ORGANISATION

Relationship between the board and management

A productive relationship between the board and management is critical for good governance and organisational effectiveness. However sometimes this can be difficult to achieve in reality. The board and management should be trying to achieve the same vision and objectives.

As such, a team approach based on trust and respect is more appropriate than a boss/subordinate relationship. Central to this relationship is a clear mutual understanding of roles, delegations and boundaries which allows each party to respect the other's responsibilities, contributions and expectations. The relationship depends on an open flow of relevant and timely information in both directions.

The formalities of the nature of the relationship and the responsibilities and expectations of each of the board and management is often set out in the organisation's board or governance charter. However, it is the translation of these principles into practice as part of the culture of the organisation and the relationship between board and management which is vital. The chair has a primary responsibility to foster and maintain a constructive and effective culture in the best interests of the organisation.

In the final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Commissioner Hayne points out "boards cannot, and must not, involve themselves in the day-to-day management of the corporation"[1]. To hold management to account, the board expects management to understand and accept that the board's role is to monitor and question, probe issues, seek clarification, offer insight and share its knowledge and experience. With management much more deeply involved in the detail and operations of the organisation, board members rely on management to share in a timely manner all material information needed for decision making to allow them to effectively fulfil their obligations as directors. The board also expects management to ask advice and make use of the directors' wealth of experience as and when appropriate.

Similarly, management has expectations of the board. Primarily, they expect that their board will trust them to implement strategies and deliver outcomes without undue interference. The CEO specifically expects the board to clearly state performance objectives and define boundaries of authority. Without this direction, the CEO is left to speculate on what the board wants him/her to achieve. The CEO should also expect regular and honest performance feedback. Recognition for

1. K M Hayne, 2019, *Final Report Royal Commission in to Misconduct in the Banking, Superannuation and Financial Services Industry Volume 1*, February, Commonwealth of Australia, p 400, **https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf**, (accessed 4 June 2019).

achievement, honesty and openness, wisdom and advice, and the ability to use directors as a sounding board are also desirable.

For optimal performance, boards and management must work together cohesively as a team with respect and candour. Responsibilities and expectations of the board include:

- Being prepared for board meetings, reading board papers and asking thoughtful questions
- Making quality informed decisions based on relevant and material information being available to the board, especially from management
- Overseeing, managing and holding management accountable
- Satisfying itself of the competence, capability and capacity of management
- Sharing learnings, experience and insights from board-members' backgrounds and experience
- Being visible to the business and attending key management, corporate and stakeholders events
- Building relationships with, and being accountable to, shareholders/members and regulators of the organisation's performance.

Board directors have high expectations (based on legislation) and demands of management to ensure timely and relevant information flow and reporting to it so that there are 'no surprises'. It is evident that boards fail to spot emerging or recurrent risks when management only provide good news and/over-simplified board reports.[2] The final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry also stated that "boards cannot operate properly without having the right information. And boards do not operate effectively if they do not challenge management."[3]

Board directors need to stay curious and make proper inquiries when reading information presented by the management. As such, boards should signal the high standards of discipline and rigour expected of management by challenging and asking hard questions concerning management reports in order to:

- test validity of assumptions made;
- stress test opportunity/risk analysis;
- test depth and breadth of management's knowledge, understanding and analysis;
- help foster trust and confidence in management; and
- stimulate innovative and creative thought.

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Board directors must courteously and respectfully listen to management with an open but constructively challenging mind to allow management to make its contribution with confidence and clarity of viewpoint, and without undue interference, constraint or trepidation. In this sense, leadership by the chair is critical in managing the relationship to meet the reasonable needs and expectations of both board and management. As recommended in the Prudential Inquiry into the Commonwealth Bank of Australia (CBA) final report, boards should strive and execute a well-balanced empowerment with sufficient challenges on management.[4]

2. J Laker, J Broadbent and G Samuel, 2018, *Prudential Inquiry into the Commonwealth Bank of Australia*, Australian Prudential Regulation Authority, April, ss 2.2.1 and 2.2.5, **https://www.apra.gov.au/sites/default/files/CBA-Prudential-Inquiry_Final-Report_30042018.pdf**, (accessed 3 June 2019).
3. K M Hayne, 2019, *Final Report Royal Commission in to Misconduct in the Banking, Superannuation and Financial Services Industry Volume 1*, February, Commonwealth of Australia, p 396, **https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf**, (accessed 4 June 2019).
4. J Laker, J Broadbent and G Samuel, 2018, *Prudential Inquiry into the Commonwealth Bank of Australia*, Australian Prudential Regulation Authority, April, p 81, **https://www.apra.gov.au/sites/default/files/CBA-Prudential-Inquiry_Final-Report_30042018.pdf**, (accessed 3 June 2019).

Conversely, through its displayed actions and performance, management must assure the board of management's competence, capability, capacity, integrity, effectiveness and efficiency. In this sense, management has a critical role in effective board decision making by:

- reporting relevant material information to the board;
- stimulating board discussion on emerging issues;
- assisting the board in analysing and considering issues; and
- responding to issues raised by the board.

> The relationship between the chair and CEO is critical. Primarily, it should be an engaged business relationship where professional and personal trust and respect are paramount in an environment of constructive challenge.

When reporting or presenting to boards, management must:

- be clear as to the purpose of the report or presentation and what the board is being asked to do arising from it (that is, for noting information purposes only, for discussion and to gain the board's wisdom and input, or for decision making and resolution);
- know their audience;
- be responsive to audience's needs;
- understand board politics and personalities;
- maintain focus on key issues; and
- be patient, polite and respectful.

Good reporting is about quality not quantity.[5] Boards and management need to work together to find a right balance between precise and appropriately targeted information and lengthy data. Boards should regularly give feedback to management regarding the quality of board information. Both boards and management should constantly consider how to improve the quality, structure and format of board information so that right information can add value in the board decision-making processes.

Management expects the board not to unduly concern or involve itself in operational matters. Notwithstanding, management should still be respectful of the need for the board to delve deeply from time to time, especially if problematic trends are emerging and are not being resolved by management.

Relationship between the chair and CEO

The relationship between the chair and CEO is critical. Primarily, it should be an engaged business relationship where professional and personal trust and respect are paramount in an environment of constructive challenge.

This is a vital relationship as the primary source of communication between the board and management between board meetings is through chair and CEO interactions.

The relationship needs to primarily be a 'business relationship' where professional and personal trust and respect is paramount and where the chair can act as a mentor/sounding board to the CEO. At the same time it should be a relationship of frankness and candour (behind the scenes) and unity and mutual support (in public).

It is to be expected that the chair and CEO meet from time to time between board meetings to help set board agendas, to debrief following board meetings, to exchange updates (positive and negative in nature) on relevant/current issues, and to give guidance on material issues impacting the organisation.

5. K M Hayne, 2019, *Final Report Royal Commission in to Misconduct in the Banking, Superannuation and Financial Services Industry Volume 1*, February, Commonwealth of Australia, p 400, **https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf**, (accessed 4 June 2019).

Relationship between individual board members and executive management

Individual board members have no inherent authority or executive power. Enquiries by board members of management and by management of individual board members should primarily be channelled via the chair and CEO. A communication protocol should be clearly stated in the organisation's board or governance charter.

Where there is any direct material contact between individual board members and executive management, the chair, CEO, and/or company secretary should be kept informed by way of courtesy. Where there is strength of mutual respect and confidence that the chair's and CEO's authority will not be undermined, communications between executive management and board members may be freer. In circumstances where the board establishes board committees and/or working groups (which may have a mix of board directors and key executives members), there may also be expectations of freer communication between the chairs of the committees or working groups and relevant executives responsible for those functions, on matters within the scope of those functions. Members of the committees or working groups should refer to their committee or working group charters or terms of reference to clarify the appropriate communication channel.

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