

## GBE BOARDS

### Introduction

- 4.1 A GBE Board is responsible for achieving the government's broad policy objectives and ensuring that the enterprise is operating efficiently and effectively. At the same time, the board and management are accountable for their performance to shareholder Ministers and the Parliament. Boards are a critical component of corporate governance. The Australian National Audit Office (ANAO) stresses this point with its observation that 'in the private sector, the focus of corporate governance is on the board'.<sup>1</sup>
- 4.2 Boards are subject to a range of disclosure requirements and duties such as providing Ministers with corporate plans and providing ongoing financial reports. This has tended to focus scrutiny of boards on their effectiveness in conforming with these requirements. However, there is an increasing focus on the performance levels of government and non-government boards.
- 4.3 The 1997 Governance Arrangements, for example, state that 'boards have absolute responsibility for the performance of the GBE, and are fully accountable for this to the shareholder Ministers'.<sup>2</sup> Hilmer also focuses on organisational performance with his statement that the 'key role of boards should be to ensure that corporate management is continuously and

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1 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 3.

2 *Governance Arrangements for Commonwealth GBEs*, June 1997, p. 8.

effectively striving for above-average performance, taking account of risk.<sup>3</sup>

- 4.4 This chapter focuses on the performance aspects of GBE boards. Boards require, in their directors, a mix of skills, experience and the ability to ask management the 'right' questions. At the same time, boards need a range of support mechanisms and incentives to achieve their outcomes. This chapter will consider some of the processes by which boards can improve their performance. For example, induction, education and training programs are increasingly being offered to boards.
- 4.5 The final section will consider the adequacy of performance appraisal for boards and individual directors. This section will discuss whether GBE boards are subject to sufficient performance appraisal, and consider measures that can help to improve performance assessment.

## Board independence

- 4.6 A key factor in ensuring that boards can function efficiently and effectively is their independence. Boards must have autonomy and independence in the conduct of their duties and be free from day-to-day involvement by Ministers. At the same time, however, boards are accountable for their performance to shareholder Ministers and the Parliament. The ANAO commented that the 'independence of directors is necessary to ensure that there are no actual or perceived conflicts of interest and to ensure that the board is effective in supervising and, where necessary, challenging the activities of management.'<sup>4</sup> The ANAO has drawn attention to aspects of selection and appointment of board members that help to ensure board independence. The ANAO notes that:
- the majority of the CAC Board should be independent of both the management team and any commercial dealings with the CAC;
  - the Board Chairperson should be independent of management; and
  - the Board should select the CEO.<sup>5</sup>

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3 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, Information Australia, Melbourne, 1998, p. 5.

4 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 21.

5 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 19, 20 and 22.

- 4.7 The 1997 Governance Arrangements include sections on board responsibility, and board appointments and removal. Two requirements in particular help to ensure the board's independence. These requirements state:
- the Board Chairperson shall not also be an executive of the GBE, unless otherwise agreed by the shareholder Ministers; and
  - the appointment of departmental officers to GBE Boards will only be considered in exceptional circumstances.<sup>6</sup>
- 4.8 In addition, the 1997 Governance Arrangements state that the 'board should consult the shareholder Ministers about the board's preferred candidate for the position of CEO and provide sufficient time for the shareholder Ministers to respond prior to an appointment being made.'<sup>7</sup>

## Selection and appointment of directors

- 4.9 A GBE's performance depends largely on the capabilities and performance of its board. In turn, the skills, experience and qualifications of individual directors influence the overall ability and performance of the board. Therefore, selection processes are important in ensuring that boards have high performing directors with appropriate skills. Hilmer has identified three factors which combine to weaken the performance orientation of boards. These include:
- confusion over the board's role and responsibilities;
  - a lack of processes to keep performance at the centre of the board's agenda; and
  - weaker director selection processes.<sup>8</sup>
- 4.10 In regard to the last dot point, Hilmer suggests that one of the dangers for boards is 'capture' by management. In some cases, management will influence board selection which could compromise the board's performance. Hilmer states:
- ...boards inevitably come to be comprised of people sympathetic to management, and with a common world view and set of values.

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<sup>6</sup> *Governance Arrangements for Commonwealth GBEs*, June 1997, Section 3.4, p. 8.

<sup>7</sup> *Governance Arrangements for Commonwealth GBEs*, June 1997, Section 3.9, p. 9.

<sup>8</sup> Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 19.

Moreover, management largely controls the shape and content of the board's agenda and the information on which decisions are based. Thus researchers have found that, in general, boards do not establish basic objectives or corporate strategies, or even ask discerning questions.<sup>9</sup>

- 4.11 Blake Dawson Waldron (BDW) commented that the selection and appointment of new directors is a matter of central importance in any GBE because 'a board's success in implementing best practice corporate governance standards and processes depends entirely on the ability and degree of dedication of its members'.<sup>10</sup> BDW suggested that some of the key qualities required of directors include 'integrity and accountability, informed judgement, financial literacy, mature confidence and high performance standards'.<sup>11</sup> With respect to boards of public enterprises, BDW stated:

Boards of public enterprises should be comprised of a variety of skilled and competent individuals who represent a cross-section of the community. Each member of a board should bring to the enterprise a different type of knowledge or experience. Membership should not necessarily be limited to persons equipped with established business skill or commercial expertise. Service on the board of a GBE should be open to all persons who demonstrate competence in a relevant field and a commitment to the service and improvement of the organisation, and to the satisfaction of stakeholders.<sup>12</sup>

- 4.12 The 1997 Governance Arrangements discuss board appointments and removal.<sup>13</sup> In particular, the governance arrangements state that 'GBE boards of directors are to comprise people with an appropriate mix of skills, who are to be appointed on the basis of their individual capacity to contribute to the board having an appropriate balance of relevant skills such as commerce, finance, accounting, law, marketing, workplace relations and management, and contribute to the achievement of the GBE's objectives'.<sup>14</sup> The 1997 Governance Arrangements set out the following requirements relating to board appointments:

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9 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 19.

10 Blake Dawson Waldron, *Submission*, p. S145.

11 Blake Dawson Waldron, *Submission*, p. S145.

12 Blake Dawson Waldron, *Submission*, p. S144.

13 *Governance Arrangements for Commonwealth GBEs*, June 1997, Sections 3.4 to 3.9.

14 *Governance Arrangements for Commonwealth GBEs*, June 1997, Section 3.4, p. 8.

- the Board Chairperson shall, through the Board, provide shareholder Ministers with a list of suitable candidates for Board membership;
  - shareholder Ministers may elect to appoint a candidate not proposed;
  - shareholder Ministers shall consult with the Prime Minister and the Treasurer on all Board appointments, and
  - Board appointments should normally be for terms of three years, with retiring directors eligible for inclusion in the list of candidates.<sup>15</sup>
- 4.13 The ANAO also supports the need for board membership to have suitable skills, knowledge and experience to perform their duties.<sup>16</sup> In relation to board appointments, the ANAO commented that to 'ensure that the best people are appointed to the board, board positions should be sought through wide external search and there should be a well defined and open procedure for the appointment of new directors.'<sup>17</sup>
- 4.14 Employment National (EN), in evidence to the inquiry, indicated it had recently undertaken an executive search and made a recommendation to the Minister that was accepted. EN stated:
- The additional board member had industry experience and that was part and parcel of the broadening of the board not only to encompass business acumen and professional directors and their capabilities but to actually get somebody who had a broad knowledge of the recruitment services industry as well.<sup>18</sup>
- 4.15 Telstra's selection and appointment process is different to that of other GBEs because it is partly privatised and listed on the Australian Stock Exchange. The Department of Communications, Information Technology and the Arts (DoCITA) advised the Committee that there is no standard requirement for the Board to provide a list of possible candidates to the Minister.<sup>19</sup> Telstra is a Corporations Law company, and under its constitution, the directors of Telstra are elected at the AGM on a rotation

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15. *Governance Arrangements for Commonwealth GBEs*, June 1997, p. 8. Notable exceptions – directors of Australia Post are appointed by the Governor-General on the nomination of the Minister in accordance with section 73 of *Australian Postal Corporation Act 1989* and directors of Telstra are appointed at a general meeting of shareholders in accordance with section 225 of the *Corporations Law*.

16 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 20.

17 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 20.

18 Mr Rod Halstead, Employment National, *Transcript* p. 23.

19 Mr John Neil, Department of Communications, Information Technology and the Arts, *Transcript*, p. 80.

of one-third. DoCITA, however, indicated that directors would need the support of the Commonwealth, given its continuing share ownership, to be elected.<sup>20</sup>

## Induction, education and training for directors

4.16 As suggested in the previous section, board directors need a combination of skills, experience and knowledge to perform effectively. At the same time, there must be a focus on continuous improvement by the board in general and by individual directors. Boards, like any other professional body or work force, need to identify possible shortcomings in their skill and knowledge base and arrange for appropriate education and training.

4.17 Training and education for new directors can begin with effective and appropriate induction programs. BDW supports the need for induction programs and reported that 'The Bosch Report, the Cadbury Report, the ABA Corporate Director Guide Book and the Toronto Stock Exchange Report all assert that it is good practice for an incoming director to receive induction training.'<sup>21</sup> BDW stated:

The purpose of such a process is to familiarise the newly appointed director with, inter alia, the nature and purpose of the business of the organisation, corporate strategy, relevant legislation, governance processes, and current issues facing the board. Directors have an obligation to develop a broad understanding of the area of operation of the government business, and such an introduction should facilitate an early understanding. In terms of the public sector, this includes an awareness of public sector values; and standards of probity and accountability.<sup>22</sup>

4.18 The ANAO also supports the need for appropriate director induction training commenting that for 'newly appointed directors to be able to effectively fulfil their duties they need to, among other things, attain knowledge of the context and purpose of the organisation and become familiar with corporate strategy and current issues facing the board.'<sup>23</sup>

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20 Mr John Neil, Department of Communications, Information Technology and the Arts, *Transcript*, p. 80.

21 Blake Dawson Waldron, *Submission*, p. S145.

22 Blake Dawson Waldron, *Submission*, p. S145.

23 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 21.

- 4.19 BDW suggested that an effective induction program should include the following elements:
- each incoming director should receive a director's resource book which contains background material including history and current structure of the organisation, board minutes of the past financial year, the corporate plan and operational information including information on products, services and distribution networks;
  - a series of planned meetings with management and senior executives;
  - familiarisation visits to the organisation's facilities and operations, with on-site briefings; and
  - detailed briefings on the expectations, legal obligations and personal liability of directors, the issue of directors dealing in the company's shares (if relevant) and the responsibilities of directors regarding committees on which they may be required to serve.<sup>24</sup>
- 4.20 In addition to an effective induction program for directors, there is also the need for continuous education. BDW commented that 'continuous director education is a major element in corporate governance best practice.'<sup>25</sup> BDW also indicated that education courses provided to directors should also be made available to others involved in the corporate governance process, including senior management. BDW suggests that this would help to develop an 'understanding of the roles and responsibilities of the board in relation to corporate governance.'<sup>26</sup>
- 4.21 The ANAO supported continuous education programs for directors commenting that 'continuing education and professional development programs will ensure that directors remain abreast of any developments which can impact on their corporate governance and other duties and maintain leadership in the area of expertise that contributed to their appointment to the board.'<sup>27</sup>
- 4.22 BDW identify the following key components which should comprise a continuous director education program:
- corporate governance training;
  - industry training;

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24 Blake Dawson Waldron, *Submission*, p. S145-146.

25 Blake Dawson Waldron, *Submission*, p. S147.

26 Blake Dawson Waldron, *Submission*, p. S147.

27 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 21.

- operational methods;
  - disclosure requirements;
  - financial reporting obligations;
  - potential conflicts of interest;
  - directors' duties and consequences of breach;
  - education on changes to the legislative regime governing the company's operations;
  - there should also be continuous director education as to the changing commercial risks associated with the company's operations;
  - directors should be continually informed about competitive behaviour and activity;
  - professional development programs should also be made available to directors to ensure that each director maintains leadership in the area of expertise that originally contributed to the director's appointment to the board; and
  - where it is appropriate, external advisers can be used to improve the process of director education through the use of specifically tailored education and training programs.<sup>28</sup>
- 4.23 BDW, in developing the previous list, commented that 'directors of GBEs must remain abreast not only of commercial matters affecting their organisation, but also of political, social, industrial, and legal developments relevant to the activities of the organisation'.<sup>29</sup>

## Performance appraisal

- 4.24 Earlier in this chapter it was reported that boards should be 'continuously and effectively striving for above-average performance, taking account of risk.'<sup>30</sup> This objective requires that systems be developed to monitor and record performance. Hilmer, in discussing non-government boards, suggests that boards should seek to define what is meant by 'above

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28 Blake Dawson Waldron, *Submission*, pp. S147-148.

29 Blake Dawson Waldron, *Submission*, p. S148.

30 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 32.



average performance'.<sup>31</sup> Hilmer cautions boards against using narrow performance measures such as quarterly earnings and instead suggests that boards develop a 'longer-term set of measures'.<sup>32</sup>

4.25 The quest to develop appropriate performance information to assess board and director performance is complicated. Hilmer suggests that difficulties in developing performance information can result in a lack of clarity regarding board performance and accountability. Therefore, Hilmer suggests that boards should spend time articulating:

- the indicators to be used, eg total returns to shareholders, market share, productivity, cash flow;
- the time frames that are considered appropriate;
- the comparison group against which performance is to be compared, eg all listed firms in Australia, industry peers in Australia or world-wide; and
- the standard that is to be considered satisfactory, eg top half, top quartile or top two-thirds of the comparison group, and how that standard might change over time.<sup>33</sup>

4.26 BDW also discussed the issue of performance measures for boards and directors commenting that an Australian Institute of Company Directors (AICD)/KPMG September Quarter Boardroom Report found that four out of five directors considered that board performance is linked to corporate performance.<sup>34</sup> BDW drew attention to the difference between indicators of corporate performance in the private sector and the public sector. BDW stated:

Government enterprises do not necessarily measure performance purely in terms of financial return. Rather they are often concerned also to maximise the generation of public benefit, meet the political and bureaucratic expectations of the Ministers with which they are associated, and to continue to secure adequate government funding support. These differing performance goals must be taken

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31 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 32.

32 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 32.

33 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 34.

34 Blake Dawson Waldron, *Submission*, p. S149.

into account when structuring a performance appraisal model for GBEs.<sup>35</sup>

- 4.27 BDW supported the need for a performance focus commenting that a board 'should monitor its own performance and that of its individual members where feasible, to ensure that it adds value, and is operating efficiently and effectively in accordance with its obligations and the evolving situation of the organisation.'<sup>36</sup> In particular, BDW drew attention to the tendency for Australian boards to focus more on conformance with legislative and reporting requirements than with performance.<sup>37</sup>
- 4.28 The Humphry Report commented that boards 'should be assessed, and decisions made in respect of their continuing tenure, against key financial and non-financial objectives and compliance with accountability including reporting requirements.'<sup>38</sup>
- 4.29 When Mr Humphry was asked about the adequacy of performance assessment, operation and capability of GBE boards, he commented that it was an area requiring 'continuous improvement.'<sup>39</sup> With respect to performance criteria for boards, Mr Humphry stated:
- Basically it is about continuing to improve the shareholders' position. Therefore you would expect them to be delivering the goods. When the finance team and myself did our review we found that the return on capital, except in the case of two outstanding examples, Telstra and Australia Post, in many other instances was well below what you would have expected. That concerned us greatly.<sup>40</sup>
- 4.30 Australia Post indicated that it had commenced a self assessment process of board performance. Australia Post stated:
- The board itself annually conducts a process of self-assessment, in a sense. It is driven by the chairman. She has developed a comprehensive questionnaire that goes to all sorts of areas—governance, individual contributions, balance on the board and so on and so forth—which is filled out individually by each of the directors. It is then subject to a one-on-one exchange between the

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35 Blake Dawson Waldron, *Submission*, p. S150.

36 Blake Dawson Waldron, *Submission*, p. S149.

37 Blake Dawson Waldron, *Submission*, p. S149.

38 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 29.

39 Mr Richard Humphry, *Transcript*, p. 112.

40 Mr Richard Humphry, *Transcript*, p. 112.

directors and the chairman and also to a collective discussion about the total outcomes at full board level.<sup>41</sup>

- 4.31 As a result of this self-assessment process, Australia Post advised that the board identifies its strengths and weaknesses and agrees on a course of action to deal with any perceived weaknesses.<sup>42</sup> In relation to the review of the current year's performance, Australia Post indicated that it will be using the ANAO's Better Practice Guide on Corporate Governance, including its checklist of actions for assessment of board performance, as part of its current review.<sup>43</sup>

### Assessment of individual directors

- 4.32 Performance of boards cannot be in isolation from the performance assessment of individual directors. There is not, however, universal agreement on this point. BDW, for example, reported that General Motors' performance assessment process seeks 'to increase the effectiveness of the board, not to target individual board members.'<sup>44</sup> In addition, AC Chandler suggested that the collegial nature of boards ruled out the individual scrutiny of directors.<sup>45</sup> BDW disagrees with these views and asserted that individual director assessment was a necessity. BDW stated:

...it is difficult to see how individual director performance can be ignored in the assessment of boards. Directors are (or should be) selected for their particular qualities and skills such as independence, integrity, accountability, numeracy, mature confidence, high performance standards, industry knowledge, strategic thinking, and the ability to ask very good questions. The performance of individuals should reflect these qualities. Where there is a lack of performance, stakeholders should be entitled to know, particularly when a director is being re-elected.<sup>46</sup>

### Performance appraisal methodology

- 4.33 While there was general agreement on the need for performance appraisal of both boards and individual directors, and the need for identification of performance indicators, there was less information on how performance

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41 Mr Michael McCloskey, Australia Post, *Transcript*, p. 123.

42 Mr Gerry Ryan, Australia Post, *Transcript* p. 123.

43 Mr Gerry Ryan, Australia Post, *Transcript* p. 123.

44 Blake Dawson Waldron, *Submission*, p. S151.

45 Blake Dawson Waldron, *Submission*, p. S151.

46 Blake Dawson Waldron, *Submission*, p. S151.

appraisal should be conducted. The ANAO supports the need for performance appraisal of boards and individual directors commenting that this 'could be done using key performance indicators developed for this purpose but may include ministerial and/or peer reviews'.<sup>47</sup> In addition, the ANAO suggested that boards 'should establish an appropriate mechanism for reporting the results of Board assessments'.<sup>48</sup>

4.34 BDW suggested that certain features of board operations such as communication with management, and separation of roles and responsibilities are 'intangibles that are difficult to measure'.<sup>49</sup> BDW has sought to address some of these concerns by proposing the following methodology for assessment:

- appointment of an external facilitator who understands the GBE's objectives, strategic direction, culture and history;
- design and distribution of a questionnaire for directors. Questions should cover a broad range of issues such as quality of communication with management and delineation of powers, effective interaction between directors, and quality and effectiveness of director induction and continuing education;
- individual director performance should include execution of specific Board duties, personal characteristics, and core competencies; and
- the Board should meet to review and analyse the questionnaire results to assist the Board to:
  - ⇒ identify areas of strength;
  - ⇒ identify areas for improvement;
  - ⇒ highlight areas of possible risk exposure;
  - ⇒ set goals; and
  - ⇒ establish and publish the link between corporate governance practices and corporate performance.<sup>50</sup>

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47 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 26.

48 Australian National Audit Office, *Principles and Better Practices, Corporate Governance in Commonwealth Authorities and Companies - Discussion Paper*, May 1999, p. 26.

49 Blake Dawson Waldron, *Submission*, p. S152.

50 Blake Dawson Waldron, *Submission*, pp. S152-153.

## Director remuneration

- 4.35 Director remuneration is an important element in attracting top applicants to boards. In relation to GBE boards it cannot be assumed that the attraction of 'public service' is a sufficient reward. Remuneration packages and schemes can be complicated depending on the way remuneration is linked with corporate performance. Share options, for example, are becoming a significant component of remuneration packages.<sup>51</sup> Humphry commented that in 'the private sector, directors also have the opportunity to own shares in the firm, which increases the likelihood of directors' interests being aligned with those of the other shareholders.'<sup>52</sup> Telstra is the only GBE listed on the stock exchange. Its directors are permitted to own shares.
- 4.36 There have been calls for parity in remuneration between directors of private sector and government boards. Humphry, for example, concluded that to 'attract and keep suitably qualified and experienced directors for its GBEs, the remuneration paid to the directors of GBEs should be benchmarked against that paid to directors of similar private sector firms'.<sup>53</sup>
- 4.37 BDW also drew attention to GBE director remuneration commenting that the remuneration offered to directors of government boards is not as attractive as that offered by the private sector. BDW stated that 'consideration may have to be given to the prospect of offering GBE directors more substantial financial rewards, if the maintenance of a high standard of skill and commitment is a serious goal'.<sup>54</sup>
- 4.38 The search for an effective remuneration scheme for GBE boards is a significant challenge. Excluding the directors of Telstra, the use of share options is not possible. In 1997 Humphry indicated that there was no link between the remuneration of GBE directors and overall corporate performance. Therefore, Humphry concluded that the public sector requires 'a scheme that linked directors' remuneration with the economic value added to the entity over the period of their directorship'.<sup>55</sup>

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51 Hilmer, F.G., *Strictly Boardroom, Improving Governance to Enhance Company Performance*, 2<sup>nd</sup> Edition, 1998, p. 103.

52 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 29.

53 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 29.

54 Blake Dawson Waldron, *Submission*, p. S144.

55 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 29.

## Conclusions

- 4.39 Corporate governance embodies processes and systems by which corporate enterprises are directed, controlled and held to account. Boards, therefore, are a central part of corporate governance. Boards of GBEs are responsible and accountable to shareholder Ministers and Parliament for delivering the government's policy objectives and ensuring that the enterprise is operating as efficiently and effectively as possible.
- 4.40 In view of the significant responsibility placed in boards of GBEs, the Committee has reviewed some of the key fundamentals that influence the capacity of boards to operate. First, is the independence of the board. Boards must be free of day-to-day involvement of shareholder Ministers in the operational affairs of the enterprise. In addition, actual or perceived conflicts of interest must be identified so as to allow boards to operate freely and, if necessary, challenge the activities of management. The Australian National Audit Office (ANAO) has drawn attention to aspects of selection and appointment which will help to ensure board independence. Most importantly, the majority of the board and board chairperson should be independent of management.
- 4.41 A second major issue for boards relates to selection and appointment criteria. It is essential that highly skilled, experienced and knowledgeable people are appointed. The 1997 Governance Arrangements indicate that boards should have a balance of relevant skills in areas such as commerce, finance, accounting, law, marketing, workplace relations and management. However, it is important that directors should not rest on their credentials when they were first selected. There is the need for continuous improvement. The Committee has noted that induction, education and training programs are increasingly being offered to board directors. GBE boards must ensure that there are appropriate and effective induction, education and training programs offered to new and existing board directors.
- 4.42 All of these factors ultimately lead to the issue of performance assessment of both the board and individual directors. Boards and individual directors must be held to account for their performance. Hilmer, Blake Dawson Waldron (BDW) and the ANAO have all discussed the need for greater attention to be given to scrutinising board and director performance. The Committee agrees with this focus and suggests that boards and directors should embrace opportunities that will strengthen performance appraisal. The Committee notes the positive work of the Australia Post board to introduce a self-assessment process involving a comprehensive questionnaire relating to aspects of board performance.

From this process, the Australia Post board identifies its strengths and weaknesses and agrees on a course of action to deal with any weaknesses.

- 4.43 A rigorous performance appraisal system, in association with identified incentives, will help develop a competitive and performance oriented culture in GBE boards. Greater focus on board and individual director performance will help to enhance corporate governance and, consequently, the achievement of corporate objectives. Therefore, the Committee recommends that the Minister for Finance and Administration amend Part 3 of the *1997 Governance Arrangements for Commonwealth GBEs* to include a section requiring board and director performance appraisal. All GBEs will be expected to comply with the new arrangements. The results of any performance appraisal should remain confidential between boards and their shareholder Minister(s).
- 4.44 The Committee acknowledges that developing an appropriate performance appraisal system for GBE boards and directors is complicated. GBE boards should develop their own performance appraisal systems which should be submitted to the Minister for Finance and Administration for approval.
- 4.45 The Committee, in proposing that GBE boards be subject to performance appraisal, acknowledges that there may be differences between private and public sector boards. BDW indicated that government enterprises may, but should not necessarily, measure performance in terms of financial return. For example, public sector boards are often concerned with maximising the generation of public benefit and meeting the political and bureaucratic expectations of Ministers. Therefore, the development of a performance appraisal system for GBE boards should take individual circumstances into account.
- 4.46 The Committee in recommending GBE board performance appraisal must deal with the view that this could lead to increased risk averse behaviour. First, GBE boards may become more risk averse. Second, the increased accountability placed on boards and individual directors may create a disincentive for applicants to stand for board selection. The Committee's intentions are completely the opposite. The Committee is seeking to create an environment in which GBE boards strive for above average performance taking account of risk.

- 4.47 The Committee acknowledges that there are differences between government and private boards and that this must be taken into account when developing suitable performance appraisal systems. At the same time, the Committee is taking a responsible position by proposing that GBE boards develop their own performance appraisal systems as they are in the best position to do so.

#### **Recommendation 4**

- 4.48 **That the Minister for Finance and Administration amend Part 3 of the *1997 Governance Arrangements for Commonwealth GBEs* to include a requirement that GBE boards ensure that there are appropriate and effective induction, education and training programs offered to new and existing board directors.**

#### **Recommendation 5**

- 4.49 **That the Minister for Finance and Administration amend Part 3 of the *1997 Governance Arrangements for Commonwealth GBEs* to include a section requiring confidential board and director performance appraisal. All GBEs will be expected to comply with the new arrangements.**