

# KEY IMPLICATIONS FOR NFPs

Royal Commissions set the  
scene of what Australia  
expects from its institutions

The image features the letters 'MMO' in a large, bold, sans-serif font. The 'M' and the first 'O' are dark grey, while the second 'O' is a bright blue ring. The letters are positioned on the right side of the page, partially overlapping a light blue vertical bar that runs down the left side of the page.

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MAY 2020**

This paper has been prepared by the legal specialists of Mills Oakley's Not for Profit and Charities team. It examines the findings of four recent royal commissions undertaken by the federal government of Australia since 2013, and the outcome of an important and recent case.

The purpose of this paper is to provide Australian Not for Profits (**NFPs**) with a practical guide for identifying and approaching risks in the management of their organisations.

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**May 2020**

## *Summary: Key Implications For NFPs*

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1. Organisational culture should encourage proper standards and discourage misconduct. This is an obligation of the board of directors and senior management.
2. Remuneration packages for directors can also consider whether the interests of beneficiaries have been prioritised and whether ethical standards have been complied with. These measures also apply for disciplinary consequences for directors.
3. The regulators and judiciary have grounds to intervene when culture fails and the organisation itself or a third party has suffered as a result.
4. Individual senior decision-makers can be held accountable for past decisions.
5. A NFP can transform the culture of its organisation by adopting a customer-centric model.
6. Boards should review their constitutions to ensure that they set and reflect the cultural expectations of the members, the directors and the organisations.
7. NFPs require robust complaint handling procedures with clear lines of responsibility that are overseen by the board.
8. NFPs must have risk systems that prevent harm occurring. These risk systems should specifically cover the safety of groups of people who may interact with the NFP, such as volunteers, beneficiaries and children.
9. Defendable evidence is needed as to how beneficiaries are prioritised first, ahead of the NFP's needs. Past and current records management should be sufficient and transparent.
10. The assessment of culture is an essential part of regulator supervision and cannot be seen as merely a supervisory "add-on".
11. Law reform will occur to encourage an organisational culture in line with intent of the law, not merely box-ticking. The standard that NFPs ought to operate by is what the public would expect of them.

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## Introduction

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In Australia, the royal commission is the highest form of inquiry on matters of public significance. Defined under their own statute, royal commissions are independent government inquiries that possess broad coercive powers that can compel individuals and entities to participate in the inquiries.

### Four Royal Commissions



This paper focuses on the common findings on institutional culture and governance in the two most recently completed royal commissions. Completed in 2017, the Royal Commission into Institutional Responses to Child Sexual Abuse (**Child Sexual Abuse Royal Commission**) released its final report on the causes of child sexual abuse and the weaknesses of the responses to child sexual abuse in institutional settings such as schools and churches. In 2019, the final report on the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Banking Royal Commission**) criticised Australian corporations for their greed, with that royal commission focusing on lenders, superannuation funds and other financial service providers.

Within relationships marked by power imbalances, Australian institutions have repeatedly failed to prevent or respond appropriately to misconduct.

Not only did the royal commissions reveal past wrongdoings and make recommendations for redress and improvement, the inquiries ultimately revealed the standard of behaviour that Australia expects from its institutions.

Two royal commissions are ongoing. The Royal Commission into Aged Care Quality and Safety (**Aged Care Royal Commission**) and the Royal Commission into Violence, Abuse, Neglect and Exploitation of People with Disability (**Disability Royal Commission**) have taken a similar route in exposing poor culture and governance practices, only with different types of institutions in their scope.

## I. Culture is the Root of Misconduct

*“[C]ulture, governance and remuneration. Each of those words can provoke a torrent of clichés. Each can provoke serious debate about definition. But there is no other vocabulary available to discuss issues that lie at the centre of what has happened in Australia’s financial services entities and with which this Report must deal.”<sup>1</sup>*

*- Commissioner Hayne, Banking Royal Commission Final Report*

If the findings from the Banking Royal Commission and the Child Sexual Abuse Royal Commission were to be summarised, it would be that culture is the root of misconduct.

In both royal commissions, the features of institutional culture that enabled misconduct were:

1. the prioritisation of the interests of the organisation or the individuals in positions of power, above the interests of the organisation’s customer (such as the beneficiary, client or child);
2. the lack of integrity and defensibility in decision-making;
3. poor attitudes, practices and behaviours towards the management of non-financial risk; and
4. remuneration models that reward individuals solely based on financial results, rather than the means taken to achieve those financial results.

### **1. Cultural failings – Banking Royal Commission**

The Banking Royal Commission exposed financial institutions for billing customers for no service, charging premiums to the dead, increasing credit for gambling addicts and even taking cash bribes. Commissioner Hayne stated that in almost every case of appalling misconduct, actions were “driven not only by the relevant entity’s pursuit of profit, but also by individuals’ pursuit of gain”.<sup>2</sup> In the corporate structure, success was measured by total shareholder return. In turn, the board of directors were rewarded with large bonuses if the organisation met certain profit targets. This remuneration model trickled down to operational staff, by a model of commissions and bonuses that was measured by sales.

Whilst such remuneration models do not necessarily cause non-compliance with the law, decision-making at every level in the financial services industry had become polluted by considerations of personal gain. When coupled with governance structures that did not adequately hold decision-makers accountable to considering the customer’s best interests or how non-financial risks were managed, the financial services industry gave itself the licence to act out of greed.

### **2. Cultural failings – Child Sexual Abuse Royal Commission**

The Child Sexual Abuse Royal Commission<sup>3</sup> reviewed a very different type of institution for a very different type of misconduct – child sexual abuse in religious bodies, schools, out-of-home care organisations, sporting and other recreational groups and detention environments. Whilst it is the perpetrator of child sexual abuse who is ultimately at fault, cultural, operational and environmental factors within institutions can all affect the likelihood of children being sexually abused.

Cultural norms within an institution influence how individuals’ value and interact with children. In its case studies,<sup>4</sup> the Child Sexual Abuse Royal Commission identified cultural risk factors that contributed to the failure to prevent or respond adequately to child sexual abuse. These included the failure to recognise children as credible sources, and the prioritisation of the

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<sup>1</sup> *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 334.

<sup>2</sup> *Ibid* 1.

<sup>3</sup> *Royal Commission into Institutional Responses to Child Sexual Abuse* (Final Report, December 2017) vol 1.

<sup>4</sup> *Royal Commission into Institutional Responses to Child Sexual Abuse* (Final Report, December 2017) vol 2 16.

reputation of an institution over the safety and wellbeing of children. Some case studies<sup>5</sup> found that in some institutions, child sexual abuse was perceived to only be a mere moral failing that did not warrant a police report, but only repentance.

Operational risk factors arose out of governance structures, such as the approach taken to recruit, screen, train and monitor staff and volunteers, and a lack of oversight over authority figures.

Environmental risk factors included access to children in isolated or unsupervised locations, and the use of online environments to groom and abuse children.

### **3. Cultural failings – Aged Care Royal Commission**

The Interim Report<sup>6</sup> from the Aged Care Royal Commission was released on 31 October 2019, summarising a year's worth of consultation and case studies that revealed a prolific neglect of elderly people by the aged care sector. Entitled "A Shocking Tale of Neglect", the Interim Report raises quality and safety issues in service delivery that is compromised by the prioritisation of financial gain. The Interim Report describes care providers as being immersed in a "culture of apathy".<sup>7</sup> This is an apt term to describe the culture of valuing elderly individuals by the funding they can attract, providing impersonalised services to save costs, and striving to only achieve minimum standards of care. Care providers have been criticised for failing to provide "consumer-directed"<sup>8</sup> care that is reactive to the needs of each individual.

Amongst the other issues which have been identified, the Aged Care Royal Commission so far has noted:

- a lack of oversight caused by ineffective review systems for boards and senior management to be able to detect, understand and rectify issues experienced by people in their care;
- complaints systems that are difficult to access;
- when complaints were made, they were oftentimes either ignored or not transparently communicated to senior decision-makers; and
- a structural failing exemplified by issues including a systemic lack of compliance with regulatory standards, governance structures that look good on paper but are not implemented in practice, the infrequency of audits, and a lack of experience relevant to the industry on boards of care providers.

The Interim Report describes the structure of the current system projecting itself as a "market"<sup>9</sup> that can competitively offer choice of aged care services to its consumers. The reality is different to its appearance. Many older people are not in the position to meaningfully negotiate prices, services or care standards, and the "market" has instead meant that care providers have employed cost-cutting financial models to increase their own profit margins, rather than increasing the quality of their care.

Such cost minimisation strategies have resulted in substandard care quality, by practices such as employing under-qualified individuals who are paid at minimum wages, and providing substandard resources to residents.

The immediate response to the Interim Report has been the implementation of new Aged Care Quality Standards that seek to establish robust organisational culture of diligent and authentic service quality and safety.

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<sup>5</sup> *Royal Commission into Institutional Responses to Child Sexual Abuse* (Final Report, December 2017) Preface and executive summary 6.

<sup>6</sup> *Royal Commission into Aged Care Quality and Safety* (Interim Report, October 2019).

<sup>7</sup> *Ibid* 1.

<sup>8</sup> *Ibid* 10.

<sup>9</sup> *Ibid* 9.

#### **4. Cultural failings – from the hearings to date in the Disability Royal Commission**

Between July and September 2018, the National Disability Insurance Scheme's (NDIS) Quality and Safeguards Commission reported over 184 incidents of abuse and neglect, 62 reports of unexpected deaths, 91 injuries, 34 complaints against individual staff or service and 75 cases of authorised restrictive practices. These incidents were across service providers in aged care, educational institutions, hospitals, corrective services, and within the disability sector.

In light of the growing attention on reports of abuse, neglect, unexpected deaths and injuries experienced by persons with disabilities in institutional settings, the Disability Royal Commission was announced on 5 April 2019.

Led by Commissioner Roslyn Atkinson, former Queensland Supreme Court Judge and President of the Queensland Anti-Discrimination Tribunal, the Disability Royal Commission has broad-sweeping authority to inquire into all forms of violence, abuse, neglect and exploitation in all settings and contexts. The Disability Royal Commission has extensive powers to compel people or organisations to produce documents and give evidence.

Hearings are currently underway, having commenced on 16 September 2019. NDIS providers can expect that the Commission will soon issue notices to produce documents into past complaints and investigations. Community forums have commenced, and submissions are now open for the public to have their voices heard and hear the work of the Royal Commission.

It is projected that the Disability Royal Commission will run for three years, with the Commissioner's interim report due on 30 October 2020, and her final report due on 29 April 2022.

## **II. Implications for NFPs**

### **1. Boards and senior management must review their culture**

#### **(a) Culture is the responsibility of the board and senior management**

The term "organisational culture" is often used to connote vague notions of values and norms that shape behaviours and mindsets. "Culture" can be understood as an organisation's governance structures and the values it embodies which drive how an organisation operates.

The Banking Royal Commission was scathing towards boards and senior management, stating that cultural failings of an organisation started from the top. Commissioner Hayne found that the primary responsibility for misconduct in the financial services industry must lie with boards and senior management.<sup>10</sup> Governance is not limited to questions of risk management, but broadly encapsulates how and by whom decisions are made, and the values or norms that decisions reflect. Culture must be set by the top, echoed to the bottom and reinforced at every level.

In his final report, Commissioner Hayne is clear. *Every* financial services entity must review its culture. *Every* financial services entity must look again at the way in which it governs itself, manages its employees, and manages any of its intermediaries. The board and senior management must give close attention to the connections between compensation, incentive and remuneration practices, and regulatory, compliance and conduct risks.

To diagnose its culture, the questions that Commissioner Hayne requires every board of a financial services entity to ask itself are:

- *"Is there adequate oversight and challenge by the board and its gatekeeper committees of emerging non-financial risks?"*
- *Is it clear who is accountable for risks and how they are to be held accountable?"*

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<sup>10</sup> *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 4.

- *Are issues, incidents and risks identified quickly, referred up the management chain, and then managed and resolved urgently? Or is bureaucracy getting in the way?*
- *Is enough attention being given to compliance? Is it working in practice? Or is it just ‘box-ticking’?*
- *Do compensation, incentive or remuneration practices recognise and penalise poor conduct? How does the remuneration framework apply when there are poor risk outcomes or there are poor customer outcomes? Do senior managers and above feel the sting?”<sup>11</sup>*

Whilst the Child Sexual Abuse Royal Commission did not deliver such similar scathing remarks towards the institutions under its inquiry, the report does not shy away from similarly placing responsibility on boards for failing to install preventative measures and adequately investigate and respond to complaints of child sexual abuse.

With responsibility firmly placed on the board to foster organisational culture that cares for and protects the vulnerable, the final report made it clear that silence or inaction from senior management were active choices.

Although employees and boards of NFPs may not be measured by profit margins as in the financial services industry, senior management must ensure both compliance with proper standards, and implementation of effective governance structures that reflect the values of the organisation. For NFPs and charities, these values may include:

- beneficiaries first;
- defensibility in decision-making; and
- integrity and accountability.

Organisational reputation must be secondary to care and justice for the beneficiary, and this must be reflected in how decisions are made.

NFPs must actively hold their senior management to such standards, and be quick to implement practical consequences. This can be done by using remuneration packages to incentivise risk compliance and robust governance structures, or by disciplinary mechanisms such as removing board members if they do not meet the legal and ethical standards that their beneficiaries and contributors expect of them.<sup>12</sup>

### **(b) Regulators and the judiciary have grounds to intervene**

Whilst courts and regulators are not likely to use the words “cultural failings” when prosecuting individuals and entities for breaches of their duties, both the regulators and the judiciary have grounds to hold individuals and entities to account where governance systems have not been managed properly and the organisation itself or a third party has suffered as a result.

Officers in companies which are NFPs (but are not charities) are generally bound by directors’ duties outlined in the *Corporations Act 2001* (Cth). For example, section 180(1) of the *Corporation Act 2001* (Cth) requires officers to exercise their powers with care and diligence that would be reasonably expected of them. Section 181 requires officers to act honestly in the best interests of their organisation and its purposes. Officers in incorporated associations are subject to similar legal duties.

<sup>11</sup> CBA Prudential Inquiry, Final Report, 3, cited in *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 333–4.

<sup>12</sup> Given the legal difficulty which may arise in relation to removing board members before the expiry of their board terms, this mandate may require NFPs to become creative in how they draft their constitutions and other governance documents to provide for the legal possibility of removing directors in such circumstances.

In relation to charities, duties are largely imposed by the Australian Charities and Not for Profits Commission (**ACNC**) Governance Standards.<sup>13</sup> The Governance Standards are very similar to the directors' duties found in the *Corporations Act 2001* (Cth).

Officers should be aware that they can be held accountable for past decisions (sometimes by previous officers).

By virtue of these legislative provisions, both the judiciary and the regulators can hold officers accountable for implementing governance structures in their organisations which do not encourage law-compliant behaviour by themselves and their staff.

### **(c) A customer-centric cultural transformation**

The key cultural shortcoming identified in the royal commissions examined by this paper is that institutions have repeatedly prioritised the interests of the organisations and their senior management over the interests of the target of their services.

These royal commissions call for customer-centric models to transform the culture of Australian institutions.

Customer-centricity involves shifting the lens through which the organisation is understood. The “customer” for every organisation is different. Whilst the “customer” is often defined as the recipient of the service that an organisation provides, this is not always necessarily the case. It could be other key stakeholders that the organisation is established to benefit, such as funders, paying customers, members or beneficiaries. Instead of viewing the organisation through the lens of the goods or services it provides, a customer-centric model shifts this focal point to identifying the organisation's target customers, and the problem the organisation is seeking to solve for them. It involves taking the customer perspective into the very architecture of an organisation, such as the organisation's constitution, governance structures and remuneration models.

For an NFP, the objects, purposes, mission and values of an organisation should be customer-centric and be demonstrated throughout its key documents and in internal cultural rhetoric.

- 1. A cultural transformation must start with revisiting who the intended beneficiary is of the NFP, and what values the organisation espouses to solve its identified problem.**
2. Once this is identified, the next step would be to **revisit the governing documents** of the organisation and the remuneration model it provides for senior management and consider whether it currently promotes the customer. For example, a clear identification of the customer and the purpose of the organisation are key in an organisation's constitution (especially in the objects clause). Key performance indicators for employees can also be used to include measures of the customer experience.
3. NFPs should then integrate active language of how the customer is benefited in other documents, such as value statements, by-laws, annual reports, business plans, and internal policies and codes.
4. NFPs should similarly **review how they make decisions** and involve the customer's input in their decision-making structures. This can involve asking and receiving feedback, holding consultations, including customer representatives on committees, and providing an effective complaints mechanism.

A governance structure that embodies the value of customer-centricity means that the staff have clear values to guide their decision-making, and the board oversees the consideration of the customer's satisfaction in its reviews of those staff members and their decisions.

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<sup>13</sup> See *Australian Charities and Not-for-profits Commission Regulation 2013* (Cth) r 45.25.

### **Key implications for NFPs:**

1. Organisational culture should encourage proper standards and discourage misconduct. This is an obligation of the board of directors and senior management.
2. Remuneration packages for directors can also consider whether the interests of beneficiaries have been prioritised and whether ethical standards have been complied with. These measures also apply for disciplinary consequences for directors.<sup>14</sup>
3. The regulators and judiciary have grounds to intervene when culture fails and the organisation itself or a third party has suffered as a result.
4. Individual senior decision-makers can be held accountable for past decisions.
5. A NFP can transform the culture of its organisation by adopting a customer-centric model.

## **2. Good culture means strong governance structures**

*“Governance refers to the entirety of structures and processes by which an entity is run. By shaping how the business is run, governance shapes culture.”<sup>15</sup>*

*- Commissioner Hayne, Banking Royal Commission Final Report*

This paper highlights below four key governance structures that can cement appropriate values and foster good cultural practices within institutions.

### **(a) An effective constitution**

An organisation’s constitution is the cornerstone document that sets the tone for an organisation’s culture. The constitution effectively operates as a contract binding the organisation with the board and its members, and prescribes the procedure for making significant decisions.

Governance must start from the top. To quote an old saying, “a fish rots from the head”. Governance starts with the structures that encourage and enhance the ability of the most senior decision-makers to make decisions which are in the best interests of the organisation. The constitution requires careful thought and precision in drafting, and should cover the following grounds:

1. what the organisation’s purpose is (and, as already mentioned in the section on customer-centricity above, who its intended beneficiaries are);
2. the relationship between the organisation, the board and the members (if any);
3. how decisions are made by the board;
4. how decisions are made by the members (if any);
5. how directors on the board are appointed, elected and removed; and
6. how directors on the board are remunerated and by which measures they are judged (if any).

The Final Report of the Banking Royal Commission stressed that the first step in overhauling the current corporate culture of institutions must be to review the models of remuneration and benefits of directors. Remuneration both shapes and reflects culture. People do what is valued and rewarded by the entity.

<sup>14</sup> We note that it is not yet widespread practice for NFPs to remunerate their directors. We further note that it is not yet common for NFPs to enact disciplinary consequences for misbehaving directors. This is due in some part to the legal difficulties which prohibit such discipline.

<sup>15</sup> *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 334.

For those NFPs that remunerate their directors, the NFPs must consider how their boards are remunerated and consider placing standards that measure compliance with the law and the management of non-financial risk, in addition to other outcomes. This must be supported by adequate disciplinary measures, such as the removal of directors from the board.<sup>16</sup>

### **(b) Risk management systems**

Within the purview of the board and senior management must be an adequate oversight of the risks in the organisation and the consideration of emerging risks. The board is ultimately responsible for the effectiveness of risk management systems, and should ensure a system is in place where risks are escalated to board-level meetings, and reviewed accordingly.

Beyond the constitution, robust risk management systems must be implemented to guide decision-making and prevent and respond to different categories of risk. The board and senior management must ensure that there are systems that reflect the purposes and values expressed by the organisation's constitution, that staff are appropriately trained, and that ongoing supervision occurs to ensure that these systems are followed and are current and effective. Risk management systems ought to be documented clearly, be accessible by the relevant members of staff, and have clear lines of accountability and responsibility.

A NFP must assess what financial and non-financial risks are relevant for its entity.

For NFPs, examples of areas where robust risk management systems may be required are:

- child safety plans for organisations that work with children;
- volunteer management;
- financial controls on how money is receipted and spent by the organisation;
- management of donor funds; and
- bullying, sexual harassment and whistleblower policies.

Risk management systems should be in accordance with law and policy, be supported by a robust complaint handling framework, and adhere to transparent and defensible records management.

### **(c) Complaints handling**

One of the major failures also raised by the Child Sexual Abuse Royal Commission was how complaints were handled. Not only were there major barriers for victims to make complaints of child sexual abuse, but some institutions investigated and responded poorly to complaints. Many reasons for these failures were raised in the final report, from internal cultural factors specific to the institution to systemic faults in the law's reporting schemes.

Complaints handling policies and procedures should cover:

1. how staff, volunteers and the public can make complaints;
2. how staff respond to complaints;
3. how staff investigate complaints;
4. how to provide support and assistance to the complainant; and
5. how the organisation achieves systematic improvements following a complaint.

Organisations must educate their staff about when to escalate complaints to appropriate government authorities, even when there are no mandatory reporting requirements.

The Child Sexual Abuse Royal Commission has since required institutions to draw clear guidelines on how they are responding to problems that cause the under-reporting of institutional child sexual abuse to police and government child protection agencies.

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<sup>16</sup> Please see our previous comment about the difficulty in removing directors from boards.

A complaint handling policy should clearly provide guidance for staff on what must be reported to government authorities, how to be sensitive to the culture and physical barriers that face children complainants, and at what stage of a complaint a report must be made to an external authority. This must be supplemented by continual training and education.

**(d) Defensible and transparent records handling**

A common theme of the royal commissions was the strengthening of the powers of the regulators, and the push towards greater oversight of institutions. Defendable evidence is needed as to how institutions have put beneficiaries first, ahead of ulterior interests.

Governance structures and processes ought to be supported by defensible and transparent records handling that record clearly how and why decisions have been made, who has approved the decisions, and what actions were taken. Particularly in the case of personal data and complaints, records management must also be robust to protect privacy. Designated levels of information access and information channels ought to be set up by senior management, facilitated with the use of technology with systems and data storage methods. Five high-level principles for records and recordkeeping, drawn from the principles for records and recordkeeping for risks relating to child safety and wellbeing in the final report for the Child Sexual Abuse Royal Commission, are:<sup>17</sup>

1. creating and keeping full and accurate records relevant to risk management should be an integral part of institutional leadership, governance and culture;
2. full and accurate records should be created about all incidents, responses and decisions;
3. records should be maintained appropriately;
4. records should only be disposed of in accordance with law or policy, where applicable; and
5. individuals' existing rights to access, amend or annotate records about themselves should be recognised to the fullest extent.

***Key implications for NFPs:***

1. Boards should review their constitutions to ensure that they set and reflect the cultural expectations of the members, the directors and the organisations.
2. NFPs require robust complaint handling procedures with clear lines of responsibility that are overseen by the board.
3. NFPs must have risk systems that prevent harm occurring. These risk systems should specifically cover the safety of groups of people who may interact with the NFP, such as volunteers, beneficiaries and children.
4. Defendable evidence is needed as to how beneficiaries are prioritised first, ahead of the NFP's needs. Past and current records management should be sufficient and transparent.

***3. Law reform will set higher standards to reach community expectation***

The royal commissions have pushed for more active regulators that do more than encourage their institutions to voluntarily comply with the law. Regulators are being encouraged to use the full coercive effect of the law to create a strict standard for organisations to comply with all the laws that apply to them, not just with those parts of the law that they find to be commercially acceptable.

The Banking Royal Commission has been described as a “wake up call” for corporate regulators to change their approach on how they enforce the law and regulate the financial

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<sup>17</sup> *Royal Commission into Institutional Responses to Child Sexual Abuse* (Final Report, December 2017) vol 8, 22–3.

services industry, including the Australian Securities and Investments Commission (**ASIC**) and the Australian Prudential Regulation Authority (**APRA**).<sup>18</sup>

Commissioner Hayne has made a series of law reform recommendations, including the creation of an external body to oversee APRA and ASIC, and for ASIC to use court action as the starting point for holding entities and officers to account. The Banking Royal Commission has also made specific recommendations for law reform to shift corporate culture, including requiring mortgage brokers to act in the best interests of the borrower, and limiting commissions for financial services providers which are selling insurance packages.

Similarly, the Child Sexual Abuse Royal Commission has recommended an independent oversight body in each state and territory, which would be responsible for monitoring and enforcing the Child Safe Standards.

Regulators must have the resources to not only encourage voluntary compliance with the law, but to supervise culture and also punish individual acts of misconduct by holding decision-makers to account. We are likely to see a greater call for increased funding for regulators and for more active use of their wider powers.

For directors' duties, the court's interpretation of open-ended language such as "reasonable" and "best interests" can bring the assessment of an institution's culture (by the management of governance structures and processes) under review.

The royal commissions have raised an expectation that the law will continually shift towards requiring institutions to have culture in line with the *purpose* of the law, rather than a culture towards compliance by mere box-ticking.

#### **Key implications for NFPs:**

1. The assessment of culture is an essential part of regulator supervision and cannot be seen as merely a supervisory "add-on".
2. Law reform will occur to encourage an organisational culture in line with intent of the law, not merely box-ticking. The standard that NFPs ought to operate by is what the public would expect of them.

### **III. A case study: The cultural failings of the Returned Services League**

Entities under the umbrella of the Returned Services League (**RSL**) NSW have been under scrutiny from the ACNC since 2016. In 2017, it was discovered that the NSW RSL president at the time, Don Rowe, had spent \$465,376 on personal expenses from his corporate credit card between 2009 and 2014, including \$213,000 on cash withdrawals. Rowe also enabled his son to stay, rent-free, in RSL-owned accommodation in the Sydney CBD for seven years.

"The shameful and disgraceful behaviour of former president Don Rowe and the culture which allowed him to get away with it"<sup>19</sup> instigated a year-long independent inquiry into the fundraising activities of RSL NSW, RSL Welfare Benevolent Institution and RSL LifeCare led by former Supreme Court Judge, Patricia Bergin. The Report of the Inquiry under the *Charitable Fundraising Act 1991* (NSW) (the **Bergin Inquiry**) was released by the NSW State Government on 31 January 2018.

The report acknowledged that it can be hard to believe that the President of RSL NSW could have misused funds across six years and then resign from the Presidential role with accolades and well-wishes from members and the public. The report from the Bergin Inquiry revealed poor governance practices and a culture that fostered and entrenched the ability to misuse funds without accountability.

<sup>18</sup> 'Banking royal commission to have 'monumental impact', say experts', *University of Sydney News & Opinion* (online, 1 February 2019) <<https://sydney.edu.au/news-opinion/news/2019/02/01/banking-royal-commission-to-have-monumental-impact--say-experts.html>>.

<sup>19</sup> Minister for Better Regulation, Matt Kean.

Among other findings, the report described the characteristics of the cultural failings of the RSL NSW:

- From the recent external assessments and evidence at the Bergin Inquiry, it was clear that the financial systems and records that were in place were inadequate and there was a complete lack of rigour from the finance department in checking the spending of the President.
- There was a failure to comply with the *Charitable Fundraising Act 1991* (NSW) by the approval and substantial remuneration and allowances given to the directors of RSL LifeCare. Legality was not considered when using the charity's funds to pay directors, staff and others to attend functions linked to the Liberal Party of Australia. This was incompatible with RSL LifeCare's charitable purposes.
- In the decade prior to 2014, there had been no refreshment of the members of the State Executive, who were responsible for the management of the organisation.
- During this decade, the same processes and systems had been stagnant without review and continual improvement. During the same decade RSL NSW had the same legal adviser and the same auditors.
- Those who asked questions about the President's expenses were rebuffed by the CEO with the retort that "a man's got to live". Amongst the findings of the report, this approach was consistent with a culture of not questioning superiors and a widespread belief that the President would do the right thing.
- There was a totally inadequate regime in the finance department for checking and/or approving the President's expenses. No one appeared to have recognised the absurdity of having the President approve his own expenses.
- There was an absence of notes and minutes taken for conversations and meetings that involved significant decisions. During the Bergin Inquiry, much of the evidence from some directors were solely from memory.
- When the State Council became aware of Mr Rowe's misuse of funds, it failed to properly investigate and did not report the allegations to the police. Instead, the State Council provided Mr Rowe with the option of resigning rather than undergoing an investigation. When Mr Rowe resigned, the State Council made misleading statements regarding the circumstances of the resignation by indicating that it was due to health reasons.
- This was then supported by the intervention of people with significant clout in the organisation urging the State Council to hide the internal investigation from police and the public. This was done through rhetoric towards the State Council to be "be generous" and to think of "the good name of the RSL" and the "bigger picture".

Based on the findings, the report set up RSL NSW for disciplinary consequences. This included:

- the suspension of RSL NSW's capacity to fundraise;
- the referral of Dan Rowe and 13 other directors to the police, ASIC and ACNC for the misconduct and the cover up of the misconduct; and
- recommendations for reform of the charitable fundraising framework that would affect other charities.

In February 2020, Dan Rowe was found guilty of two counts of dishonestly obtaining a financial advantage by deception for his misuse of RSL NSW's credit card.<sup>20</sup> He was sentenced in April 2020 and was placed on a two-year community corrections order, in addition to receiving a fine of \$2,000. In her judgement, Magistrate Atkinson condemned Dan Rowe's exploitation of the position

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<sup>20</sup> Alison Xiao, 'Former NSW RSL president Don Rowe found guilty of misappropriating funds', *ABC News* (online, 28 February 2020) <<https://www.abc.net.au/news/2020-02-28/magistrate-finds-former-rsl-president-don-rowe-guilty/12010870>>.

of trust he was in as president of the RSL, and made explicit the power of the court to re-sentence Mr Rowe should he reappear before the court for any other matter.<sup>21</sup>

After the resignation of Dan Rowe, James Brown took over the presidency role at RSL NSW in May 2017, a few days after the Bergin Inquiry was announced. The past two years have seen him rebuilding the culture of the RSL NSW by addressing numerous governance issues and reforming the entity's constitution. His efforts to overhaul the management and governance structures of RSL NSW ultimately seek to restore public trust in the once reputable organisation. James Brown has since become successful with having the fundraising ban lifted, but remains in the process of achieving consensus for a new constitution that re-establishes the framework underpinning RSL NSW.

## Conclusion

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The royal commissions lament that institutional culture has prioritised the interests of the organisation over the interests of its customer. This is characterised by many decisions made over time both by senior and front-line decision-makers that have ultimately chosen to ignore proper governance standards, suppress complaints and incentivise self-seeking behaviour.

NFPs often face the tricky task of maximising their limited resources to reach their beneficiaries whilst simultaneously reinvesting funds into the growth of their organisations.

Because many NFPs concentrate their efforts on their operational purpose (applying funds to beneficiaries), attending to the culture of their organisation and governance of their systems, procedures, employees, management and volunteers is given scant critical regard or may even be overlooked altogether. The findings of the recent royal commissions and NSW RSL case serve to remind NFPs of the heightened risk to their reputation, and to the beneficiaries they serve, if they ignore their own culture and governance.

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<sup>21</sup> Jamie McKinnell, 'Former RSL president Don Rowe fined \$2,000 but avoids jail over credit card fraud', *ABC News* (online, 17 April 2020) <<https://www.abc.net.au/news/2020-04-17/nsw-rsl-president-don-rowe-sentenced-for-fraud-offences/12156880>>.

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*Corporations Act 2001* (Cth)

## About the Authors

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### **Vera Visevic**

Vera is a Partner in the Mills Oakley Not for Profit and Charities team. She has over 25 years' experience in acting for numerous charities, religious and not-for-profit organisations.

Vera provides a full suite of commercial services to not-for-profit clients, including protecting commercial arrangements through drafting services agreements, privacy policies, internal policies and procedures, and reviewing grant and other government agreements.

Her expertise includes:

- assisting not-for-profit clients with organisational restructures, mergers and collaborations, regulatory issues, bequests and estate administration and governance issues, all with a view to help boards function more effectively and in a legally compliant manner;
- advising clients on tax exemptions and endorsements, including charity applications, DGR applications and applications for exemptions from State and Territory land tax, stamp duties and Council rates across Australia;
- advising not-for-profits on regulatory matters including ACNC and State regulator enquiries, charitable fundraising licences, lottery permits and compliance with cemetery and funeral fund laws; and

Vera also has expertise in property law, with over 25 years' experience.

### **Nancy Lee**

Nancy worked as a Paralegal in the Not for Profit and Charities team prior to the completion of her education in law at the University of New South Wales. She now holds a Graduate position as she works towards being admitted to the Supreme Court of New South Wales.

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