boardroom

Magazine of the Institute of Directors in New Zealand

JUNE/JULY 2017

THE BOARD DYNAMICS ISSUE

THE VIEW FROM THE HELICOPTER

Governance lessons from Tony Carter

THE CHALLENGE OF AUTHENTICITY

ETHICAL BUSINESS

Climate change risks | Is governance failing our potential? | Revolution and evolution | Thinking about board dynamics | Reporting to a board

What Matters in board dynamics

Ensuring your board remains successful tomorrow. With resources, development, services and branch events you can help improve your board's awareness and analysis of board and director relationships, board composition, and boardroom ethics.

Resources

The IoD is developing a Practice Guide on CEO succession. IoD Practice Guides on Board Meetings and Conflicts of Interest along with DirectorsBriefs on boardroom conflict and the board's role in talent strategy are available on our website. Getting on board with diversity, is the IoD's guide for getting diverse talent on boards.

In August the 2017 Directors' Fees report, the key source of information on director remuneration trends, will be released.

Development

Mentoring for Diversity pairs experienced directors with board chairs and senior directors for a year; the 2017 intake begins on 1 July. The Future Directors programme provides future directors with an opportunity to sit at the board table of a New Zealand company for a year; boards can join at any time. Our branch network is currently calling for applications for its Emerging Director Awards.

The IoD's online ethics module explores how ethics shape the way you do business. Our webinars on Chairing Fundamentals, Risk agility for SME directors and Risk Trends, facilitate learning at a time that suits you. A course on board dynamics and reporting to a board is being launched shortly.

Branch events

In July, Waikato branch have a function on growth and succession planning, Canterbury branch have a workshop on Informal Influencing Techniques and the Nelson Marlborough branch has John Palmer ONZM reflecting on 30 years as a director. In August in Queenstown, Otago Southland branch has a panel discussion on board dynamics and another on transparency and ethics. In September, Bay of Plenty branch will host a panel discussion on CEO and chair relationships.

Services

Whether establishing a board, recruiting new board members, looking to retain them through the right remuneration or reviewing their performance, the IoD offers a range of services aimed at ensuring boards are the best they can be.

Find out more:
iod.org.nz/whatmatters/boarddynamics

LEADING GOVERNANCE

Institute of Directors

A note from the editor

Following our first themed issue, 'What Matters in digital' in February, this issue looks at board dynamics. Topics in this theme include leadership, ethics, boardroom relationships and CEO succession planning. You will find threads of these issues in articles throughout the magazine.

Thank you to Tony Carter who appears on our cover. On page 12 Tony shares governance lessons gleaned from his career in the cooperative sector and transition from CEO to professional director and board chair. Some IoD members will have been fortunate enough to hear from Tony at branch events or at the 2017 IoD Leadership Conference; we are very pleased to be able to bring those messages further to all BoardRoom readers.

Another speaker who appeared at the Leadership Conference is Harold Hillman, whose moving and heartfelt talk ultimately communicated a very important message about embracing imperfection and being your authentic self. I was lucky enough to attend his talk and hope you find something to take away from the article on page 8.

Emma Sturmfels
BoardRoom Editor

Institute of Directors

Institute of Directors in New Zealand (Inc)
Mezzanine Floor,
50 Customhouse Quay
PO Box 25253, Wellington 6146,
New Zealand
tel: 04 499 0076
fax: 04 499 9488
email: mail@iod.org.nz
www.iod.org.nz

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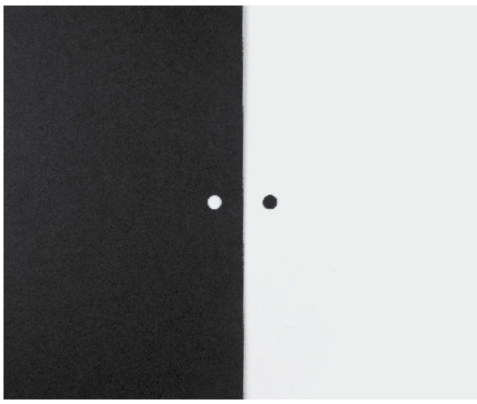

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BoardRoom is designed to inform and stimulate discussion in the director community but opinions expressed in this magazine do not reflect IoD policy unless explicitly stated.

Editor
Emma Sturmfels, 027 536 8062 or email emma.sturmfels@iod.org.nz

Contact the Editor for any advertising queries.

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Institute of Directors in New Zealand (Inc)
Mezzanine Floor, 50 Customhouse Quay,
PO Box 25253, Wellington 6146,
New Zealand Tel: 04 499 0076
Fax: 04 499 9488, Email: mail@iod.org.nz

www.iod.org.nz

Welcome from our new CEO

Tēnā koutou

It's a real honour to have joined the IoD as Chief Executive and I am looking forward to the challenges and opportunities ahead. The organisation has a wonderfully impactful membership and I would like to thank those of you who have already been in touch to express your welcome, your support, and to share your insights of how I can help lead the IoD into the next phase of its development.

This edition of BoardRoom kicks off our second 'What Matters' theme for the year – board dynamics. In these volatile and uncertain times, our businesses and our communities need good governance more than ever. The New Zealand governance community has an essential leadership role to play in creating real and lasting value. Effective board dynamics are an integral part of value creation.

Having previously worked at New Zealand Rugby for some years, I am interested in the connection between team cohesion and team performance that so often plays out in sport. And while sporting analogies are often over used in the New Zealand business context, what is not often fully recognised or understood is governance is in fact a team sport.

That doesn't mean that as a team we all must agree, in fact quite the opposite. However, while we approach the boardroom table as individual players, it is when the entire team comes together that the true benefits and success of effective governance can be unlocked. Ehara taku toa i te toa takitahi, engari he toa takimano – My strength is not that of an individual but that of the collective.

The 2017 Edelman Trust Barometer reports that "trust is in a crisis around the world". The percentage of respondents who rate boards of directors as extremely or very credible has declined 10 points to only 35%. CEOs don't fare much better, with a reduction of 12 points to 37%; an interesting challenge for those of us in leadership roles.

Integral to board dynamics and integral to rebuilding trust is ensuring strong ethical foundations and culture. Like all culture creation we know this is clearly a governance leadership issue that starts from the top.

One of the stand-out speakers at our recent IoD Leadership Conference was UK economist, John Kay, who challenged us to get back to asking questions about what the real purpose of business is, and posed that it should not be a competitive pursuit of individual achievement or ambition. He noted "we have been too long in the hands of people who see leadership as a prize, and not a responsibility."

Thank you for the opportunity to serve and support you as you take on the responsibility to lead New Zealand through the challenges ahead.

Ngā mihi
Kirsten (KP)

Upfront

APPOINTMENTS

The IoD congratulates the following members on these board appointments:

Chartered Fellow John Quirk has been announced as the new chair of Kordia Group board, taking over from Chartered Fellow Lorrain Witten who completed three terms in the role

Chartered Fellow Adrienne Young-Cooper has been appointed to New Plymouth District Council's Audit and Risk Committee and reappointed to the board of NZTA

Chartered Fellow Anthony Beverley has been appointed deputy chair of Property for Industry Ltd

Chartered Member Mark Darrow and Vanessa van Uden have been appointed to the board of NZTA

Chartered Member Grant Lilly has been reappointed to the board of the Civil Aviation Authority

TVNZ has reappointed the following IoD members to the board: Dame Therese Walsh elected chair and Chartered Member Andy Coupe deputy chair, and Julia Raue reappointed to the board

Civil Defence appointed the following IoD members to the newly established Technical Advisory Group: Chartered Member Roger Sowry as Chair; Chartered Member Major General Tim Gall; and Sarah Stuart-Black

Lotteries Commission appointed Chartered Members Matthew Boyd (Presiding Member) and Tony Mossman (Deputy Presiding Member), and Monique Cairns

Superannuation Fund Authority Board appointed Chartered Members Cecilia Tarrant (Chair) and Alison O'Connell, and Shelley Cave

Peter Cowper has been reappointed to the board of Maritime NZ

Phil O' Reilly has been appointed to APEC Business Advisory Council

Bill Osbourne has been elected vice-president of New Zealand Rugby Union

Ben Gilmour has been appointed as a director of business advisory firm, Moore Stephens Markhams Hawkes Bay Ltd.

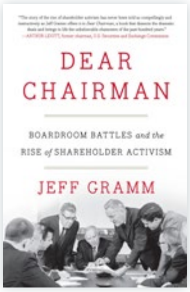
Suzanne Snively has been reappointed to the Health Research Council

Maxine Shortland has been appointed to the Lottery Grants Board

Caren Rangi has been reappointed as Deputy Chair of Creative NZ

Dairy Woman of the Year

Congratulations to Fonterra Shareholders' Councillor Jessie Chan-Dorman, the winner of the 2017 Dairy Woman of the Year award. Jessie is an IoD member and was the Canterbury branch 2014 Aspiring Director Award winner.



Member views

Do you have a view on any of the issues raised in this edition of BoardRoom? We would love to hear your thoughts. Email boardroom@iod.org.nz and you could win a copy of Jeff Gramm's Dear Chairman: Boardroom Battles and the Rise of Shareholder Activism

Annual Report

The 2016 Institute of Directors Annual Report is now available for download at www.iod.org.nz

IoD BY NUMBERS

Did you know that **52% of 2017 Company Directors' Course** attendees have registered interest in sitting the **Chartered Member Assessment?**

If you have completed the CDC and wish to sit the CMA just get in the touch with the membership team, they're here to help. membership@iod.org.nz

2375

members of the IoD are women

888

Chartered Members of the IoD

8281

IoD members

276

Chartered Fellows of the IoD

Numbers correct as at 31 May 2017

The Queen's Birthday honours 2017

The Institute of Directors congratulates the following members who have been appointed to various levels of the New Zealand Order of Merit.

DNZM – Emeritus Professor Peggy Gwendoline **KOOPMAN-BOYDEN**, CNZM, of Hamilton.
For services to seniors.

CNZM – Mr Roy James **AUSTIN**, of Auckland.
For services to children's health and the community.

CNZM – Ms Candis Eileen **CRAVEN**, ONZM, of Auckland.
For services to ballet and business.

CNZM – Mr Angus Lindsay **FERGUSSON** of Auckland.
For services to governance.

CNZM – Professor Peter John **GILLING**, of Tauranga.
For services to Urology.

CNZM – Mrs Lynette Diana **PROVOST**, of Upper Hutt.
For services to the State.

CNZM – Ms Maxine Helen **SIMMONS**, of Auckland.
For services to science, particularly biotechnology.

ONZM – Mr Desmond Albert **ASHTON**, of Blenheim.
For services to the New Zealand Defence Force and aviation.

ONZM – Mr Waihiao Raymond James **GRAY**, JP, of Rotorua.
For services to Māori and governance.

ONZM – Ms Susan Mary **HURIA**, of Auckland.
For services to governance.

MNZM – Mr Stephen Edward **CANNY**, of Invercargill.
For services to the community, governance and cycling.

MNZM – Mr Graham Russell **KENNEDY**, of Ashburton.
For services to business.

MNZM – Mr Rebecca Louise **KEOGHAN**, of Westport.
For services to business, particularly the dairy industry.

Congratulations also go to those who received the Queen's Service Medal.
QSM – Ms Dorothy Margaret **MCKINNON**, of Whanganui.
For services to the community.

For further information visit www.honours.govt.nz

DNZM – Dame Companion of the NZ Order of Merit
CNZM – Companion of the NZ Order of Merit
ONZM – Officer of the NZ Order of Merit
MNZM – Member of the NZ Order of Merit
QSM – The Queen's Service Medal

CPD keeps you ahead, but are you on track?

Check your dashboard now to see how you're tracking.

Your IoD activity is already logged, but did you know you can log any other governance related development.

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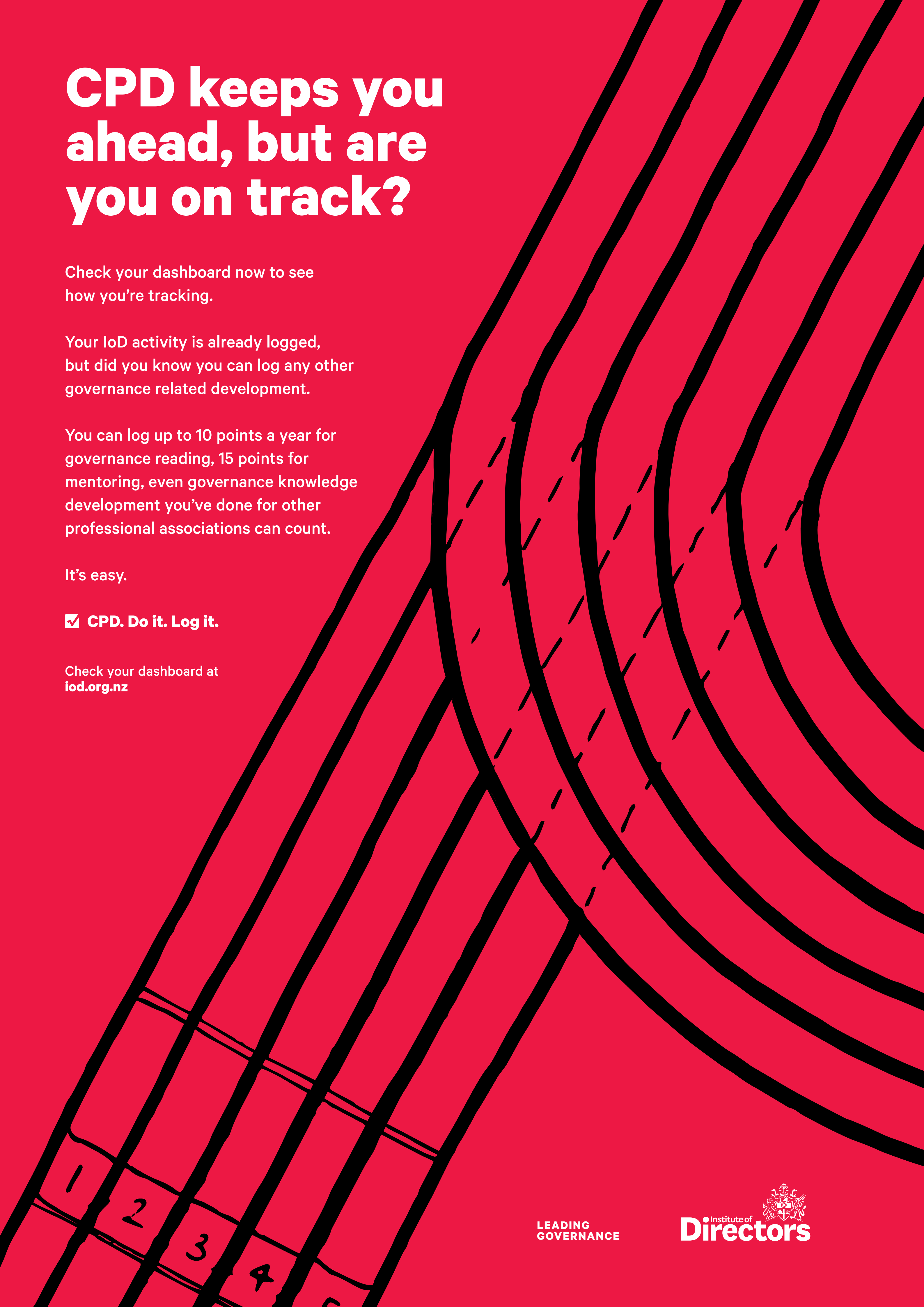
iod.org.nz



LEADING GOVERNANCE

Institute of Directors

INSTITUTE OF DIRECTORS

A Change in Leadership

The Institute of Directors (IoD) has appointed Liz Coutts ONZM, CFInstD as its first female President, and Alan Isaac CNZM, CFInstD as Vice President, at its Annual General Meeting in Auckland on 15 June.

Michael Stiassny

Liz Coutts

Alan Isaac

Mrs Coutts, who was the IoD's first female Vice President, replaces outgoing President Michael Stiassny CFInstD.

The Institute of Directors has and continues to play an important role in supporting director's prepare for tomorrow's challenges.

Mr Stiassny has led the IoD through significant change, and further helped the IoD transform into a modern professional body - increasing its profile, reputation and relevance to aspiring and leading directors.

Both within and outside the IoD, Mr Stiassny has been a driver for change, particularly on diversity.

In 2013 with Des Hunt and Sir Stephen Tindall he established the Future Directors' programme. Last year that expanded into the Public Sector and continues to strengthen New Zealand's director pool, delivering board diversity, new talent and fresh perspectives while developing the next generation of directors.

In 2015 Mr Stiassny was at the helm when the IoD's successful Mentoring for Diversity expanded to promote diversity in the wider sense, including ethnicity, age, skill and experience in addition to gender. He has been a regular mentor of the programme and is a founding member of the 25% Group.

An artificial Intelligence call to action government paper with Chapman Tripp; calling NZX chairs to change the sobering board diversity statistics; providing resources for directors on cyber-risk before they knew they needed it; calling for the establishment of a government lead cyber security centre – this year CERT was created; Governance with a Purpose training programme, developed with the Ministry of Social Development; and governance training course developed with Te Puni Kokiri for iwi and Māori boards and trusts were are just a few of the many achievements the IoD made during his time as President.

The IoD's profile has increased significantly allowing the IoD to speak with a stronger and more influential voice. Membership continues to grow, last year passing 8,000 members.

Mr Stiassny says: "The IoD is in good stead and has accomplished much over the last two years. We live in a dynamic and complex world with globalisation and technology reshaping the business landscape. I leave the IoD in great heart and am excited about its plans to connect, equip and inspire directors in New Zealand business and society to face the challenges and grasp the opportunities of tomorrow.

"Both Liz and Alan will continue to strengthen this strategic priority to meet the needs and expectations of our members."

Mrs Coutts, an IoD Chartered Fellow, was made an Officer of the New Zealand Order of Merit for services to governance in the 2016 Queens Birthday honours. Ms Coutts' extensive board experience includes being Chair of Oceania Healthcare Ltd, Ports of Auckland Ltd, Skellerup Holdings and Urwin &Co Ltd. She has directorships on EBOS Group Ltd, Yellow Pages Group, Sanford Ltd. and Tennis Auckland, and is a member of the Marsh New Zealand Advisory Board.

Mr Isaac is also a Chartered Fellow of the IoD, and a fellow Chartered Accountant. In 2013 New Year's Honours he was made a Companion of the New Zealand Order of Merit for services to cricket and business. Mr Isaac is Chair of the New Zealand Community Trust and McGrathNicol. He has directorships on Opus International Consultants Ltd, Scales Corporation Ltd, Fliway Group Limited, Skellerup Holdings, Oceania Healthcare Ltd, Isaac Advisory Services Ltd, New Zealand Vault Ltd, Murray Capital General Partner Ltd, and the Wellington Free Ambulance.

In the next issue of BoardRoom, we talk to Mrs Coutts about her vision for the IoD.

The challenge of authenticity

When managing the inherent tension between 'fitting in' and 'standing out,' directors face the same challenge as leaders on other teams. Are you bringing your full voice to the board table? BoardRoom attended Harold Hillman's session at the 2017 IoD Leadership Conference to find out more about authenticity in leadership. Here are some of Hillman's lessons on stepping out from behind the mask, learning to be comfortable with showing vulnerability, and embracing imperfection.

Harold Hillman

"I have lived behind the mask," Hillman says, and it's not a place he recommends anyone spend their time.

Hillman's story of living behind the mask is poignant. As a psychologist Hillman applied for a role teaching at the US Air Force Academy, with the intention of completing three years and gaining more experience for his resume. Instead Hillman found his life on a completely different path.

Hillman performed exceptionally in the role, and in 1993 was invited to serve on a government commission to investigate whether the US military's policy of banning homosexual men and women from serving should be overturned. The commission was at the request of President Bill Clinton, and it was considered an honour to be selected. But standing in front of a crowd of 1000 having a medal pinned to his chest in recognition of his service, Hillman did not feel pride, but instead emptiness.

Hillman recalls a question on a form he filled out prior to joining the military with a specific question asking about sexual orientation.

"I was used to lying, but I'd never been asked to sign it. I thought I could just hold my nose for three years. Where was my integrity?"

A decision was made, and an intimate conversation had with his wife. Hillman also spoke to his Commanding Officer, who he considers a great friend to this day. Hillman had hidden his true identity for a long time but could not any longer.

Now open about his sexuality, Hillman knows how difficult it is to show your authentic self, especially if to do so would cause you to stand out from the rest of the group. There is a strong pull towards fitting in, that's just human nature. The challenge for those in leadership positions is to be authentic in your interactions. No stranger to the pressure of the boardroom, Hillman acknowledges that there are certain expectations of directors.

"It's tough inside the tent."

While Hillman takes that phrase from the military, he says it could mean any tent – any organisation; any family; any scenario involving entering a situation where there are certain expectations or ways of behaving.

How many directors have heard the phrase 'you were brought in to think differently, we don't need you to think the same way as everybody else'? With a push towards diversity on boards, there is far more focus on seeking board members who think differently. Hillman argues the intention to be yourself and think differently can be stifled when faced with the inevitable – navigating the social order, or 'how things work around here'.

"You can tell the social order around aesthetics. I made the mistake of going to the Waikato in a pinstripe suit!" Hillman laughs, thinking back on his early experiences in New Zealand with Fonterra.

Thankfully Hillman reports the farmers gave him a lot of latitude and forgiveness. While sometimes it might be necessary to dress down to suit the occasion, the story really shows how easy it can be to feel out of place and feel the need to change something about you to try and fit in. Those in leadership positions are not immune to these feelings.

"Sometimes I work with CEOs who find the social order quite daunting. They're coming in to change the social order and all of a sudden they are changing the way they dress and the way they conduct themselves."

"You would be amazed. Sometimes I work with CEOs who find the social order quite daunting. They're coming in to change the social order and all of a sudden they are changing the way they dress and the way they conduct themselves," Hillman says.

People begin to feel pressured around principle – in this organisation or around this table this is how things are done. It could be as simple as someone finding they are laughing more than they normally would to fit in with a jovial group. But what if, Hillman says, they find themselves laughing at things that they find a little bit offensive because they feel pressure to fit in?

"I'm not talking 21 year olds; I'm talking senior tier people," Hillman stresses. "I make the case that there is a very strong gravitational pull towards fitting in."

Hillman argues that very often the team already sitting there, whether around the board table or the executive team running an organisation, is psychologically wedded to the current way of doing things. It is difficult to come in and change that, and you might instead find your own behaviour changing.

Hillman remembers a friend who was told he had an 'ignorant laugh' because he would snort when he laughed. His manager told him never to laugh during client meetings. Someone who snorts when laughing cannot help it, Hillman explains it is an action connected to the limbic system. To be told not to do this is being instructed to act in a way that is unnatural. Hillman says the request to not laugh is an example of someone being pressured to change their behaviour not on principle but on preference from someone in a leadership position.

"We confuse principle with preference. Sometimes we turn the volume down out of preference. The principle in the US was 'serve your country', the preference was 'do it straight'. And we don't question the preference? Who says?

"Why would we ask someone to turn the volume down? There are always calibrations we make for working with other people, but stop laughing? Don't be so perky? Stop asking questions? Divergent thinkers are naturally inquisitive; when someone tells you 'stop asking so many questions' it goes to the heart of how your brain works. Your question should be 'is that principle or is that preference?'

"A lot of the time, as leaders, we require people to turn the volume down on things that irritate us but don't really have much material impact on the business. That's where leadership is very important because we want in our organisations, people who believe they can bring their whole persona, that's rich and unique, with different aspects of who they are."

Feeling the need to fit in, to work around the preferences of a work place, to behave in a way that is acceptable in the boardroom, in any room, can lead people to behave in crazy ways Hillman says. Doing all of this comes at a cost: loss of authenticity. Ultimately a loss of authenticity means people are unable to connect.

"There is a gravitational pull towards fitting in. But, be careful about lying about who you are because it will catch up with you.

You've turned the volume down on a part of your persona – that isn't sustainable.

"Sometimes the mental models that we wear to the table around who we are and who we are supposed to be, and the pressure we put on ourselves, does break connections. Some people struggle with being wrong, some people need to be in control, some people associate leadership with 'hands on the wheel'. They don't realise that they are breaking connection."

The deep challenge in being yourself, and not a version you think fits with the room you are in or the table you are sitting at, involves acknowledging something that drives a lot of human interaction – vulnerability. Hillman says that too many people are still afraid to show vulnerability, whether they are afraid to be proven wrong or take their hands off of the wheel.

Hillman considers two different personas demonstrated by people trying to protect themselves from vulnerability – the person who hides away in their shell like a turtle, away from attention and avoiding criticism, or at the other extreme, the one who blows up like a blowfish almost challenging anyone to disagree with them.

Hillman has felt it himself in the boardroom. "I could feel the pressure associated with sitting there, I could feel myself blowing up like a blowfish; all of those things that sometimes keep us from being able to connect. It does impact on the quality of learning that goes on at the table."

Usually the reasons for behaving in such a way are to do with pride, status and anxiety, Hillman says, and a sign of discomfort with showing vulnerability. The ability to show vulnerability and to make connections are key qualities in an authentic person and Hillman believes changing the attitude at the board table to one that accepts vulnerability can make a big difference.

"It's about trust – are you comfortable with imperfection? A lot of people struggle with this – they have to be the one with the best idea at the table.

"There is a gravitational pull towards fitting in. But, be careful about lying about who you are because it will catch up with you. You've turned the volume down on a part of your persona – that isn't sustainable."

"Nobody is perfect. If everybody at the table agrees that 'I am not a perfect person' then that shifts the dynamic considerably, because it is hard to connect with a perfect person. Agree that 'I don't need to be right, I don't need to win'.

"I'm glad that a number of boards these days are focused on the quality of relationships, because I'm a firm believer that in the essence of quality conversation and thinking there's got to be a solid foundation of trust at that table. That typically is born from our ability to see each other not as titles and impressive CVs but as real, whole people; people with lives outside of the CV."

What would you offer up if you were not afraid to be wrong? What would you learn about someone else and how might their contributions change if they felt comfortable to offer their opinions in a way that was in line with their personality, annoying laugh and all? In being open, you empower others to do the same and change the conversation that is possible. You cannot expect to mute an aspect of your personality to fit in and get away with it for long. Hillman says we have an inbuilt mechanism that tells us if we are pushing something aside.

"The beautiful thing about your conscience is that it will not let you sleep if there is unfinished business," Hillman says. "It will keep you awake at night asking you 'why am I not putting forward this perspective?

"This question goes to the heart of self-awareness, as a leader and as a person: How perfect do you need to be in an imperfect world? Your answer to this question will either make or break strong connections in your life."

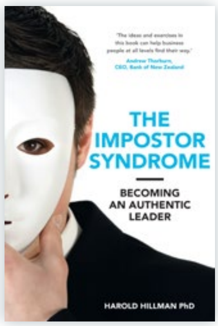
Two questions to ask:

Why should I turn the volume down? Is it the principle or just preference?

How perfect do I need to be in an imperfect world?

READ MORE:

The Impostor Syndrome' and 'Standing out, Fitting In' by Harold Hillman



Board dynamics – what boards need to know

Company performance relies on a well-functioning board but not enough companies are placing effective board dynamics at the top of their priority list, according to experts in the field.

BoardRoom interviewed Associate Professor at the Faculty of Business and Law at AUT University, Coral Ingley, and Meena Thuraisingham, Principal at BoardQ, a Melbourne-based advisory practice working with boards and top teams. Both agreed that board dynamics required greater focus.

They said that while it was generally accepted that board dynamics mattered, there was not enough understanding of how these dynamics actually impacted on decision-making and, ultimately, company performance and shareholder return on investment.

It was this overall lack of understanding of the pervasive influence of board dynamics that inspired Thuraisingham to study the impact of board dynamics on director decision making for her PhD. She found that non-executive directors, while sharing similar beliefs about board accountability for strategy, differed in how each went about exercising this accountability. This led her to believe that there was a social dimension at play.

Thuraisingham set out therefore to study more closely the human dimension to the governing of public corporations. She hoped that it would contribute to a more balanced, fuller understanding of what really goes on when boards contemplate big 'bet the farm' decisions such as acquisitions or divestments.

Her research, based on a group of 15 large ASX listed companies, looked at the hidden social structure within each board and its ramifications. This hidden 'hierarchy' was a consequence of a largely sub-conscious process in which directors made subjective judgements about each other's legitimacy to influence a given decision on the basis of their experience and expertise.

Thuraisingham said this hidden hierarchy shaped the degree to which a director would listen to the perspectives of others and how divergent views are resolved – in effect, who listened to who. She said it was important that this hidden social reality was made visible and its effects fully understood by directors.

"Stable boards require a balance of trust and mistrust. It is this productive tension between cohesion and harmony on one hand and dissent and discord on the other, that keeps a board dynamic healthy."

This, Thuraisingham argued, was particularly true when debating significant decisions such as acquisition. The chair played a critical role in such debate. In addition to having great facilitation skills, a chair needed to create a safe environment in which dissenting voices can emerge and create the space for unspoken concerns to surface.

When asked what personal attributes effective directors brought to the boardroom, Thuraisingham said that they needed to demonstrate both humility and courage.

"What I mean is that directors need humility to know they may be wrong, to trust the wisdom of others, but also have the courage to practice detachment from the majority view and not concede to social pressure to conform to an overwhelming opinion. This goes to the core of the role of an independent director – the ability to practice independent mindedness. This is of course easier said than done as it is often difficult to find humility and courage in the same person."

Directors were often appointed based on their commercial expertise, knowledge and functional expertise, rather than for example their skills in constructive dissent. These social skills were crucial to read the dynamic, skilfully navigate discussions and make a valuable contribution to major decisions.

"Nominations committees may also have to consider the effort that needs to be invested in the individual and collective development of directors so that a healthy dynamic grows and thrives."

In this climate of rapid business disruption and change, Thuraisingham said it was especially important that boards had quality discussions where a wide range of views could be expressed.

Ingley agreed, saying that dynamics varied from one board to the next so each board needed to work out for themselves their interpersonal relationships and these would change over time with tenure changes.

Coral Ingley

Meena Thuraisingham

Appointing new board members was an opportunity to balance the dynamics with a mix of different personalities and leadership styles and should never be a shoulder tapping exercise.

There was no one correct formula for an effective board makeup and dynamic but using psycho-metric testing, professional search firms and/or Institute of Directors' advice when appointing new members were common tools.

Ingley said the attributes needed by effective directors were emotional intelligence (EQ) and emotional agility (E-agility). EQ is awareness of the social skills you need in any social situation while E-agility is a deeper understanding of how you personally react in different situations and your impact and influence on others.

"New Zealanders are no better or worse than boards elsewhere for these types of skills but the key is in developing the skills. Board members don't often come to the table for the first time with these attributes."

Companies needed to invest in board member development through facilitated workshops, role play, simulations and the like so members could reflect on behaviour and change together if required. These tools could help a dysfunctional board become an effective board although some problems were difficult to fix such as weak chairs, grandstanding and domineering personalities.

Ingley said a common problem with New Zealand boards was our fairly passive-aggressive kind of culture.

"This passive-aggressive behaviour means we don't like confrontation so tend to let situations build up until they are intolerable and then are not well handled. That's why it is important for board members to have the emotional agility to cope with situations before they become intolerable."

The key to identifying problems was effective, regular board reviews, Ingley said.

"Better boards have effective reviews but some are just box ticking exercises to satisfy compliance requirements rather than trying to improve board effectiveness. This is a missed opportunity. New Zealanders often get defensive about reviews but they should be about board development and intellectual honesty. Board members need to be socially mature to look at themselves critically and use these evaluations as a personal development tool."

Ingley said in her experience, the majority of people who accepted board positions genuinely wanted to make a positive contribution to that board. Therefore they were usually responsive to change when it was required.

"Boards are acting in a very challenging environment with the rapid pace of change – digital, social, economic, political – and so they need to be vigilant and be aware of assumptions and falling onto negative habits of interacting. The good news is there are many tools and third parties that can help improve board dynamics and effectiveness and thereby boosting company performance."

BOARD DYNAMICS INTENSIVE

Consider how a shift in your board's culture and communication can increase its effectiveness.

This course launches in Auckland on 15 and 16 August.

What Matters in board dynamics

The view from the helicopter

IoD Chartered Fellow Tony Carter shares his views on governance, including what directors can do to improve boardroom culture and relationships between the board and executive team.

Despite the numerous accolades received during his career as a director, Tony Carter doesn't see himself as a senior, experienced director; "I've only been a professional, full-time director for about six years."

Those words are key – professional and full-time. It is the understanding of governance as a profession that guides Carter's approach to his governance positions, and his willingness to support the work of the Institute of Directors.

"I do believe what I do is a profession in much the same way as law and accountancy. That's why I believe ongoing education and training is so important and why I'm a strong supporter of the IoD.

"I do see my role as full-time; while some might criticise mine and other directors' workloads, the directors that really worry me are the ones who see it as a part-time retirement role. I can think of people I know who are on one board, they never come to anything like this (referring to IoD branch networking and learning opportunities), they dust off the suit once a month and they come along to the board and expect to make a contribution. Bluntly, they are ill-equipped to make that contribution."

Best known for his roles as chairman of Fisher & Paykel Healthcare, Air New Zealand and the Blues LLP, Carter is also a director of ANZ Bank New Zealand, Fletcher Building Industries and Avonhead Mall, and a trustee of the Maurice Carter Charitable Trust.

The first of seven lessons Carter shares with other directors comes from his early experience working in a cooperative environment. Carter's governance career began as an executive director and later chairman of Mitre 10 New Zealand. After joining Foodstuffs group as chief executive Foodstuffs South Island, Carter took over as managing director of Foodstuffs in Auckland in 2001. In a cooperative, Carter says there are no secrets from the board, who hear about goings on from many sources in the company – from the executive team to the delivery drivers.

"One particular aspect of those organisations is as a director you have multiple sources of information and the director is often better informed than the CEO. One lesson I learned really quickly is

Seven lessons

- #1 Expect your management to be open and honest with you
- #2 Don't beat up anyone for bringing bad news to the board table
- #3 Don't be afraid to disagree with a proposal
- #4 Get some role models and mentors and learn from them
- #5 You are part of a team and must support the team decisions
- #6 Be careful the company you keep
- #7 Be careful what you ask for

you can't be economical with the truth in a cooperative board because they know about it better than you."

Bearers of bad news?

The nature of those cooperative environments meant transparency and openness were a given and that is a lesson Carter says he has carried through to non-executive roles. Carter says directors should expect management to be open and honest, and the actions of the board need to encourage this. The second lesson is therefore don't beat up someone for bringing bad news to the board table.

"If management are afraid to bring things up then you will discourage the openness that I think is so vital to any board."

Carter has no time for recriminations, and has a favourite saying that guides behaviour when bad news arises – "we are where we are". That doesn't mean you don't look back on lessons to be learned, Carter says, but it focuses the board on looking forward to solutions rather than dwelling on who is to blame.

Clearly Carter's approach is having an impact. In recognising Carter's selection as 2014 Chairperson of the Year by Deloitte Top 200 judges, Dame Alison Paterson noted that Carter is also chair of 2013 Company of the Year, Fisher & Paykel Healthcare, and 2014 Company of the Year, Air New Zealand. Air New Zealand continues to bring in accolades, the 2016 list includes Airline of the Year (AirlineRatings.com), International Airline of the Year (Roy Morgan) and number one corporate reputation in New Zealand (Colmar Brunton) to name a few.

The chair sets the tone for the boardroom, and Air New Zealand and Fisher & Paykel Healthcare are excellent examples of what can happen when the tone is one of openness and trust. The board plays a key role in an organisation striving for excellence on the world stage, and in Carter's

"If management are afraid to bring things up then you will discourage the openness that I think is so vital to any board."

boardrooms the board both mentors and challenges their management teams.

"I certainly don't see it as a contest between management and the board. Hopefully both management and the board have the same objectives. I see the board's primary role is to mentor and constructively challenge management.

"I've seen boards at one extreme who were there to make management's life a misery, and at the other where they didn't challenge management and were simply there to rubber stamp everything. Neither approach will ultimately add any value."

Challenge and consensus

There is a balancing act involved in the boardroom when it comes to challenging management. As a former CEO, Carter has experienced this from both sides. As a CEO it was frustrating when a seemingly straight forward matter would become controversial and the board would be uncomfortable. But, Carter says, "without exception those situations would lead to a better decision, even if it was frustrating at the time".

Sitting on the other side of the table Carter recalls a time when a proposal was put forward, and although the board didn't really feel comfortable it went unopposed during the meeting. It wasn't until outside of the board setting many of the board confessed their discomfort with the proposal and it was later dropped. The lesson is that directors cannot be afraid to disagree with a proposal – after all, that is your job and, as Carter's CEO experience demonstrates, disagreement can lead to better decisions being made.

Building a culture within the board that is accepting of disagreement but being able to come together and reach consensus is the role of the chair. Carter explains that each of his boards has a unique personality and its own culture; "I suspect some of that is simply how they have evolved, but a lot will have to do with the chairman."

Coming to consensus within a board requires balancing debate and decisiveness – a chair who focuses too much on making a decision can cut debate short whereas one who lets debate go around in circles will never get anywhere. "The key from my perspective is to try to give every director the opportunity to make their points but then intervene and try to find the consensus view. That's quite a skill."

What if everyone cannot agree?

"As a director you are a member of a team – everyone has the opportunity to give their input, but once a consensus has been reached you are duty bound to support that decision. It's a bit like collective responsibility in cabinet."

The exception, Carter says, is if the consensus view goes against your personal values or you truly cannot support the collective decision; at that point you might find you have little choice but to resign.

It can be lonely at the top

Carter made the move to full-time, professional governance in 2010. In the change from full-time CEO to director there are three key things Carter noticed about life in governance, one of which he hadn't anticipated.

"Most obviously, you're on your own with none of the support you come to rely on as a CEO. You answer your own phone, you manage your own diary, you do your own admin. One of the things I try to do is accept invitations from professional firms and come to events to get that stimulation."

Learning from others is incredibly important, and Carter believes in finding mentors to help you work your way through some of the challenging and unexpected parts of governance.

"Over the years I've learned so much from working with and observing some wonderful people. Get some role models and mentors and learn from them. In my case the three who stick out are Dame Alison Paterson, Roger France and John Palmer."

The thing Carter hadn't been prepared for was the need to quickly switch focus to different organisations. "In an executive role you focus on one company. When I was a CEO I had one company to focus on, and I spent basically every waking minute thinking about it; all of a sudden I had four boards."

Coming from a CEO background rather than professional services meant Carter wasn't used to splitting his focus that way. It was an unanticipated challenge of the role. Understanding how much information you will receive and recognising how much is too much is also a key learning.

"You have to get your head around board papers. I'm a believer in less is more; it's the board's job to govern, not to manage. That means staying in the helicopter. If you get into too much detail you will miss what is really important."

Ultimately the board is responsible for the level of detail management provides, and needs to be clear about expectations. A lot of information isn't necessarily a good thing, Carter says.

"It's the board's job to govern, not to manage. That means staying in the helicopter."

"I'm always nervous about directors asking for more information than they need."

There are moments when more information can be very useful, especially when joining a board. Carter says it is important for directors to do their due diligence prior to joining a board: you need to know whether the board culture is the right fit for you.

"Talk to the CEO, fellow directors, the CFO. The most important thing to do when you join a board is talk with the other directors on the board– do they hold similar values? Do they have integrity?"

For Carter this is related to another lesson – be careful about the company you keep. It can be lonely at the top, so select wisely the organisations and people you want to be aligned with.

Once on a board one of the most important relationships you will foster as a board member is with the CEO. Appointing the CEO is without question, Carter says, is the most important decision the board makes.

"A good CEO can make the company."

Carter would know – Air New Zealand faced the challenge of appointing a first-class CEO following the departure of Rob Fyfe. Carter explains that within a company like Air New Zealand it is important to find someone with industry experience. Part of succession planning at the organisation involved bringing someone into the organisation with the purpose of watching their progress for growth into the CEO role. The plan was successful; that someone is current CEO Christopher Luxon, the 2015 Executive of the Year.

The success of Air New Zealand is rightly drawing attention of late and that is in no small part due to the leadership of its board and management. This year Air New Zealand was named most reputable company not only in New Zealand, but across the ditch in Australia too. The actions of those at the top really do make a difference, if the success of the national airline of a small country at the bottom of the world is anything to go by.

Tony Carter has graciously given his time to share these insights with audiences at a number of IoD branch events, most recently in Taranaki and Waikato.

Climate change: a developing risk for directors

A legal opinion commissioned by two lead organisations has put climate change on the radar as an active liability risk for directors across the Tasman. We need to take notice because the duties which create the accountability in Australia apply with equal force here.

The galvanising event in Australia was a roundtable organised by the Centre for Policy Development and the Future Business Council. On the agenda was legal advice on the extent to which corporate law requires directors to consider and respond to climate change risks affecting share values.

The report concluded that: "It is only a matter of time before we see litigation against a director who has failed to perceive, disclose or take steps in relation to a foreseeable climate-related risk that can be demonstrated to have caused the harm to a company (including, perhaps, reputational harm)".

Key findings are that:

- climate change effects as they occur will be regarded by the courts as predictable and therefore may be relevant to a director's duty of care and diligence to the extent that they intersect with the company's interests
- directors are not legally restricted from taking into account climate change and related economic, environmental and social sustainability risks where those risks are or may be material to the company, and
- directors who fail to consider the impact of such risks now could be found liable in the future for breach of duty.

The analysis has generated significant debate and commentary in legal and governance circles in Australia and is timely in the New Zealand context, given the push in the NZX Corporate Governance Code 2017 toward more ESG reporting.

New Recommendation 4.3 states: "An issuer should provide non-financial disclosure at least annually, including considering material exposure to environmental, economic and social sustainability [ESG] risks and other key risks. It should explain how it plans to manage those risks and how operational or non-financial targets are measured".

The newly updated Code recommends that issuers explain how they intend to manage ESG factors, that they report against a recognised international framework such as the Global Reporting Initiative and that they describe how the business is performing against its strategic objectives.

Ben Williams

Roger Wallis

So what to do?

A good place to start is with the guidance produced in December last year by the 32 member multi-national Task Force on Climate-related Financial Disclosures, chaired by Michael Bloomberg.

Its report was focused mostly on the financial sector but they consider that it is broadly applicable across a range of sectors. They recommend four layers of disclosure:

Governance – the organisation's governance arrangements around climate-related risks

Strategy – the actual and potential impacts of climate change on the organisation's business strategy and financial planning

Risk management – the processes used to identify, assess and manage climate related risks, and

Metrics and targets – the measurements use to guide and evaluate performance.

Obviously, to provide this volume of information, the board will need to set in place procedures to ensure that it is kept informed of the company's climate change risk profile and of the potential impact of climate change effects on the business.

Such effects might include sharp revaluations of carbon-intensive assets or, in the case of buildings, an increased risk of flooding. Insurance is likely to become more expensive or, in some locations or industries, impossible to obtain. And increased planning restrictions on use of properties in vulnerable areas are also on the cards as local authorities seek to "adapt" to the impacts of climate change.

New legal requirements?

Much of the response to the climate change challenge will be generated at the national and local government level, requiring of businesses only that they comply with the law. New Zealand has committed in the 2015 Paris Agreement to reduce emissions to 30 percent below 2005 levels by 2030 (within 13 years). This is an ambitious goal, considering that in the years 2000 to 2014, New Zealand emissions increased 6 percent.

To inject some integrity into the target, the government has instructed the Productivity Commission to inquire into the Opportunities and Challenges of a Transition to a Lower Net Emissions Economy for New Zealand. Terms of reference include the role of market-led solutions, direct regulation (such as minimum fuel efficiency standards), how research and design might contribute to the development of low emission technologies and whether there are any barriers in New Zealand to domestic investment in reducing net emissions.

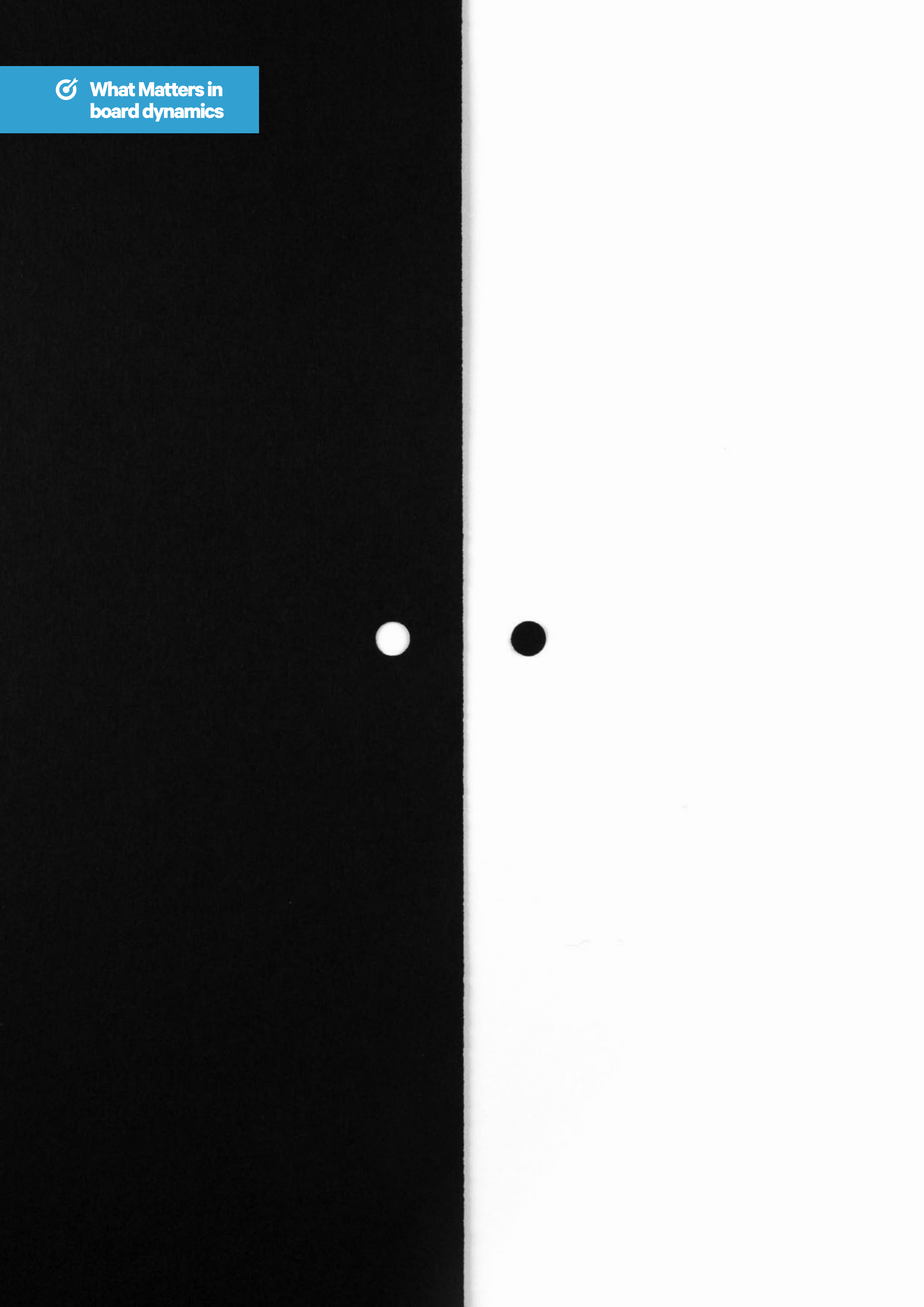
The Commission is due to present its conclusions to the government by 30 June 2018. This advice will be useful but directors should be giving thought to these issues now, not least because the climate change die is already cast in a number of important respects.

For example, research commissioned by the outgoing Parliamentary Commissioner for the Environment demonstrates that even a modest rise in the sea level will increase the frequency of extreme weather events and that the 30cm increase projected for New Zealand by 2065 will turn a 100 year flood into an annual event in Christchurch and Wellington.

Roger Wallis and Ben Williams are both partners at Chapman Tripp. Roger specialises in corporate and securities law and Ben in natural resource and urban infrastructure.

CHAPMAN TRIPP

What Matters in board dynamics



Spotlight on corporate ethical behaviour

BoardRoom editor Emma Sturmfels looks at public commentary and perceptions on ethical behaviour. What motivates an organisation to look at its ethics? And what do directors need to be thinking about?

They say a fish rots from the head, and the boards of large corporations rightly come under scrutiny when the actions of those under their leadership are revealed to be less than wholesome. Companies including Volkswagen, Wells Fargo, United Airlines and Uber have all hit the headlines recently with commentators questioning the ethical standards of practice shown at levels from front line staff through to boards of directors.

The scandals drawing attention are often not the actions of one bad apple. Take for example the more than 5000 staff dismissed for fraudulent activity at Wells Fargo, or the million plus vehicles fitted with software to cheat emissions tests by Volkswagen. There are clear signals something is not right with the ethical standards set by the board when this many people are involved in such activity.

Worryingly, the boards of these companies were quick to distance themselves from the actions of staff in the organisations they head; either directly placing the blame on senior management or failing to recognise the role the board had played in the outcome.

Discussing a report on the investigation into the activities at Wells Fargo, where more than 5000 staff members were found to have opened false accounts to boost sales, the LA Times notes that the board essentially blamed senior management for failing to provide accurate information about what was going on. The Times understandably dismisses this excuse:

> Sorry, that won't do. A careful reading of the report reveals a board that took months, even years, to get its arms around the scandal despite plenty of warnings about its nature and magnitude. These include an investigation by The Times in December 2013 and a lawsuit filed by Los Angeles City Atty. Mike Feuer in May 2015.

To claim that management did not properly brief the board is a poor excuse – the board needs to have confidence in the information management provides. But as Fortune notes, the lack of responsibility taken by the board is demonstrative of a wider issue. The report also ignored the board's failure to address whistleblower cases. In doing so Wells Fargo missed an important opportunity to "signal a new culture of openness and shared accountability, rather than retaliation. Instead, the report strongly suggests that an emphasis on blame will continue to permeate the culture as long as the current board rules."

The Times summarises that the scandal and lack of responsibility taken by the board isn't unique, noting "almost any corporate scandal can be traced to some degree to a board unwilling or unable to perform its function of riding herd on management."

Writing for Project Syndicate, Professor of Leadership and Governance at IE Business School, Lucy Marcus, says that trouble at governance level is one rarely publically discussed as a cause of large corporate failings. Of the risks highlighted in the World Economic Forums' 2016 Global Risk Report, Marcus argued none caused "the recent spike in debt crises or the wave of scandals that engulfed – just in the last year – Volkswagen, Toshiba, Valeant, and FIFA. These developments (and many more) are rooted in a more pedestrian – and perennial – problem: the inability or refusal to recognise the need for course correction (including new management)."

Can a leopard change its spots?

In October 2015 the Financial Times asked whether Volkswagen's decision to nominate a long-serving executive as chairman again highlighted the carmaker's corporate governance and culture, which some experts argue were a root cause of the diesel-emissions scandal:

> VW has admitted installing software in engines over several years so they passed laboratory emission tests but belched out dangerous nitrogen oxides when on the road…Governance experts argue the cheating was predictable because of VW's lax boardroom culture and peculiar corporate culture. "The scandal clearly also has to do with structural issues at VW…There have been warning about VW's corporate governance for years, but they didn't take it to heart and now you see the result," says Alexander Juschus, director at IVOX, the German proxy adviser.

At a meeting in 2016 Volkswagen CEO Matthias Müller told shareholders the scandal could prove to be beneficial for VW, should they manage to turn the crisis into an opportunity: "The crisis has also opened doors. It forced us to strengthen and speed up overdue changes, and to set new priorities... What unites all of us with a role to play here at Volkswagen... is the desire to do everything we can to win back trust."

The Financial Times article notes however, that previous crises at VW – including a prostitutes and bribery scandal in 2006 – did not deliver real reform. Mr Juschus commented to the publication "If VW doesn't change now then they will never do it. It really depends on the three big shareholders – whether they are willing to reform. I have my doubts."

Carved in stone

Arguably what has happened at both Wells Fargo and Volkswagen is a question of ethics. Setting ethical standards of practice and building a culture that values employees doing the right thing is not just a matter of writing out a few company values. You can carve your values into marble, à la Enron, but that won't mean the company lives by those.

If the main concern of the business is to improve the bottom line does that mean those within your organisation can do whatever it takes to achieve that goal – fraud included? It isn't a good look for a public relations stand point, but will ethical issues be addressed if the bottom line is not heavily impacted by unethical behaviour? Wells Fargo has not lost nearly so many customers as anticipated as a result its scandal. Volkswagen is enjoying increased sales, recently overtaking Toyota to become the top-selling vehicle brand; sales in China are high – according to the Guardian 'dieselgate' was a 'non-issue' there.

Even as bribery and corruption scandal envelopes top executives at Samsung, the company continues to enjoy high profits, in April posting its best quarterly profit in three years. Bloomberg reports the scandal, involving South Korean president Park Geun-hye, spurred millions of South Koreans to take to the street in protest "over cosy ties between the government and the family-run chaebol[1] that control much of the country's corporate landscape." That seems to be more of an action against government than of corporate governance issues.

Fortune magazine considers the varied responses from Samsung stakeholders:

Needless to say, investors won't be happy if the scandal ends up hurting sales and public confidence in the company, but bear in mind that many consumers might not even be aware of allegations against the company. If you use a Samsung device, have you switched brands after reading about its bribery accusations? For many consumers, the answer is no.

Samsung investors and consumers will react differently. Investors who are aware and outraged by the charges are likely to consider investing elsewhere. Consumers, on the other hand, even if they are aware of the charges, will likely stay with the company, as long as their devices continue to work properly.

The Financial Times noted in April that after the nightmarish episode involving a passenger being violently hauled off a United Airlines flight, the airline's shares were down just 5%:

In the volatile airline sector, though, this is a blip. It has barely underperformed its competitor Delta Air Lines over the period...Does this incident not show a brutal callousness toward the customer, reflecting a deeper cultural failing?

"What if even serious damage to corporate reputations is not, in many cases, very economically important in itself? ...Where the consumer is happy to judge a company by the last product it turned out, the profit motive on its own makes a poor mechanism for keeping managers on the straight and narrow. Boards and regulators must step up."

ETHICS AND CONDUCT ADVICE TO BOARDS NEEDS TO IMPROVE

Boards have a key role in leading and overseeing ethics and conduct risk. This involves supporting management and holding them to account on achieving and maintaining a healthy organisational culture and ethical practices. However, our 2016 Director Sentiment Survey with ASB found that only 37% of boards receive comprehensive reporting from management about ethical matters and conduct incidents, and the actions taken to address them. The repercussions from bad conduct can be devastating to a business, the emissions scandal at Volkswagen being a prime example. Boards need to ensure that management provide comprehensive and timely advice on ethical matters and conduct risks. Follow through from the board is critical to setting the right tone. How a board tackles its ethical issues can send a very clear signal to the CEO, senior management and the whole organisation.

Taking a stand

Considering the behaviour of Uber CEO Travis Kalanick, a writer at Fastcompany (April 2017) pondered whether businesses actually take ethics into account:

"Businesses don't have to be ethical, they only have to make bottom lines. It's usually the government's job to step in and prevent abuses that arise from vigorous tactics."

A cynical point of view, but perhaps unsurprising considering the lack of trust reported in business in recent surveys such as the Edelman Trust Barometer. Is the message being sent that bottom line is the only consideration? That behaviour will not change unless shareholders demand it or the government steps in?

The IoD's Four Pillars of Governance Best Practice notes there is a strong relationship between values and ethics in business. Directors are of course under pressure to deliver financial targets, but "focusing on ethical practice is not a

1 Chaebol: in South Korea, a large family-owned business conglomerate.

diversion from core business... running a company with consistent integrity and high ethical values is simply good business."

The benefits for an ethical business include attracting the best people and investment opportunities. Consumers can vote with their feet, and more and more investors are considering a wide range of values when deciding where to put their money. Speaking at a World Economic Forum event, Blackrock's Barbara Novick noted there has been a huge shift in how the world sees companies and the boards responsible for them. Corporate governance issues are being elevated to front page news, not staying hidden away behind boardroom doors.

Investors have helped to push through change, engaging with businesses when they disagree with their values rather than just walking away. "Engage with companies on issues you have concerns about," Novick says. "At the end of the day, the board members are there to protect the shareholders and they should be thinking about long-term."

Shareholders will speak out. Wells Fargo's board might not have taken responsibility for the issues in their organisation, but at the bank's AGM in April, just 56% of shareholders backed board chair Stephen W. Sanger. The New York Times reported that five other directors failed to achieve a 70% vote "that typically denotes a serious protest vote and which often forces companies to respond on such matters as 'say on pay.' Not only does it suggest shareholders are displeased that board members were too slow to act, but also that the bank's internal investigation into the years long affair was too soft on them."

Dov Siedman, CEO of LRN USA, notes "when the world is bound together this tightly, everyone's values and behaviour matter more than ever. ... We've gone from connected to interconnected to ethically interdependent."

Looking at what media says at any point in time can influence perceptions.

The tone from the top sets the culture of the entire organisation – the fish rots from the head.

Director Vacancies

DirectorVacancies is a cost-effective way to reach IoD members – New Zealand's largest pool of director talent. We will list your vacancy until the application deadline closes or until you find a suitable candidate.

TAURANGA HOCKEY ASSOCIATION
Role: Board Members
Location: Mount Maunganui, Tauranga
Closes: 30 June 2017

NGA MAUNGA WHAKAHII O KAIPARA WHENUA HOLDINGS LTD
Role: Director
Location: Auckland
Closes: 30 June 2017

KIDZ NEED DADZ
Role: Board members (2-4)
Location: Tauranga
Closes: 31 July 2017

DIABETES NEW ZEALAND
Role: Independent Board Member
Location: Meetings held in our National Office in Wellington
Closes: 18 Aug 2017

NEW ZEALAND RED CROSS
Role: Chair of Audit & Risk Committee, Foundation Trustee & Full National Board Membership
Location: National, meetings are mostly held in Wellington
Closes: 31 Aug 2017

The following positions remain open until filled:

EPILEPSY FOUNDATION OF NEW ZEALAND INCORPORATED
Role: Governance Board Members
Location: Auckland meetings

REGISTERED MASTER BUILDERS ASSOCIATION OF NEW ZEALAND INC
Role: Board Chair
Location: Wellington

FRANKLIN HOSPICE CHARITABLE TRUST
Role: Trustees/Board Members (2)
Location: Pukekohe

ALZHEIMERS WELLINGTON
Role: Board Members (2)
Location: Petone, Lower Hutt

FAMILY ACTION
Role: Board Member
Location: Henderson

DEMENTIA CANTERBURY
Role: Executive Committee/ Board Chair
Location: Christchurch, Canterbury

MS WAIKATO TRUST
Role: Trustee
Location: Hamilton

ASPIRE CANTERBURY
Role: Chairperson and Treasurer
Location: Christchurch

THE ORPHEUS CHOIR OF WELLINGTON INC
Role: Board members (2)
Location: Wellington

RUTHERFORD ST KINDERGARTEN
Role: Board member
Location: Nelson

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laudererasmus@kpmg.co.nz

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Is governance failing our potential?

A strong statement, but one supported by poor survival statistics of our early stage enterprises that don't survive the transition from start-up to a high performing organisation. It is a well-known fact that a large portion of our enterprises fail within five years of launching. What we don't know is the true cost to New Zealand's economy from this lost potential. Could one of these failed fledgling business been our first Unicorn (private business valued at USD$1b+)?

The role of governance in driving success

According to the CB Insights January 2017 report there are 183 global 'Unicorns', with the majority of these having reached this status in the last three years. New Zealand is yet to register its first Unicorn. You may not be concerned about this measure, but we ought to be concerned about the potential role governance is playing in these statistics of failure and success.

There are a handful of studies and research papers on the role of governance in New Zealand in early stage enterprises and they remain largely inconclusive. The challenge is how to measure the impact of strong governance on a start-up organization. Empirical evidence is hard to come by and research techniques and frameworks don't answer the question being raised – "What is needed to ensure a successful transition to a high performing organisation to avoid failure?"

A number of studies focus on the theory of governance as being either;

1. a separation of ownership and management control (agency),
2. management are stewards of a company's resources used to maximize profits for shareholders (stewardship) or,
3. the board is the critical link between the enterprise and key resources needed.

These studies look to define the types of governance activities at distinct periods of an organisation's life-cycle. There is a stark difference between the role directors play in early stage growth enterprises and those that are established – directors in start-up's are more active and reach directly into the organization's decision making, and anecdotally have a greater influence on performance. This is compared to a board of a larger company that is generally more focused on monitoring and reporting.

The role of the Director

If the role of directors changes from active participation to passive oversight, what happens at the point of transition and is this happening at the same time our companies are failing? Do our enterprises fail as the board steps away from actively driving strategy and its implementation? Does the transition point from having a single investor's direction to dispersed ownership create a real survival risk for a business? These are difficult questions to answer and there is no apparent New Zealand research on this. However, what is obvious is boards of early stage growth enterprises are actively managing key activities such as capital raising, research and development, product manufacturing, marketing and distribution decisions and this is driving organisational performance.

The lesson is that continued active involvement is essential in our high growth enterprises as they move to true commercialisation and establishing true potential. Careful planning and a board succession plan is needed at this time. As these businesses move through continued heavy investment in commercialisation, typically funded through a dispersed source of investment, the composition of the board will change. This needs careful management to ensure new entrants to the board continue to actively participate in the business activities.

In my view there are a number of key steps directors of an organisation can take to help avoid the paradigm of New Zealand small to medium enterprise failure:

1

Don't step away from active participation as the organisation transitions. The risk of failure of the company as it moves from early stage through to a commercialised operation should be clearly identified. New directors joining the board as a consequence of new shareholding need to understand the importance of continuing this role. Succession planning for this phase is a critical mitigation to this risk.

2

Continue to define and actively guide the organizational strategy. It is vitally important to be focused on the content of the strategy and its outcomes, and less important on due process and passive monitoring. Avoid separating involvement from management through the use of formal frameworks.

3

Continually validate. Validation of the market opportunity should not only form part of the initiation of a start-up's business model. Continual validation of the market and its propensity to purchase the product is needed at critical decision points. Validation is often referred to in the initiation of the business, but is a critical tool for a board to support its active decision making at key milestones.

4

Balance the board's agenda between developing the organisations competitive proposition and compliance and risk management. As more investors join the board, there will be the tendency to move towards ensuring systems are in place so that the enterprise is accountable to those investors. This need for extensive monitoring and reporting should not be the sole focus of the board and management. It requires balance. It is important to understand that governance is about running a really good business and not just about enforcing controls.

5

Take a skills stocktake of the board. Ensure critical areas are filled by subject matter experts that can provide fresh thinking, partnerships and contacts. Using these skills, focus less on the exit event and more on ensuring transition from early stage into a sustainable growth enterprise that moves through the commercialisation phase.

New Zealand's high growth enterprises and the directors that help guide these businesses have a significant opportunity to navigate the challenges during commercialisation to help New Zealand reach our potential. Establishing an actively engaged strategy with systems and processes fit for purpose will be critical to achieving this goal. Take independent advice if there are questions over the balance settings at the board level.

What Matters in board dynamics

Reporting to a board

Trust is the essential element of an effective relationship between a senior executive team and its board and while it can take time to establish, there are steps the CEO can take to ease the process.

That is the advice from those who have been on both sides of the boardroom table.

Mark Waller, Rick Christie and Mark Hamilton are highly experienced chairs and directors and also former CEOs and all agree that trust, or the lack of it, is what makes or breaks good collaboration between board and management. Good collaboration is fundamental to a successful organisation.

Mark Waller is currently chair of the EBOS Group and was formerly the group's chief executive and managing director. He is also director of Scottech.

He said in his experience, new CEOs often view reporting to the board as a pain that slows them down but as CEOs mature and evolve they can appreciate the difference between the roles.

"This evolution of CEOs means that they can understand what the board is actually there to do and can use that knowledge to value the skillsets around the board table and tap into them."

Rick Christie is currently chairman of IkeGPS, Service IQ and NeSI and is director of Southport, Solnet Solutions and PowerHouse Ventures. He said the CEO's understanding of the board's role and how a board thinks is vital to developing a trusting dynamic.

"There's no point telling boards everything that is going on, on a day to day basis. CEOs often have to make a judgement call about what to report and that's why it's important they actually know how boards work so they can make good judgement calls. "

"Board members will ask themselves 'can I rely on what management is telling me?' and 'are they telling me everything and leaving nothing important out?' It's vital they can say yes to those questions."

Mark Hamilton is an independent director of several companies and former CEO of BrewGroup, formerly Bell Tea and Coffee Co.

He said when he was a CEO he had good advice from one chair who said there was no point presenting a perfect report as no business ran perfectly.

"There is the temptation by CEOs, especially New Zealand CEOs because we hate conflict, to present perfect reports. But if you're presenting a paper that doesn't report any issues or problems then you're not presenting a true picture. It just leads to directors to ask a lot of questions instead of being reassured. The way to build trust between a board and management is for the CEO to be honest and upfront rather than make things seem rosy."

Neglecting to pass on the issues and challenges so they can be discussed thoroughly can expose an organisation to risk and undermine performance. Christie said an example of this was Solid Energy where "things went completely off the rails".

"They completely missed the main critical factor that was their undoing – the coal price. With the benefit of hindsight, both board and management failed to do their job adequately as they ignored the risks."

Hamilton said CEOs needed to give a lot of thought to reporting and use templates to deliver accurate, timely, concise and insightful reports. Barriers to developing trust were reports that gave too much information, gave too little information or were delivered in a defensive tone or manner.

Waller said as a chair his ideal report from a CEO would include a macro section on the international situation and possible effects on the organisation, a quick operational overview, and the strategic implications.

Christie said boards hated getting too much detail too early. "My advice is to state upfront what the paper is about and put supporting information in the appendix. Directors want to know the main points first."

He said in a crisis or serious situation, CEOs should raise the issue with the board as soon as possible but preferably when they had a good picture and could brief thoroughly on the risks. Risk evaluation was a key board role.

Hamilton said he also believed in a "no-surprises" approach and if an issue could be a key risk to an organisation it should be raised with the board outside of the normal meeting schedule.

"Directors should never be blindsided and in serious situations it's not up to management alone to solve it."

Waller said when he was a CEO if a crisis arose he would talk to his executive team first. He'd try to get the information so they could look at how the situation arose, look at how to prevent a repeat and come up with some recommendations then approach the board.

"Its best to take it to the people who are less emotionally involved – the board."

The relationship between the CEO and the chair is at the heart of the trust between the executive and board. Waller said although the chair sets the tone, the CEO does have the ability to strengthen the relationship. As a generalisation, he said there were three different types of chair: those too hands-off and so ill-prepared for meetings, those too hands-on and trying to do the role of CEO, and those who were well-balanced and diligent.

CEOs could meet with a hands-off chair ahead to board meetings to engage them in the issues and brief them on the reports and important risks. Dealing with a chair who was trying to act as a pseudo-CEO was more difficult. However, the CEO should never make it personal but always focus on the issue at hand and ask them to logically explain why they want to take a certain course of action.

Christie agreed that it was crucial to avoid actual arguments with directors.

"My advice for everyone is to leave your ego at the boardroom door. Bad decisions can result if people's egos get in the way of common sense."

Hamilton said whether you are a director, a manager or a business leader you cannot know everything.

"The only way you can be successful is to have good trusting relationships and value the views of others."

Waller likened the board-executive relationship to the one between the All Blacks and their coaching team.

"The coaching team is not out on the field playing the actual game but provides the strategic overview and support. Its key that both groups trust each other to do their roles the best they can."

Reporting to a board
First course is in Auckland, 8 August 2017

Revolution & evolution

Martyn Levy speaks to the Boardroom editor about the lessons New Zealand can learn from Israel, why speaking several languages has helped his career, and why continuous learning matters.

Martyn Levy is a Chartered Member of the Institute of Directors, a non-executive director with Instant Finance and owner of digital marketing and managed services provider Acurix Networks. The former banking lawyer now runs strategic advisory business MilaXAG and was previously board chair of Kadimah School.

As a 20-year old, Levy took a year off university to immerse himself in a Kibbutz-based Hebrew language and geopolitics course in Israel on route to a 3-month Russian language and literature scholarship at the Pushkin Institute in Moscow. Levy understood from an early age that to really understand a people and a country you need to immerse yourself in the language and the culture of the place.

At that time, the newly independent Russia was itself in a state of revolution. Around the time of the collapse of the Soviet Union in 1991 around one million Soviet Jews fled to Israel, with the last wave of this coinciding with Levy's time studying at a Kibbutz in Northern Israel. Half the course was made up of people from the former Soviet Union.

"Some very talented and qualified people were arriving in Israel with no jobs and no language. Fresh off the boat, they had five months to learn Hebrew and begin a process of accelerated integration into Israeli life. I was living with these new immigrants – working as a fisherman in the morning and studying in the afternoon; by the time I got to Moscow I had mastered Hebrew and my Russian was already that much better."

Learning from Israel

Levy sees Israel's ability to leverage its talent pool as a great advantage. 60% of immigrants to Israel in the late 80s and early 90s were university-educated, so tech business incubators were created to leverage the skills of the new scientists, engineers and doctors. Six incubators grew to 24 and millions of dollars continue to be invested in this space with these incubators feeding the vibrant and hugely successful venture capital and technology industries in Israel. Just last year, Levy says, Israeli tech companies achieved over US$10 billion in exits. Already in 2017 Intel announced its intention to purchase NYSE-listed Israeli driverless technology firm Mobileye for US$15 billion.

"It was very interesting to see all of that happen before my eyes from the beginning; how to integrate people from all over the world into a different society, united by a common bond. Language is critical to engagement and so I've always sought to study as many languages as I can."

Levy will take part in a cybersecurity delegation to Israel this year, led by National Cyber Policy Office director Paul Ash, and says the lessons to be learned in Israel keep him going back.

"I keep going back every year, or twice a year if I can. Israel is a world leader in innovation and commercialisation and they have managed to leverage their unique situation and turn it into a competitive advantage. Plus Israel has such an energy and the people are so passionate about everything they do. It's infectious and worth going there just to soak it up."

Levy's experiences in Russia also had a big impact. Arriving in Moscow in 1993, he witnessed rioting on the streets and tanks shelling the Russian white house – "This was Yeltsin's way of resolving the constitutional crisis. He was on the outside with the military and all its power and Khasbulatov and Rutskoy were on the inside waiving the constitution," he says.

The chaos, the people, the deep culture, the revolution; rather than scare Levy off, it made him determined to return to Russia for work at some point in his career. That point came sooner than expected.

Back in New Zealand, Levy was working as a banking and finance lawyer at Bell Gully in Auckland when a UK law firm came through Australia and New Zealand seeking western-qualified, Russian-speaking banking lawyers, who weren't Russian.

"I had to take it right? That's the first time I really understood, and from a personal perspective, that an in-demand combination of niche capabilities give you an edge."

"Language is critical to engagement and so I've always sought to study as many languages as I can."

Levy stayed in law through the dotcom bubble of the late '90s to early '00s. He saw friends' businesses boom and bust and boom again and decided to move into the venture capital and tech space getting involved with a WiFi equipment vendor, which he grew and sold to US-interests in 2009. Later, while working as Head of Strategy at 2degrees, he again found himself leveraging his unique skillset to make the most of an opportunity.

"I was with 2degrees at a conference in Hong Kong, and I met these Russian investors who were looking for a Russian-speaking Westerner with IT and telco start-up experience to execute on some technology and digital propositions for the Russian market. I had just been through eight years of a start-up and then with 2degrees."

"I enjoy helping companies chart the right strategic pathways to achieve a set of business outcomes."

Levy suggested three up-and-coming technology propositions over lunch. "I could see an opportunity here," Levy says, and surely enough an 18-month engagement resulted in a move with his family to Spain and Israel for much of 2013.

"I was fortunate to access these opportunities. I think I've had the most fun and challenged myself the most when I have seized opportunities that allowed me to use my strengths and those of the team around me to create value.

"If you're not feeling uncomfortable, then you're not probably stretching or challenging yourself enough. It's good to have specific expertise that is valued – if you can do something you're good at, that is valued, and that you get paid for it, that's Nirvana."

Talking to robots

Levy is an early adopter of tech, something many might claim but he backs up. His EA Julie, who set up this interview, "is a bot – she's actually an amazing cloud-based artificial intelligence platform developed in France with superb natural language processing capabilities," Levy says.

He also has three home helpers in the form of Amazon's Echo Dot 'Alexa' voice assistant. Like Siri, Alexa has a growing list of commands from basics such as playing media and making lists, to integrating with smart home platforms to perform tasks such as switching on lights or locking doors.

Using technology in his own life has allowed Levy to see where tech advancements can work in business and how technology can help put the customer at the centre of a business, whether at advisory levels with clients, on a board, or the businesses he owns himself.

"If you don't use and experiment with new and emerging technologies it's very hard to understand or apply it to other things. By testing it in your own environment you're able to better apply it to a business. For example, AI and deep learning goes hand-in-hand with data analysis now. Businesses need to take that data, structure and analyse it to accelerate the creation of insights and then use those insights to gain a competitive advantage."

He recognises that there is a real risk when directors do not understand technology, citing cybersecurity as a case study.

"Mitigating cybersecurity risk is not simply the case of a board adopting a strategy. The cyber risk landscape is changing all the time and requires regular review and consultation with experts. It's not like adopting an accounting standard where you have time to adopt the standard and clearly defined rules to follow. The frequency, ferocity of cyber-attacks is growing exponentially and the attack vectors morph on an almost daily basis.

"I've watched cyber come up and I've watched the IoD push cyber and elevate it onto the boardroom agenda, successfully in my view, for those companies whose directors are in and around the IoD.

"If you're not feeling uncomfortable, then you're not probably stretching or challenging yourself enough."

"Board members might not understand how some of it works, but they certainly understand risk. Cyber, as an example, is a risk that needs to be mitigated. You certainly get some pushback, but increasingly they don't have an option. I think it's just an overwhelming requirement. Cyber knows no borders."

Levy says New Zealand also needs to make sure it has people graduating into the workforce who can actually work in the cybersecurity sector – we need to build collaboration between the government, intelligence, private and academic spheres. This collaboration is something Israel does very well and from which New Zealand can learn. At another level Levy thinks there needs to be greater focus on tech skills at schools.

"Do we have science, technology, engineering and maths coming through schools?"

Levy was a trustee for a school which now runs a STEAM (STEM plus Arts) integrated curriculum. While no longer on the board, he is a big supporter of this change. Education matters at all levels and as a trustee Levy helped to put clear governance structures in place and focused on getting board training up to standard.

"I'm a firm believer in continuing professional development, which is of course the focus of the IoD. It's just so critical."

Levy recently became a Chartered Member of the IoD and continues to build his governance career and seek out interesting opportunities.

"I enjoy helping companies chart the right strategic pathways to achieve a set of business outcomes. I also like sitting across a number of different businesses, verticals and projects as it keeps your mind sharp and provides variation, all while certain horizontal issues such as digital transformation or planning for long-term sustainability remain a constant. You never know what issues are going to come up.

"Governance is another evolutionary part of my career. I've consciously chosen to pursue a governance path alongside my strategic advisory and infrastructure businesses. Down the track, and as my governance experience grows, I'll aim to transition from mid-size companies to the boards of larger companies – that's an exciting and logical career evolution."

In the space Levy occupies, who knows what sort of conversations will be had around the board table in ten years' time, and that's why Levy says directors have to be constantly looking at new technologies, risks, and opportunities.

"As a director you have to have a deep understanding of the industry you're in, the key risks and opportunities, the internal and external landscape and strategic context. You can't just sit and be a passive director; you're an active board member and have to help set the strategy for the business, hold management to account for execution. As directors we need to be prepared to pivot and adapt strategies and business models to ensure the long-term viability and sustainability of the enterprise no matter the future operating environment in which it will exist."

GOVERNANCE LEADERSHIP CENTRE

Update

Refreshing the Four Pillars of Governance Best Practice, welcoming the new NZX Code, helping members explore directing in a global environment, and submitting on governance and director-related matters have been key areas of focus for the GLC, says Felicity Caird.

Felicity Caird, Manager, GLC

UPDATING THE FOUR PILLARS OF GOVERNANCE BEST PRACTICE

The GLC has been busy updating The Four Pillars of Governance Best Practice this year to reflect legal and governance developments, and global trends. The new edition will be sent to members later this year and a new and enhanced online version will also be available.

NZX CORPORATE GOVERNANCE CODE 2017

The final NZX Corporate Governance Code for companies listed on the NZX was released in May. This is the first substantial update to the Code since 2003. It represents a significant step forward for corporate governance reporting requirements and brings New Zealand more in line with global trends. The Code has gone further than expected with recommendations which include:

- setting measurable objectives for achieving diversity (gender at a minimum) and assessing and reporting on progress in achieving the objectives
- requiring non-financial disclosure in relation to environmental, economic and social sustainability risks (including how the risks are intended to be managed and how non-financial targets are measured)
- disclosing how health and safety risks are managed and reporting on health and safety risks, performance and management.

The Code will apply for all reporting periods from 1 October 2017 and is available on www.nzx.com. Directors should also be aware that NZX is intending to consult this year on changes to the NZX listing rules.

DIRECTING IN A GLOBAL ENVIRONMENT – AN INTRODUCTION

Increasingly, New Zealand companies are looking overseas to produce and distribute goods and services. Traversing the regulatory and cultural terrain as an international director is anything but straightforward. Governance practices are not standardised across borders. Rather they are influenced by various factors inherent to each country's business environment. The GLC's latest DirectorsBrief explores some of the cultural differences, operational challenges and governance frameworks directors may encounter in other jurisdictions.

SUBMISSIONS

It is important that entities present financial information that is understandable and meaningful to investors and other stakeholders. This is fundamental to good governance and underpins trust and confidence in business. The Financial Markets Authority consulted on updating its guidance on disclosing non-GAAP financial information. The IoD, in its submission, supported updating this guidance to help entities that present non-GAAP financial information ensure that this information is helpful and not misleading.

The IoD also submitted on Inland Revenue's exposure draft of an interpretation statement on the application of scheduler payment rules to directors' fees. The IoD's submission generally supports the interpretation statement and focuses on specific situations in which tax must be withheld from payments of directors' fees (e.g. when payments of directors' fees are made to individuals, companies and other entities).

IoD submissions, guides, DirectorsBriefs, and other governance resources are available at iod.org.nz

Cyber security: Poor alignment leaves the gaps in which attackers thrive

Cyber security policy is still being left in the hands of the technologists. Peter Bailey looks at what that means for business and why it is so important for boards to take ownership of cyber policy.

Information security is generally recognised as an integral component of doing any sort of business – especially as so much business today is done online. Related to this recognition is the need to elevate the topic of cyber security to the boardroom. While some more forward-thinking companies understand this need, there is still a large number of companies that aren't treating information security as a significant risk to the business. This in turn means they're unknowingly leaving gaps in policy – and it is in those gaps that cyber attackers thrive.

This has emerged in the results of research conducted by Kordia in March this year with more than 180 business decision-makers from New Zealand organisations with 20 or more employees. Respondents provided insight on a range of cyber security issues, including structures for reporting breaches to boards of directors and customers, completeness and effectiveness of tools available, and the presence of policies and training to support an appropriate information security posture.

The study showed that while businesses in New Zealand are generally well-prepared and positioned to respond to cyber security attacks, technology and business executives aren't aligned when it comes to information security. Also, medium-sized companies are more likely than their larger counterparts to leave themselves open to cyber-attacks, and business leaders have little confidence in policies to deal with the aftermath of a data breach.

In businesses with more than 200 employees, 82% of respondents said there are enough tools available to them to educate and assist their business in making informed cyber security decisions, compared to 58% for those with 60 – 99 employees.

Similarly, seven in ten respondents overall stated that their company currently has policies or training in place relating to online security, but the number drops to 58% for medium-sized businesses.

Businesses with 20 to 99 employees are less well prepared as they likely don't have the budget, the skills or the inclination to focus on information security. Instead, energies are more likely to be focused on operational issues.

But the most notable finding from the survey is that there is a lack of communication and alignment between Chief Executives/General Managers on the one hand and Chief Technology Officers on the other. IT staff members are much more likely to know there are policies or training systems in place relating to online security (84%), while only 54% of CEOs/GMs know this information. And while 70% of those who have cyber security policies in place are confident that those policies will prevent a cyber breach, the number comes down dramatically depending on who is asked: just 46% of CEOs/GMs believe

Peter Bailey, General Manager, Aura Information Security

that the policy in place will be effective in dealing with a cyber-attack.

That technical staff are more confident in the response policy is because they, and not the board of directors, are probably responsible for its design. The 'business' side either perceive the policy as inadequate, or they may simply not know enough about it to have a higher level of confidence.

In other words, cyber security is still broadly the remit of the IT department. Cyber security policy, which should flow from the highest levels of the company, is being left in the hands of the technologists.

And while those technologists can certainly provide input on policy, their real expertise typically lies in policy implementation, not determination.

The resulting shortcomings are the gaps which tend to emerge – particularly when vertical industry-specific protection, which depends on director-level understanding of the business, isn't appropriately implemented.

What should directors do about it? First, understand the risks and threats facing your business and what is being done to mitigate them. This requires knowledge of the 'attack surface'; what parts of your business are vulnerable, where the potential weak points are and how they are these protected. Understand the tools, systems and policies in place to ensure a breach does not occur. If it does happen, assess the likely impact of an attack on your business and/or customers, and how the impact will be managed (including from a media/communications perspective).

Secondly, ask plenty of questions on a regular basis. Talk to people at every level of the business, from the front line, to management, the CIO and the CISO. Engage experts for an outside comma - opinion, potential review of policies and procedures – invite them to speak or provide reports to the board. Request regular reporting on cyber for internal teams and check that the vendors and third party suppliers with which you work take a similar approach to security.

Finally, be a cyber champion and prioritise information security as a boardroom issue. Lead by example, foster a culture that sees cyber as a serious business issue, and treat the risk as a priority with sufficient funds allocated to it.

Like a chain, cyber security is only as strong as the weakest link. Only when the board takes it up as a regular issue which depends on its input, can cyber security become a company-wide issue.

THE COMPLEX WORLD OF WATER GOVERNANCE

One of the most contentious topics for communities in New Zealand presently is water. Chris Coughlan, business manager for Irrigation New Zealand, interviewed leaders and key influencers across political and philosophical boundaries, asking how they see the hierarchy of water governance and where tensions lie, with a particular interest in the role of irrigation scheme boards. Some key challenges and possible ways forward are highlighted here.

Water for New Zealand has been described as a 'Wicked Problem'.

For New Zealanders water is a passion; an integral part of our lives and our environment. It is also an important resource for agriculture and economic development. Our need to balance expectations to achieve optimal outcomes for all New Zealand is paramount.

While it has always been significant, the scrutiny of governance and management of water has never been greater, as competing needs and the environmental impact of land and water use has become better understood.

There are many layers of water governance in New Zealand. Water governance in New Zealand is not well integrated. There is responsibility for, or a connection to, water in almost every government department. There has been both a top-down and bottom-up approach to water governance in New Zealand. Approaches have worked well in combination, but a lack of co-ordination or alignment is now creating tensions as government shows increasing interest.

Managing our resources

New Zealand's primary legislation for the sustainable management of its natural and physical resources, the Resource Management Act (RMA), was passed in 1991 giving regional councils the power to implement change. The councils charged with implementing the RMA are often poorly resourced and approaches to water management vary across the country.

Irrigation schemes began as 'a collective of water users' attached through infrastructure. With the purchase of the infrastructure, these collectives co-ordinated their own leadership group or board under cooperative structures to ensure their schemes

Chris Coughlan

would continue to convey water to their shareholder's farm gate.

Irrigation scheme boards are now finding themselves in a far more complex situation.

Irrigation growth in New Zealand was a consequence of a collision of international events. New Zealand suddenly found itself, as a low cost producer of dairy products, with enormous economic opportunity. To take advantage of the opportunity and meet demand meant increasing production, and the answer to that was water and intensified land use.

As the degradation of our water ways has become more evident, environmental groups and the media have been increasingly effective in highlighting issues. This has done an enormous amount of damage to the confidence and trust placed, not only in irrigators and irrigation schemes as water users, but also 'brand Agriculture'.

The slow response to environmental expectations politically, regionally and by the primary sector led to the growing influence of less formal but significant voices being heard, such as media and NGOs. The accumulative effect of competing voices and government policy development, including environmental bottom lines, led to an unprecedented scope and pace of change, now experienced on the ground by irrigators and irrigation schemes.

Once conveyors of water to the farm gate, the role of irrigation schemes and their boards is now one of resource management. They are being ambitious, and investing significantly in supporting their shareholders in implementing change in water management but this is unchartered territory and not all benefits or pitfalls can be anticipated. Maintaining relationships, with both shareholders and councils as the granters of the consent, are of primary concern and this is going to be critical to their success.

Trust and diversity

This project, undertaken as part of the Kellogg Rural Leadership Programme, exposed deep challenges around trust and confidence at all levels of water governance in New Zealand. This research has highlighted an opportunity: to change perceptions so that irrigators and irrigation schemes are acknowledged as effective, legitimate and trusted users of water for the benefit of New Zealand. This is a first and critical step for irrigation schemes to 'break the ice' and become trusted users of water, our public resource.

Irrigation schemes need to be willing to embrace a more diverse and outward looking board. Many of those interviewed for the project challenge schemes to appoint truly independent directors to challenge their thinking and hold them to account. Building diverse boards that look outwards and have societal values will go a long way to building external confidence. As one interviewee pointed out "There has been some tinkering around the edges – mainly with lawyers and accountants and while they can be valuable additions the question needs to be 'what is the skill we need?' and 'what is the issue we are dealing with?'

Such an approach will be confronting but will provide transparency and openness to start discussion. It will also provide an opportunity to have realistic conversations and find reference points for communities to collaborate. That everything is connected – environment, society, economy – is not well understood. New Zealand is a modified landscape so a national conversation around what we want was identified through this report as an important forward step. We want vineyards, vegetable paddocks and orchards but also pristine water bodies – but what is realistic? If agriculture is still a cornerstone of the New Zealand economy and we all prosper from its success then the process for change needs to be a whole of society response.

This project also highlighted the role of a coordinated primary sector to build trust in those using our water and considers the possible impact of changing the models and structures of irrigation schemes. Could a hybrid model, where schemes are made up of irrigation shareholders and those with a wider view who bridge the gap to what society values, be an effective model?

The challenge going forward is that while these clear opportunities exist, trust is the big issue. Getting things right is not just the domain of irrigation schemes but the responsibility of all. Leaders and influencers have a responsibility at all levels – political, regulatory, environmental, scheme, community and on farm – they need to work together to build a robust and mutually beneficial framework – political, regulatory, environmental and social. A governance framework is required that is well integrated and reflects the values of catchment and community.

The challenges immediately facing irrigation schemes include the refinement and implementation of best practice for the governance of water, for current and future generations. For irrigation scheme boards to perform their roles with confidence, be effective and successful, they need to sit comfortably within New Zealand's wider water governance story. They need clarity of purpose, role and responsibility.

Chris Coughlan is business manager for Irrigation New Zealand. This article is based on a report produced as part of the 2016 Kellogg Rural Leadership Programme.

For the full report: kellogg.org.nz/alumni/projects

We're taking part in a conversation about water. The BoardRoom editor attended part of the LGNZ Water Symposium and will speak to experts in upcoming issues of the magazine about the governance of water in New Zealand. Look out for these pieces of the coming months.

New rules under Fire and Emergency New Zealand Act

The Fire and Emergency New Zealand Act, known as the FENZ Act, received Royal assent on 11 May 2017. Although its main purpose is to bring together the urban and rural fire services into a single unified fire services organisation from 1 July 2017, the legislation places great emphasis on compliance. The Act repeals previous fire legislation.

As Fire and Emergency New Zealand (FENZ) remains funded by those who seek to transfer risk from fire, earthquake and other perils to insurers, the Act introduces a strict compliance regime of record keeping, levy anti-avoidance and penalties. The levy part of the FENZ Act, Part 3, is now due to commence from 1 January 2019.

The purchase and negotiation of business insurance often sits with the chief financial officer or a director. Anyone who is responsible for an organisation's insurance policies should become familiar with the compliance regime the FENZ Act imposes on New Zealand's insurance-buying entities. This becomes a necessity for those who purchase insurance from an insurer, insurance broker or other insurance intermediary located overseas as the FENZ Act imposes additional penalties on any party deemed a "levy payer".

Fire property tax

Under the Fires Services Act tax was paid on fire insurance policies. Even policies that did not insure fire as the primary cause, such as a terrorism-only policy or earthquake-only policy, were subject to fire insurance tax according to the New Zealand Fire Service (NZFS). NZFS called this fire insurance tax a levy.

From 1 July 2017, as a direct result of the FENZ Act, the fire insurance tax will increase by 39.47%. This is the first step of the FENZ Act making insurance in New Zealand less affordable.

Property insurance tax

From 1 January 2019 the FENZ Act rewrites the rules for how fire levies will be applied to insurance policies. The levy changes from a tax on fire insurance policies to a tax on almost any insurance policy protecting property in New Zealand. The change to a property insurance tax is expected to see the levy payable by larger policyholders increase dramatically from 2019.

The amount on which the new levy will be charged also changes. Under the Fire Service Act most policyholders paid a levy based on the indemnity value of property insured under the Fire Service Act; under the FENZ Act the levy will instead apply to the amount insured. This may double the amount upon which the levy applies for the majority of policyholders.

From January 2019 the levy also applies to some liability policies, including third party only motor vehicle policies and potentially some parts of management liability policies. It is assumed the latter is unintended and results from poor drafting of the Act.

Compliance and levy payers

Part 3 of the FENZ Act introduces three new areas of compliance to levy payers: records, avoidance and greatly increased penalties, including up to two months imprisonment.

Whom the Act deems a levy payer is determined by whether the insurer is licensed by the Reserve Bank and whether an insurance broker or other insurance intermediary, if used to place an insurance policy with an overseas insurer, is located in New Zealand.

It is imperative directors understand whether the Act deems them as a policyholder to be a levy payer due to the additional compliance and potential penalties the Act subjects a levy payer to.

Records

Under the Fire Service Act the NZ Fire Service had limited powers to request information.

Part 3 of the FENZ Act changes this by introducing a record keeping requirement, necessitating insurance contracts subject to a levy to be retained by levy payers and insurance intermediaries for a minimum of seven years, which are to be available to FENZ upon demand.

Penalties for not doing so include fines of up to $50,000 or up to two months' imprisonment. The same penalties apply if false or misleading information is provided to FENZ.

Avoidance

A key part of the FENZ Act's levy rules is the introduction of levy anti-avoidance measures. Under the Fire Service Act avoiding paying a levy was not explicitly forbidden, although NZFS has successfully appealed court rulings on levy decisions that had gone against them.

Under the FENZ Act levy avoidance includes directly or indirectly altering the incidence of the levy and avoiding, postponing, or reducing any liability to pay the levy.

The FENZ Act as originally drafted treated a policyholder reducing their sum insured as an act of levy avoidance and therefore subject to penalties. Following submissions by Marsh and others the Act was amended to clarify that the extent to which property is not insured (in whole or in part) is not considered levy avoidance for the purposes of the Act.

Where the levy avoidance arrangement is deemed to have occurred FENZ gets to determine the levy payer's liability for levy in a way it considers appropriate. This will likely result in the policyholder incurring shortfall penalties.

Shortfall penalties

Under the Fire Service Act, late payment of levies resulted in interest payable of 1.5% per month and a penalty surcharge of 10% charged every six months levies remained unpaid.

Part 3 of the FENZ Act introduces a new penalty regime if the correct amount of levy is not calculated and paid to FENZ by the legislated date.

Under the Act it is FENZ that determines whether any wrong calculation of the levy is a result of not taking reasonable care, having taken an unacceptable levy position or gross negligence, and therefore the level of penalty that is applied.

Although the FENZ Act determines who the levy payer is, the Act makes the insurer, the policyholder and the broker or other insurance intermediary jointly and severally liable to pay any shortfall penalty. This means a policyholder may be liable for a shortfall penalty because of the actions of their insurer and/or insurance intermediary, and vice versa, although the Act also lists instances where being penalised for the act of another may be avoided.

Becoming aware

The levy changes being introduced from 1 January 2019 will likely result in additional compliance costs for all parties deemed to be levy payers under the Act. This may be the policyholder, the insurer and/or the broker/insurance intermediary. In many cases the need for additional compliance will apply upon all of the above.

The FENZ Act also appears to place a greater liability on the party responsible for determining the amount of levy charged.

As well as highlighting the importance of accurate insurance documentation record keeping, the Act means directors and officers of a business must ensure they are aware they are paying the correct levy and paying it by the designated time.

This knowledge becomes even more important as other parties to the insurance contract may choose to withdraw from offering this service due to the new penalty regime. The message for businesses is to choose your insurance professional well.

Disclaimer: *None of the above should be taken as legal advice. In addition a number of rules will appear as regulations outside of the Act. It is suggested legal advice is taken to understand how the compliance and penalty regime of part 3 of the Fire and Emergency New Zealand Act will affect you. In addition, the FENZ Act introduces additional non-levy penalties in other parts of the Act.*

Māori governance training – tailored to fit

Two and a half years in to their settlement Maungaharuru-Tangitū Trust were ready for some input and the new governance training course, developed by Te Puni Kōkiri in partnership with the Institute of Directors, was a perfect fit.

Eighteen participants from Maungaharuru-Tangitū Trust attended the course held in September. The group included the Trust's company directors, business partners, management staff and board members. "We heard about it from one of our TPK partners," says Trust CE Shayne Walker (Ngāti Kahungunu). "We wanted to build capability and grow everyone together. The IoD training gave us that opportunity."

The IoD, has a membership of almost 8000 members across the country, and as a founding member of the Global Network of Director Institutes, has a strong track record of delivering high quality governance services and were an easy partnership choice for TPK.

Susan Huria (Ngāi Tah u, Ngāi Tuāhuriri) is a Chartered Fellow with IoD and has facilitated training programmes for the IoD in the past. With over 20 years board experience including current positions on Ngāi Tahu Property and Marsden Maritime, Susan helped to develop the programme for Māori governance entities

and is one of a group of facilitators who delivered the training to Maungaharuru-Tangitū Trust. "The great thing is that we can tailor the examples to real-life issues that iwi are dealing with," says Susan. "So, if we're looking at strategy, it's their strategy we are talking about – not some other company's that they have no connection with."

Context is key in the delivery of the course and the programme highlights issues that are most significant to Māori. It draws on the aspirations as well as the needs of each entity while covering the three key areas of governance, strategy and finance.

Susan says that the issues Māori entities are grappling with are fairly generic across the range of organisations she has worked with. "Things like getting the right mix of culturally competent and commercially savvy people on board and director tenure – how long is too long and how do we ensure we retain the institutional knowledge?"

Three facilitators delivered the Napier based training and Susan's focus was strategy. "Most of the rōpū we are working with are really strong on vision and purpose. It's the nuts and bolts of how to achieve those things that I am most interested in them figuring out."

Currently involved in a range of initiatives, from environmental restoration projects to driver's licencing programmes for rangatahi, Shayne Walker says that for Maungaharuru-Tangitū Trust Susan's facilitation style was spot on. "It was great how she cut straight to it. Basically, a key message for us was just 'slow down'. We don't have to be achieving everything at once. What's more important is that we are doing the right things at the right time."

Course facilitators are drawn from experienced Māori practitioners all around the country and all have rated very strongly with participants. Shayne describes the finance session as "the most understandable financial education session our people have ever had."

While Māori governance entities are not new, the continued development of governance skills and best practise models for Māori in governance is a key issue for a growing number of iwi pre and post Treaty settlement. Twelve Māori entities from across the motu have participated in the governance training programme last year and the response from participants has been overwhelmingly positive. Shayne says they are looking to develop their learnings from the training further. "We want to ensure we are being authentic as leaders and in our dealings with others. Our focus is making good decisions for our people. Having the opportunity to explore what that means together has been invaluable."

Another twelve Māori entities will have the opportunity to participate in this training programme again this year.

Financial reporting – a changed landscape

Financial reporting in New Zealand is on the brink of the biggest change since the adoption of International Financial Reporting Standards (IFRS) a decade ago. Of key relevance to boards are three new accounting standards which will significantly change the accounting treatment of financial instruments, revenue and leases – with potential implications for the whole business.

Financial instruments

For those organisations with limited exposure to financial instruments, the impact may be minimal. However banks and other financial institutions will be more significantly impacted. Under the new standard, categorisation of financial assets has been streamlined from four categories to two. As a result, equity investments, such as shares in other entities, can now be recognised at fair value through other comprehensive income, potentially reducing profit or loss volatility.

Further, the global financial crisis in 2008 provoked criticism that loan provisions were recognised 'too little, too late'. A new impairment model was developed in response. The model requires entities to estimate expected losses when they first lend money or make an investment, recognising them immediately. This applies to all financial instruments exposed to impairment, including trade receivables.

Also, there is an easing of the rules around hedging making it more accessible. In light of this, boards may wish to reconsider treasury and risk management models to make greater use of hedging.

Revenue

For some entities, the new revenue standard will impact when they recognise revenue for accounting purposes. For example, revenue currently recognised at the start or end of a contract could be recognised over the contract term or vice versa. For most straightforward contracts there will be little or no impact. However, for contracts which extend over more than one accounting period or have multiple elements, the changes are likely to be more significant.

The new standard requires the recognition of revenue using a five-step approach. The core principles are:

- the transaction must occur in an agreement with another party that creates enforceable rights and obligations; and
- the contract includes sufficiently specific performance obligations.

An agreement is enforceable when the other party is able to enforce it through legal or equivalent means.

Under the new standard there is no longer an automatic right to recognise revenue (and hence profit) on a progressive basis. The new model replaces the percentage completion basis making it particularly relevant to entities with revenue from construction contracts. For some this could result in a mismatch between the timing of the recognition of revenue, and the expenses associated with earning that revenue.

The new standard only permits the recognition of revenue once performance obligations have been met. It is therefore vital that performance obligations are clearly defined in contracts. Boards may wish to reconsider the form and content of such contracts if the preference is to recognise revenue over time rather than at a point in time.

Leases

A significant change under the new standard is the removal of the differentiation between operating and finance leases. All leases will be recognised on the balance sheet as a right-to-use asset at fair value and a corresponding lease liability. The liability will be valued at the present value of future lease payments. The implications of this are far greater than just grossing up the balance sheet as the asset and liability will unwind at different rates. Determining the interest rate implicit in the lease will be challenging in cases where the discount rate to be used is not explicitly stated in the lease agreement.

The profile of expenses will also change. Rent will be replaced by depreciation and interest – the former an operating expense and above the profit line, and the latter not and therefore below the line. As a result – operating profit will increase, as will EBITDA. Debt covenants may also be impacted, as may other financial metrics including gearing and interest cover ratios. Employee incentive schemes linked to these types of measures may need to be reviewed, and of course there may be tax implications. This may lead boards to reconsider current leasing arrangements altogether, and reassess previous lease versus buy decisions.

Next steps

The date of transition to the new standards is the beginning of the comparative year. For financial instruments and revenue this was 1 January 2017, and for leases it is 1 January 2018. For many, in order to meet the requirement to disclose their assessment of the impact of these accounting standards issued but not yet effective on their financial performance and position, changes to business strategy and processes will be required. Such changes take time, and the time to act is now.

Zowie Pateman CA, Acting Reporting Leader, Chartered Accountants Australia and New Zealand

Action items at a glance:

1. **Professional development** – Provide relevant staff with training
2. **Contracts** – Analyse contracts and agreements and consider re-negotiating terms to maintain original intent
3. **Systems and processes** – Make changes to accounting systems to ensure sufficient data capture
4. **Compensation and bonus plans** – Review the impact of the new standards on key financial metrics and measures tied to remuneration
5. **Investor relations** – Educate stakeholders about changing results and ratios

Out & about

AUCKLAND

The branch has hosted a number of events over the past few months, including a breakfast with Air NZ CEO Christopher Luxon, and risk panel with speakers from IoD partners ASB, KPMG and Marsh.

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TARANAKI

In early April Taranaki branch hosted a panel discussion with a retail theme. In May the branch was pleased to hear from Tony Carter, with Tony passing on his seven governance lessons. You can read more about this on page 12 of the magazine.

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WAIKATO

In recent months Waikato branch members have attended events including a lunch function with Graeme Wheeler, a 2017 budget update with Hon Steven Joyce and taken governance lessons from Tony Carter.

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WELLINGTON

Wellington branch was pleased to host Callaghan Innovation CE Vic Crone, and Colin McDonald at events during May. Branch members also heard from Reserve Bank Governor Graeme Wheeler, discussing the New Zealand economy in 2017.

BAY OF PLENTY

In May the branch hosted Kevin Stirrat, discussing de-globalisation, geo-political conflict and the economy.

A number of branches are hosting members of parliament in the lead up to the 2017 Election; Bay of Plenty branch members hosted Hon Simon Bridges, sharing his experience of governance in Central Government.

1 | Rob Lee, Sharelle Burroughs (Auckland)
2 | Philip Whitmore, Kim Mundy, Costa Zakis (Auckland)
3 | Lindsay Render, Angela Buglass (Auckland)
4 | Carrie Hobson, Don Mann (Auckland)
5 | Pramod Khatri, Malcolm Sutherland (Taranaki)
6 | Craig Hattle, Craig Waite and Bill Roy (Taranaki)
7 | William Durning, Jan Gatley, Mark McCabe, Hon. Steven Joyce, Simon Lockwood, Kirsten Patterson (Waikato)
8 | Paul Bell, Marie Hall (Nelson Marlborough)
9 | Mike Stenhouse (Nelson Marlborough)
10 | Gordon Walker, Matthew Mark (Canterbury)
11 | Devanshi Gandhi, Meaghan Harrington, Hugh Baird, Daniel Chan, Katherine Pease (Canterbury)
12 | Krisztina Kormoczi, Vincent Pooch, Richard Hegan (Canterbury).

NELSON MARLBOROUGH

Andy Symons from PwC gave a fascinating insight into digital disruption and emerging technologies that could impact our businesses in the future. In May the branch hosted Sheffield for the exclusive release of their South Island leadership survey, and bid farewell to branch manager Jane Peterson who is now taking on a role with the IoD's head office.

CANTERBURY

During May Canterbury branch hosted Ngaire Best, talking the ins and outs of Crown appointments, and heard from Gordon Walker on how lessons from professional sports can be applied in the boardroom.

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OTAGO SOUTHLAND

Events during May included health and safety tips for directors and and an event with Michael Stiassny who addressed the question 'what keeps directors awake at night?' Then in early June members had the chance to attend a site visit to Dunedin International Airport with CEO Richard Roberts.

Company Directors' Course

QUEENSTOWN 14 MAY 2017

Front row: *Boyd Williams, George Carter, Phillip Roth, Steve Gracey, Ella Farrell, Vivienne Bryner, Kate Morrison, Manaia Cunningham, Kevin Arthur, Robert Brewer, Graham Clark*

Back row: *Brent Cook, Alison Shanks, Sinead Horgan, Krisztina Kormoczi, Martin Veitch, Alan Williams, Michelle Henderson, Graeme Finlay, Christopher Watney, Siobhan Quayle, Jane Leahy, Jim Lindsay, Chris Gregory*

INSTITUTE OF DIRECTORS

Events Diary

For more information visit www.iod.org.nz, or contact the director development team or your local branch office

Self-paced study

Online modules can be completed anytime, anywhere and at your own pace.

- Directors' and Officers' Insurance
- Ethics – How directors do business
- Health and Safety Governance
- Not-for-Profit Finance Fundamentals
- Hot topics for SME directors webcast

Webinar

1 AUGUST
Chairing Fundamentals

Auckland

28 JUNE
Finance Essentials

01 JULY
Not-for-Profit Governance Essentials, Albany

03 JULY
Director Accelerator Lunch

7 JULY
Breakfast with John Spencer, Lions Tour Manager

10 JULY
Company Directors' Course – Non-residential

25 JULY
Advanced Health and Safety Governance

26 JULY
Digital Essentials

01 AUGUST
Governance Essentials

02 AUGUST
Finance Essentials

03 AUGUST
Strategy Essentials

08 AUGUST
Lunch function with Jeremy Jones

08 AUGUST
Next Generation Director workshop, Auckland CBD

17 AUGUST
Cocktail meeting in Whangarei with Rachel Hopkins

29 AUGUST
Welcome cocktails and 2017 Emerging Director Award

29 AUGUST
Governance Essentials

30 AUGUST
Finance Essentials

Bay of Plenty

05 JULY
Next Generation Workshop, Tauranga

19 JULY
Governance in agriculture with Will Wilson, Taupo

27 JULY
New members dinner, Tauranga

22 AUGUST
Governance Essentials, Tauranga

23 AUGUST
Risk Essentials, Tauranga

Taranaki

05 JULY
Risk Essentials, New Plymouth

13 JULY
Lunch event with Kirsten Patterson, New Plymouth

Waikato

04 JULY
Lunch event with Colin Groves, Hamilton

23 AUGUST
Lunch function with Prof. Neil Quigley, Hamilton

Wellington

28 JUNE
New members after 5 welcome event

08 AUGUST
Governance Essentials

09 AUGUST
Digital Essentials

10 AUGUST
Risk Essentials

11 AUGUST
Finance Essentials

15 AUGUST
State Sector Governance

20 AUGUST
Company Directors' Course

Nelson Marlborough

6 JULY
Lunch function with John Palmer ONZM

Canterbury

6 JULY
Sponsors panel discussion with University of Canterbury

24 JULY
Informal influencing techniques

28 JULY
New members luncheon

4 AUGUST
Sponsors lunch with Marsh Ltd

09 AUGUST
Advanced Health and Safety Governance

10 AUGUST
Governance CV workshop with Kelly McGregor

Otago Southland

28 JUNE
Strategy Essentials, Dunedin

29 JUNE
Risk Essentials, Dunedin

20 JULY
Presentation of 2017 Emerging Director Award with speaker, Lauren Semple

10 AUGUST
Advanced Health and Safety Governance, Dunedin

17 AUGUST
Lunch event with Suzanne Snively