

Non-Government Schools Not-For-Profit

Good Governance Principle 4 – Timely and full disclosure of conflicts of interest and related entity transactions

Good governance arrangements ensure school proprietors and boards¹ manage their affairs with suitable oversight and accountability, and are critical for meeting not-for-profit (NFP) obligations under section 83C of the *Education Act 1990 (NSW)* (the Act).

To help schools develop and maintain good governance practices, the Non-Government Schools Not-for-Profit Advisory Committee has developed a set of [Guiding Principles for Good Governance](#).

Good Governance Principle 4: Timely and full disclosures of conflicts of interest and related entity transactions

states that:

'Board members must make sure they make timely and full disclosures of all conflicts of interest and related entities². The proprietor or governing body must ensure there are policies and procedures for managing potential and actual conflicts of interest and related entities, which are properly documented and easily accessible.'

Timely, full and transparent disclosures of conflicts of interest and related entities are crucial for school boards to meet the legal obligations to operate on a NFP basis. The key elements of this principle, outlined in the following sections, are:

- Timely, full and transparent disclosures of conflicts of interest and related entities.
- Policies and procedures to manage conflicts of interest and related entities.

Timely and full disclosures of conflicts of interest and related entities

Conflicts of interest and related entities are a common potential hazard for NFP compliance which can be controlled with good management practices.

Poor management of these transactions can lead to:

- Use of school income and assets that is not for the operation of the school.
- Payment/s for services, property or goods at more than reasonable market value.

The activities above can lead to a school breaching its legal obligation to operate NFP. This may result in compliance action being taken against the school.

Conflicts of interest

Conflicts of interest occur when an individual's personal interests conflict with their responsibility to act in the school's best interests. While this principle relates to board members, it is important to understand that, under the Act, conflicts

¹ 'Proprietors and Boards' refers to all members of the governing body of the school sometimes also referred to as 'directors'. In these documents the governing body is referred to as the 'school board' or 'board members'.

² 'Related entity' refers to any person or legal entity that is related to a proprietor or school either as a result of office, membership, management, control or influence or a personal/familial relationship.

of interest must be managed for all 'responsible persons'³ at the school, not just board members.

'Personal interests' refers to a board member's own interests, interests of their family, friends, or other organisations they are involved with. It also includes a conflict between a member's duty to the school or other roles. Board members should disclose all conflicts of interest.

Conflicts of interest may be unavoidable, so effective management is critical for meeting the school's best interests.

In making full and timely disclosures, school boards should:

- Promote a culture of disclosure.
- Have a conflict of interest policy which is read and understood by all board members.
- Keep an up-to-date conflicts of interest register.
- Add disclosures of conflicts of interest as a standing item for all board meetings.
- Manage all identified conflicts in a timely manner.
- Ensure that all identified conflicts are managed fully and transparently for the duration of the conflict.

Related Entity Transactions

A 'related entity'⁴ means any person or legal entity that is related to a proprietor or school either as a result of office, membership, management, control, influence or a personal/familial relationship. Further details are found in the [Not-for-Profit Guidelines for Non-Government Schools](#).

Schools are required to fully disclose all related entity transactions in an

independently audited related party transaction register. Further details on this requirement are found in the NSW Education Standards Authority (NESA) [Registered and Accredited Individual Non-Government Schools \(NSW\) Manual](#).

Schools may at times be unclear as to what comprises a related entity. If in doubt it is best practice to declare and note the related entity relationship and/or transaction. Schools benefit from considering the need to disclose related entity transactions through the prism of reducing risk and harm to the school. These risks include not acting in the best interest of the school resulting in for-profit activity.

Related entity transactions need to be appropriately disclosed and managed so that they do not lead to for-profit activity. It is crucial that schools ensure terms of the transactions be considered 'arms-length'. Any interested party should be able to access an up-to-date register and schools should ensure its policies and procedures are easily accessible.

Policies and procedures to manage conflicts of interest and related entities

Conflicts of interest

Schools boards should implement policies and procedures to ensure conflicts of interest (actual, potential and perceived)⁵ are properly managed.

An effective conflict of interest policy should include:

- Definitions of actual, perceived or potential conflict of interests.
- A conflict of interest declaration process for all board meetings.

³ The Education Act defines a 'responsible person' as: the proprietor of the school and, if the proprietor is a corporation, each director or person concerned in the management of the school, or a member of the governing body of the school, or the principal of the school.

⁴ The Education Act refers to related entity. A related entity is the same as a related party. A related entity transaction is the same as a related party transaction.

⁵ A real conflict of interest: You are being influenced by a conflicting interest; A perceived conflict of interest: You could be influenced by a conflicting interest; A potential conflict of interest: You could appear to be influenced by a conflicting interest.

- A transparent process for recording conflicts of interest.
 - A plan for the board to manage conflicts of interest if and when they arise. For example:
 - excusing board members from relevant discussions when an actual, potential or perceived conflict is identified
 - board members not voting on matters where they have a conflict of interest.
 - A plan and timeline for reviewing the policy.
- proceed with other options.
 - Abides by all relevant school policies and procedures (that is, procurement, anti-fraud, conflict of interest and/or staff delegation's policies).
 - Implements and documents a plan for the ongoing management of the transaction. A plan that is proportionate to the relationship and transaction, for example, a construction contract as opposed to a stationery contract.
 - Updates and makes readily accessible, the related entities transactions register. The register is also subject to independent audits.

Related entity transactions

Schools should exercise great care when considering entering into a related entity transaction and thoroughly discuss whether or not to go ahead.

Should a school determine it will enter into a transaction with a related entity, it is crucial that the board:

- Demonstrates it obtained independent valuations to ensure reasonable market value.
- Ensures that it negotiated terms as it would for an 'arm's length' transaction (that is, if the parties were independent of one another).
- Document whether or not there were other options, and if so, why it did not

[The Not-for-Profit Guidelines for Non-Government Schools](#) includes detailed information on how schools can manage related entity transactions.

Non-government schools must also meet registration requirements for managing related entity transactions. Details of all registration related requirements can be found in the NSW Education Standards Authority (NESA) [Registered and Accredited Individual Non-Government Schools \(NSW\) Manual](#).

Related entities and related entity transactions are also defined by the Australian Accounting Standards Board (AASB) in its "[Related Party Disclosures](#)".

Case studies

Case study A – Effective management of conflicts of interest and related entity transactions

Building Great Minds is a small regional school. The proprietor of Building Great Minds is Regional Kids Ltd. Regional Kids Ltd does not operate any other businesses or schools and has a small board of 5 members. The school requires a new cleaning contractor, and proposals have been received by the only 2 commercial cleaning companies in town (Bob's Cleaning and Sunshine Cleaning Services). Bob's Cleaning is owned by the brother of the Board Secretary (Secretary).

At the opening of the board meeting, the Chair's first standing order of business is to call for any conflict of interest declarations. The Secretary declares his conflict of interest with the cleaning contract proposal. When the cleaning contract discussion is due to start, the Secretary excuses himself from the decision-making process and leaves the room. Another member acting temporarily as the Secretary records the board member's conflict of interest in the minutes and notes that he left the room.

The services and prices in both proposals are similar. The board papers include a report with independently verified references for both companies. Sunshine Cleaning Services references note a record of not completing the cleaning at times required under contracts.

The Board discuss the 2 bids and decide to award the contract to Bob's Cleaning. The acting Secretary records the reasons for the board's decision in the minutes and updates the related party transaction register to include the cleaning contract.

The Board also agrees to a plan for the ongoing management of the contract that includes the Secretary excusing himself from any involvement in the contract and its discussions, and a signed declaration that he will he not disclose any board discussions to his brother. The Board designates a three-person ad-hoc committee that will manage any strategic decisions relating to the contract and report back to the Board. The day-to-day management of the contract will be done by the school administrative staff.

Shortly after the meeting, the minutes and updated related entity transactions register are emailed to all of the board members so that they can confirm the accuracy of the record.

The Board has practiced effective management of conflict of interests and related entity transactions as the:

- Chair called for declarations of conflict of interests at the start of the meeting.
- Conflicted board member excused themselves from discussion and left the room.
- Conflict of interest was recorded in the board minutes.
- Related entity transaction register was updated to note the related entity relationship between the contractor and the board member.
- The Board implemented a plan for the ongoing management of the contract to ensure no involvement from the conflicted board member.

Case study B – Ineffective management of conflicts of interest and related entities

The proprietor of Happy Kids School is Happy Kids Ltd. Happy Kids Ltd also operates a for-profit child care centre, Sunny Kids Centre. One board manages Happy Kids School and Sunny Kids Centre. The CEO of Sunny Kids Centre, Mr Bear, is also the Chair of the Happy Kids Ltd Board.

Happy Kids School is co-located with Sunny Kids Centre on land owned by Sunny Kids Centre.

The Board does not have strongly embedded disclosure practices as:

- Conflict of interest policy is outdated and not easily accessible to board members.
- Related entity transaction register is not regularly monitored or updated.
- Board members are not expected to abstain from discussions or voting on matters where they have a conflict of interest.
- Board meetings do not require members to make conflict of interest declarations as a standing item.

A recent board meeting included a paper to renew the rental agreement between Happy Kids School and the Sunny Kids Centre. The paper did not include any evidence on independent market valuations of the rental agreement. The Board accepted the new rental price with little discussion.

The Board did not practice appropriate processes for the timely and full disclosure of related entities and conflicts of interest as:

- As a transaction with a related entity, the Board should have ensured it can demonstrate the rental payments are at reasonable market value.
- The Board does not have appropriate conflicts of interest and related entity transaction policies and processes in place.

As the Board did not demonstrate the rental agreement terms were at (or below) reasonable market value, it has potentially breached its NFP obligations. As a Board of 2 entities that have an ongoing significant related entity transaction (that is, the lease of the school site), the Board should have:

- An up-to-date conflict of interest policy that it requires all board members to understand.
- Maintained a related entity transaction register that is up-to-date and easily accessible.
- Ensured that the staff preparing the paper understood the importance of seeking independent advice.
- At least considered creating a subcommittee of members not affiliated with the child care centre to manage and report on the relationship.
- A detailed, well documented plan for rental agreement that focuses on ensuring the transaction is priced and managed in the best interests of the school.

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