated under specific state legislation, and will be subject to other specific requirements contained in the legislation, which may include the requirement to keep a register.

Generally, individuals with a conflict of interest are prohibited from taking part in discussions and voting on matters relating to the conflict.

A specific conflict should be declared as early as possible in the discussion at a board meeting of a particular item, and recorded in the minutes, even though the general conflict may already be noted in the register. Ideally, a specific conflict should be declared prior to the meeting, with consideration given to excluding any relevant board papers from the board

pack provided to the director in question. Depending upon the type of conflict declared, it may be appropriate for the director in question to leave the room during the entire discussion of and voting on the matter. They can return to the meeting once invited by the other board members. This absence from the meeting, including the time the director left and returned to the meeting and the reasons for the absence, should be recorded in the minutes. This allows the board to prevent any appearance of impropriety or perceived conflict by ensuring that the director in question:

- is not involved in the discussion and the decision
- does not obtain information from the earlier discussion that would allow them to influence the final decision.

If the board determines, with the assistance of legal advice, that the conflict of interest cannot be resolved or managed, and the director determines that they cannot discharge their duties, then the director in question should resign from the board.

Conflicts of interest policy

A comprehensive conflicts of interest policy will assist everyone in the organisation to understand types of conflicts and how they are managed.

It should:

- contain a statement noting that the management of conflicts is central to organisational integrity
- define a conflict of interest (noting that there are real and perceived conflicts) and provide examples of types of conflicts
- provide an overview of directors' duties (and note that the protection offered in s180(2) — the business judgment rule — will not apply in situations where a director acts on a material personal interest) and that s 189 is relevant to reliance on advice
- clarify to whom the policy applies
- set out the guiding principles for the disclosure of conflicts of interest
- describe the processes for the disclosure of conflicts, including the register and a standing agenda item at board meetings
- provide direction as the point at which conflicts are so material that they effectively prohibit the individual from performing in their role

- describe what is expected of a director if the conflict is significant
- include reference to how regularly the policy will be reviewed.

If the NFP is a charity, the policy should also refer to the Australian Charities and Not-for-profit Commission's (ACNC's) Governance Standard 5 (duties of responsible persons) and the duty to disclose and manage conflicts of interest.

The conflicts of interest policy should also either cover related-party transactions or refer to the related-party transactions policy. The policy should be circulated to everyone in the organisation (employees and volunteers), and confirm that the policy is a board policy applying across the organisation. The board will 'set the tone from the top' in relation to how it manages related-party transactions and conflicts of interest. The board should set a date for review of the policy.

Further information can be found in Governance Institute's *Good Governance Guide: Issues to consider when developing a policy on disclosure of and voting on matters involving a director's material personal interests* (which has been developed for public listed companies) and *Good Governance Guide: Issues to consider when developing a policy or process for managing related party transactions*.

Communication

The policy should be communicated internally and externally.

Internally, it can form part of the induction package provided to new directors and employees and also any regular training that is provided to employees on the NFP's policies.

Externally, it should be communicated to members of the NFP and the community via the NFP's website.

The policy should also refer to the NFPs' policies on:

- whistleblowing, and
- diversity — it is **good governance** to have a diverse mix of skills, backgrounds, beliefs, ethnicities on the board, which can aid in identifying and analysing potential conflicts of interest.