

CONFLICTS AND COHERENCE IN THE CHARITIES SPHERE: WOULD A CONFLICT BY ANY OTHER NAME PROSCRIBE THE SAME?

(2020) 14 Journal of Equity
ROSEMARY TEELE LANGFORD

Abstract: Proscriptions on conflicts of interest have long been a core component of governance regimes. In the charities sphere such proscriptions arise from a number of sources, including general law, statute and governance standards articulated by the regulator. Unfortunately the wording of relevant conflicts duties varies extensively, giving rise to acute incoherence and uncertainty. This article undertakes detailed critical analysis of the myriad of conflicts duties in order to provide certainty and comprehensive guidance. This resolution is relevant beyond the charitable sphere given the multitude of ways in which conflicts proscriptions are expressed in other governance contexts.

CONTENTS

I	Introduction	1
II	Overview of Regulation	3
III	General Law	3
IV	Statutory duties	8
A	Material Personal Interests	9
B	Directly and Indirectly Interested	13
C	Holding an Office or Having an Interest in Property whereby Directly or Indirectly Duties or Interests might be Created that could Conflict with the Directors' Duties or Interests	15
D	Direct or Indirect Pecuniary Interest in a Contract or Proposed Contract with the Association	16
E	Comparison with General Law Standard	17
V	ACNC Governance Standard 5	18
A	Perceived or Actual Material Conflicts of Interest	20
1	Meanings	21
VI	Conclusion	32

I INTRODUCTION

BA, LLB (First Hons) (Melb), PhD (Mon); Associate Professor, Melbourne Law School, University of Melbourne. This research was funded by the Australian Government through the Australian Research Council. My thanks to the many people I consulted on this topic and to Miranda Webster for research assistance.

According to the rule of law, for rules and rulings to be a reliable guide for citizens and form reasons for action and normative guidance, law should be clear, consistent, predictable and publicly known.¹ These attributes are notably absent from the incohesive collection of obligations that regulate conflicts of interest in the charitable sphere. Persons who govern charitable entities are subject to conflicts proscriptions under general law, statute and regulations of the Australian Charities and Not-for-profits Commission ('ACNC'). Relevant provisions range from 'material personal interests' to being 'directly or indirectly interested' to 'perceived or actual material conflicts of interest'. And more than one provision will apply to the one person.

This deep incoherence in the way that the myriad of governance obligations imposed on responsible persons are expressed was highlighted by the Committee reviewing the Australian Charities and Not-for-profits Commission legislation ('the ACNC Review'):

[T]he current system of different governance requirements is complex and confusing. It is unreasonable to expect volunteer directors working in the sector to understand and comply with multiple jurisdictional and sometimes inconsistent governance requirements. While there are common themes across the competing governance requirements, such as duties to act honestly and avoid conflicts, the expression of those duties differs between them and imposes an unacceptable level of red tape.²

The aim of this article is to simplify and synthesise these requirements. On closer analysis, each of the relevant obligations proscribing conflicts can be seen as subsets of the overarching general law duty to avoid unauthorised conflicts, based on a standard of real sensible possibility of conflict. Synthesising and mapping these interrelated duties is essential in bringing coherence and certainty to the governance landscape. This analysis is relevant more broadly to for-profit companies as well, given the differing terms used by statute and general law in that sphere, and the lack of clarity as to whether non-pecuniary and third party interests are included within the interests that need to be disclosed.

Given that this incoherence has been caused to a large extent by multiple layers of regulation, the solution is unlikely to be more legislation. The ACNC Review recommended a referral of power by the states and territories to the Commonwealth government.³ In the meantime the challenge is to develop a coherent framework for those who govern charitable entities. This article takes up the challenge as concerns conflicts of interest. A corollary of this analysis is an assessment of the suggestion

¹ See Matthew Harding, 'Equity and the Rule of Law' (2016) 132(2) *Law Quarterly Review* 278.

² Commonwealth of Australia, *Strengthening for Purpose: Australian Charities and Not-for-profits Commission Review Legislation Review - Report and Recommendations 2018* (2018) 47 ('the ACNC Review'). This review was conducted to meet the Commonwealth Government's statutory obligation to undertake a review of the *Australian Charities and Not-for-profits Commission Act 2012* (Cth) and the *Australian Charities and Not-for-profits (Consequential and Transitional) Act 2012* (Cth) after their first five years of operation: see *Australian Charities and Not-for-profits (Consequential and Transitional) Act 2012*, s 16.

³ See ACNC Review (n 2) 21, 102, 113.

that the concept of ‘perceived material interest’ be removed from the governance standards imposed under the ACNC Regulations.⁴

II OVERVIEW OF REGULATION

There are a number of different types of charitable entities including trusts, companies limited by guarantee, statutory corporations, incorporated associations, unincorporated associations and co-operatives. Governance requirements vary according to the type of entity. The charitable sector is regulated by the ACNC.⁵ Persons who govern charitable entities are known as responsible entities or responsible persons. Responsible persons are subject to a number of requirements relating to governance. These stem from general law (ie, common law and equity), statute and ACNC Governance Standard 5, which sets out governance obligations of responsible persons.⁶ Responsible persons may also be subject to requirements under industry codes and funding agreements.⁷ The duplication and complexity have been a cause of consternation and concern.⁸

III GENERAL LAW

The core fiduciary duties to avoid unauthorised conflicts and profits apply to trustees and directors. Scholars argue that these duties also apply to directors of co-operatives and members of management committees of incorporated associations.⁹ This is

⁴ See *ibid* 48, 50.

⁵ See *Australian Charities and Not-for-profits Commission Act 2012* (n 2) ss 5-10(1), 105-5.

⁶ See *Australian Charities and Not-for-profits Commission Regulation 2013* (Cth) reg 45.25(2); *Australian Charities and Not-for-profits Commission Act 2012* (n 2) ch 3. Note also the External Conduct Standards: see *Australian Charities and Not-for-profits Commission Regulation 2013*, div 40; *Australian Charities and Not-for-profits Commission Act 2012* (n2) ch 3. ACNC Governance Standard 5 is set out in Section V below.

⁷ See, eg, the Code of Governance for the Australian Community Sector; the Australian Council for International Development ‘Code of Conduct’; the Australian Institute of Company Directors, ‘Good Governance Principles and Guidance’, cited in ACNC Review (n 2) 44.

⁸ See, eg, Ian Ramsay and Miranda Webster, ‘Registered Charities and Governance Standard 5: An Evaluation’ (2017) 45(2) *Australian Business Law Review* 127; Kim D Weinert, ‘Legal Duties as Part of the Governance Framework for Incorporated Associations: A Comparative Analysis’ (2014) 29(1) *Australian Journal of Corporate Law* 38.

⁹ Bruce Cowley and Stephen Knight, *Duties of Board and Committee Members: A Guide for Corporations, Associations and Statutory Bodies* (Lawbook Co, 2018) [11.600], [13.120]; AS Sievers, ‘What Is the Future for Honorary Directors and Committee Members? Their Duties and Liabilities’ in Myles McGregor-Lowndes, Keith Fletcher and AS Sievers (eds), *Legal Issues for Non-Profit Associations* (LBC Information Services, 1996) 30; Charles Parkinson, ‘Duties of Committee Members under the Associations Incorporation Acts’ (2004) 30(1) *Monash University Law Review* 75, 79.

reinforced by reg 45.25(1) of the *Australian Charities and Not-for-profits Commission Regulation 2013* (Cth).¹⁰

In *Aberdeen Railway Co v Blaikie Bros*¹¹ Lord Cranworth said:

[I]t is a rule of universal application that no one, having such duties to discharge, shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect. So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.¹²

The rationale behind the duty to avoid conflicts ('the conflicts rule') has been described as 'to preclude the fiduciary from being swayed by considerations of personal interest'¹³ and also to ensure that fiduciaries generally conduct themselves 'at a level higher than that trodden by the crowd'.¹⁴

The conflicts rule encompasses conflicts of interest and conflicts of duties. The conflicts rule supports the operation of the more fundamental duty to act in good faith in the interests of the entity and is, in a sense, a corollary of that rule. Conduct or inaction that breaches the conflicts rule is also likely to breach the duty to act in good faith in the interests of the entity and is often litigated under that duty.¹⁵ The duty to act in good faith in the interests of the entity has additional roles in relation to conflicts.¹⁶ For example, it may require extra action of conflicted fiduciaries and proscribes conflicts and profits that relate to third parties.¹⁷

Following the judgment of Lord Upjohn in *Boardman v Phipps*,¹⁸ the test has been one of 'real sensible possibility of conflict'. His Lordship said:

¹⁰ Regulation 45.25(1) of the *Australian Charities and Not-for-profits Commission Regulation 2013* (n 6) states: 'The object of this governance standard is (1) to ensure that the responsible entities of a registered entity conduct themselves in the manner that would be necessary if: (i) the relationship between them and the entity were a fiduciary relationship; and (ii) they were obliged to satisfy minimum standards of behaviour consistent with that relationship ...'

¹¹ (1854) 1 Macq 461 (HL).

¹² Ibid 471–2.

¹³ See *Chan v Zacharia* (1984) 154 CLR 178, 198–9 (Deane J). See also *Bray v Ford* [1896] AC 44 (HL) 51.

¹⁴ See *Warman International Ltd v Dwyer* (1995) 182 CLR 544, 557.

¹⁵ In the corporate sphere see, eg, *Chew v The Queen* (1991) 4 WAR 21, 49; *Digital Cinema Network Pty Ltd v Omnilab Media Pty Ltd (No 2)* [2011] FCA 509, [158]; *Australian Securities and Investments Commission v Maxwell* (2009) 59 ACSR 373, 400 [106]; *Australian Securities and Investments Commission v Macdonald (No 11)* (2009) 23 FLR 1, 111 [664]; *Re Wan Ze Property Development (Aust) Pty Ltd* (2012) 90 ACSR 593, 601–2 [35].

¹⁶ See Rosemary Teele Langford, *Company Directors' Duties and Conflicts of Interest* (Oxford University Press, 2019) 18–19 [2.18]–[2.21], 294–300 [10.07]–[10.23].

¹⁷ Ibid 291–300 [10.01]–[10.23]. Benefits to third parties may also contravene the duty to act for proper purposes or constitute a fraud on a power see, eg, Geraint W Thomas, *Thomas on Powers* (Oxford University Press, 2nd ed, 2012) 415–20 [9.26]–[9.34].

¹⁸ [1967] 2 AC 46 (HL).

The phrase ‘possibly may conflict’ requires consideration. In my view it means that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict: not that you could imagine some situation arising which might, in some conceivable possibility of events not contemplated as real sensible possibilities by any reasonable person, result in a conflict.¹⁹

Another phrase used in Australia is ‘real or substantial possibility of conflict’. Thus, in *Pilmer v Duke Group Ltd (in liq)*²⁰ McHugh, Gummow, Hayne and Callinan JJ (quoting, in part, *Hospital Products Ltd v United States Surgical Corporation* (Mason J))²¹ stated:

[T]he fiduciary is under an obligation, without informed consent, not to promote the personal interests of the fiduciary by making or pursuing a gain in circumstances in which there is ‘a conflict or a real or substantial possibility of a conflict’ between personal interests of the fiduciary and those to whom the duty is owed.

The test is objective²² and the interest may be expectant or contingent.²³

These phrases indicate that something less than actually being in a situation of conflict is sufficient for the conflicts rule to be breached. Australian case law sets a threshold of real sensible possibility of conflict or real or substantial possibility of conflict.

A particular question that arises is whether the conflicts rule encompasses non-pecuniary interests and interests of third parties. Non-pecuniary conflicts are personal conflicts that do not entail a financial benefit. An example would be gains in terms of experience and skills, or money being given to research centres with which responsible persons are associated. Third party conflicts are conflicts that involve the interests of a third party. An example would be conferral of a benefit on a fiduciary’s sibling, cousin or friend.

In terms of judicial consideration of inclusion of non-pecuniary and third party interests within the conflicts rule, English and Australian case law demonstrates that the conflicts rule includes an interest as a shareholder (whether held beneficially or as trustee)²⁴ and that the rule extends to partnerships of which a fiduciary is a partner.²⁵

¹⁹ Ibid 124.

²⁰ (2001) 207 CLR 165, 199 [78]. See also *Bell Group Ltd (in liq) v Westpac Banking Corp (No 9)* (2008) 39 WAR 1, 560 [4512].

²¹ (1984) 156 CLR 41, 103.

²² See, eg, *Australian Securities and Investments Commission v Adler* (2002) 168 FLR 253, 412 [735]; *Robash Pty Ltd (ACN 008 975 773) v Gladstone Pacific Nickel Pty Ltd* (2011) 86 ACSR 432, 452–3 [78]; *Burns v Financial Conduct Authority* [2018] 1 WLR 4161 (CA) 4183 [75]; *Richmond Pharmacology Ltd v Chester Overseas Ltd* [2014] Bus LR 1110 (Ch) 1124–5 [70]–[72].

²³ See, eg, *Grimaldi v Chameleon Mining NL (No 2)* (2012) 200 FCR 296, 346 [180]; *Bell Group Ltd (No 9)* (n 20) 559 [4509].

²⁴ See *Transvaal Lands Co v New Belgium (Transvaal) Land and Development Co* [1914] 2 Ch 488, 503 (Swinfen Eady LJ).

It also extends to corporate vehicles associated with a fiduciary²⁶ (particularly, but not exclusively, where the vehicle is the alter ego of the fiduciary), although some cases examine the extent of the interest.

Case law relating to trusts equivocated on whether a benefit to a trustee's spouse included a benefit to the trustee.²⁷ An influential factor was whether the fiduciary himself or herself was receiving a direct or indirect benefit. In the Australian case of *Vanguard Financial Planners Pty Ltd v Ale*²⁸ a benefit to a director's wife constituted a conflict of interest but not necessarily a profit from position.²⁹

The bottom line in cases involving non-pecuniary interests and interests of friends or relatives is whether the interest amounts to a real sensible possibility of conflict on the part of the fiduciary. This was the approach taken in the English case of *Breitenfeld UK Ltd v Harrison*,³⁰ in which a managing director caused his company to enter into contracts and to undertake dealings with a newly founded company owned by his son and daughter-in-law. Third party interests were also included in the Hong Kong case of *Esquire (Electronics) Ltd v The Hong Kong and Shanghai Banking Corporation Ltd*,³¹ which involved a senior partner selling his principal's property to his junior partner in a private sale.³²

On the other hand, the line needs to be drawn somewhere. As mentioned, the touchstone is provided by the requirement that the interest (whether pecuniary, non-pecuniary or third party) must amount to a real sensible possibility (or real or substantial possibility) of conflict.

Another, arguably attractive, approach is that of David Richards J in the English case of *Newgate Stud Co v Penfold*³³ (which concerned benefits to a director's partner and her father). In evaluating the law concerning the application of the self dealing

²⁵ See, eg, *Imperial Mercantile Credit Association (in liq) v Coleman* (1873) LR 6 HL 189 ('Coleman'); *National Grid Electricity Transmission plc v McKenzie* [2009] EWHC 1817 (Ch) [114], [118] ('McKenzie').

²⁶ See, eg, *Coleman* (n 25); *Aberdeen Railway* (n 11); *Transvaal Lands* (n 24) 503; *Todd v Robinson* (1884) 14 QBD 739; *Re Thompson's Settlement* [1986] Ch 99; *Movitex Ltd v Bulfield* [1988] BCLC 104 (Ch); *McKenzie* (n 25) [114], [118]; *Gencor ACP Ltd v Dalby* [2000] 2 BCLC 734 (Ch); *Aerostar Maintenance International Ltd v Wilson* [2010] EWHC 2032 (Ch) [202]–[207]; *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 140 [110]. See also *Grimaldi (No 2)* (n 23) 415–16 [557].

²⁷ For cases see *Burrell v Burrell's Trustees* [1915] SC 333 (Inner House) 337; *Robertson v Robertson* [1924] NZLR 552; *Tanti v Carlson* [1948] VLR 401, 407; *Re Douglas* [1928] 29 SR (NSW) 48; *Tito v Waddell (No 2)* [1977] Ch 106, 240; *Re King's Will Trusts* (1959) 173 EG 627; *McPherson v Watt* (1877) 3 App Cas 254; 5 R (HL) 9; *Woodfull v Lindsley* [2004] 2 BCLC 131 (CA); *Re McNally (dec'd)* [1967] NZLR 521, 523. See also *Ferraby v Hobson* (1847) 2 Ph 255, 261; 41 ER 940, 943.

²⁸ (2018) 354 ALR 711.

²⁹ Cf *Grimaldi (No 2)* (n 23) 346 [180].

³⁰ [2015] 2 BCLC 275 (Ch) 292–3 [67].

³¹ [2005] 3 HKLRD 358 (CFI) [41]–[42].

³² For further discussion see Remus Valsan, 'Fiduciary Duties, Conflict of Interest, and Proper Exercise of Judgment' (2016) 62(1) *McGill Law Journal* 1.

³³ [2008] 1 BCLC 46 (Ch).

rule³⁴ to benefits to spouses, his Honour observed that social changes necessitate reappraisal of the approach to spouses and potential extension of the rule to other couples.³⁵ David Richards J concluded that:

What is however true is that in any such relationship there exists the potential for the exercise of fiduciary duties to be influenced by personal considerations. If a director causes his company to enter into a transaction with a close relation, or a spouse or other partner, there is a significant risk that the director will be compromised by a desire to favour the other party ...³⁶

In his Honour's view, the solution (in cases where the fiduciary does not have a personal interest in the transaction but may be influenced by 'personal loyalties') is to put the burden on the fiduciary to demonstrate that the transaction is 'demonstrably in the best interests of the company'.³⁷

This approach of switching the onus to the fiduciary has been taken in other cases.³⁸ It has significant merit. Where the circumstances involve a personal relationship rather than a direct monetary or other benefit to a fiduciary, it is sensible to shift the onus to the fiduciary to demonstrate that the course of dealing is in the interests of the entity. It is also important to remember that interests not encompassed by the conflicts rule may well result in a responsible person breaching the duty to act in good faith in the interests of the entity. Indeed some authorities have seen third party interests as more relevant to the discharge and application of this duty than the conflicts and profits rules.³⁹ In this respect David Richards J's proposition that, in the case of personal conflicts, the onus be placed on the fiduciary to show that the transaction was in the interests of the entity, has appeal.

Part of the problem in ascertaining the extent of the conflicts rule is arguably, as identified by Smith, the fact that there is no definition of the term 'conflicts of interest' in the cases.⁴⁰ Smith argues that the word 'interest', in the context of conflicts of interest, means 'something that is of value to the person in question', noting that 'self-interest, of course may be pecuniary or non-pecuniary; my interests include the welfare of those who are important to me ...' The adoption of this definition would also be beneficial.

In summary, the fiduciary duty to avoid conflicts arises at a point before the fiduciary is actually affected by a conflict, namely where there is a real sensible (or real or substantial) possibility of conflict. The extension of the duty to non-pecuniary

³⁴ The self dealing rule applies where a trustee (or other fiduciary) sells property (or property the subject of a fiduciary obligation) to themselves.

³⁵ *Newgate Stud* (n 33) 105 [237]–[239].

³⁶ *Ibid* 105–6 [240].

³⁷ *Ibid* 106 [242].

³⁸ *Bristol and West Building Society v Mothew* [1998] Ch 1, 18 ('Mothew'). See also *Murad v Al-Saraj* [2005] WTLR 1573 (CA) [82].

³⁹ See, eg, *Bell Group Ltd (No 9)* (n 20) 561–2 [4520]–[4521].

⁴⁰ See Lionel Smith, 'Conflict, Profit, Bias, Misuse of Power: Dimensions of Governance' in Paul B Miller and Matthew Harding (eds), *Fiduciaries and Trust: Ethics, Politics, Economics and Law* (Cambridge University Press, forthcoming 2020).

and third party interests is not fully settled, although where such interests amount to a real sensible possibility of conflict on the part of the fiduciary there will be a breach. An appealing option is for the onus to be shifted to the fiduciary where non-pecuniary and third party interests are at stake. In contrast to the position at general law, it will be shown below that the ACNC is firmly of the view that such interests must be disclosed for the purposes of ACNC Governance Standard 5.

IV STATUTORY DUTIES

Over time statutory duties have also been imposed on responsible persons. There are multiple statutory duties requiring disclosure of interests in legislation relating to co-operatives and incorporated associations.⁴¹ In terms of the terminology employed, these can be grouped into four sub-categories:

- (1) material personal interest;⁴²
- (2) directly or indirectly interested;⁴³
- (3) holding an office or having an interest in property whereby, whether directly or indirectly, duties or interests might be created that could conflict with the directors' duties or interests as director;⁴⁴
- (4) direct or indirect pecuniary interest in a contract or proposed contract with the association.⁴⁵

The exceptions to these duties and consequences of breach, however, differ. It is notable that neither Queensland nor Tasmania impose duties on management committee members of associations. General law duties and the indirect duties imposed by ACNC Governance Standard 5 nevertheless apply.

At this point in time the statutory duties in ss 180–183 and 191–194 of the *Corporations Act 2001* (Cth) have been 'turned off'.⁴⁶ However, the ACNC Review

⁴¹ See *Corporations Act 2001* (Cth) s 191; *Co-operatives National Law*, s 208 [*The Co-operatives National Law* is set out in the appendices to the *Co-operatives (Adoption of National Law) Act 2012* (NSW); *Co-operatives National Law (ACT) Act 2017* (ACT); *Co-operatives (National Uniform Legislation) Act 2015* (NT); *Co-operatives National Law (South Australia) Act 2013* (SA); *Co-operatives National Law (Tasmania) Act 2015* (Tas); *Co-operatives National Law Application Act 2013* (Vic)] ('*Co-operatives National Law*'); *Cooperatives Act 1997* (Qld) s 227; *Co-operatives Act 2009* (WA) s 220; *Associations Incorporation Act 1991* (ACT) s 65; *Associations Incorporation Act 2009* (NSW) s 31; *Associations Act 2003* (NT) s 31; *Associations Incorporation Act 1985* (SA) s 31; *Associations Incorporation Reform Act 2012* (Vic) s 80; *Associations Incorporation Act 2015* (WA) s 42.

⁴² See *Associations Incorporation Reform Act 2012* (Vic) (n 41) s 80(1); *Associations Incorporation Act 1991* (ACT) (n 41) s 65; *Associations Incorporation Act 2015* (WA) (n 41) s 42; *Corporations Act 2001* (n 41) s 191.

⁴³ See *Co-Operatives National Law* (n 41) s 208; *Co-Operatives Act 1997* (Qld) (n 41) s 227; *Co-Operatives Act 2009* (WA) (n 41) s 220(1); *Associations Incorporation 2009* (NSW) (n 41) s 31.

⁴⁴ See *Co-Operatives National Law* (n 41) s 208(5); *Co-Operatives Act 1997* (Qld) (n 41) s 227(5); *Co-Operatives Act 2009* (WA) (n 41) s 220(5).

⁴⁵ *Associations Act 2003* (NT) (n 41) s 31; *Associations Incorporation Act 1985* (SA) (n 41) s 31.

has recommended that these duties be turned back on. In addition, jurisprudence surrounding the statutory duties in the *Corporations Act* is far more extensive than that concerning the equivalent duties in incorporated associations and co-operatives legislation. These provisions will therefore also be included in the analysis in this article.

It is therefore necessary to probe the terms ‘material personal interest’, ‘directly or indirectly interested’ and ‘direct or indirect pecuniary interest’ to bring clarity. The third category encompasses duties or interests that conflict with the directors’ duties or interests, thus importing the considerations outlined in Section III above concerning the general law duty. Aside from s 191 of the *Corporations Act* and its predecessors, there has been scant consideration of these provisions. A search of explanatory memoranda, other relevant commentary and judicial consideration of these statutory sections yielded no relevant results.

A Material Personal Interests

As mentioned above, some statutory sections applicable to responsible persons refer to material personal interests. An example is s 80 of the *Associations Incorporation Reform Act 2012* (Vic), which states: ‘(1) A member of the committee of an incorporated association who has a material personal interest in a matter being considered at a committee meeting must ... disclose the nature and extent of that interest to the committee.’⁴⁷ This is similar to s 191 of the *Corporations Act* which provides: ‘A director of a company who has a material personal interest in a matter that relates to the affairs of the company must give the other directors notice of the interest [subject to the exceptions in s 191(2)].’

There are, however, differences in terms of the nexus with the entity. Section 191 of the *Corporations Act* refers to ‘in a matter that relates to the affairs of the company’. By contrast, s 80(1) of the *Associations Incorporation Reform Act 2012* (Vic) refers to ‘in a matter being considered at a committee meeting’.⁴⁸ Exceptions also vary.⁴⁹

⁴⁶ In its recently released response to the ACNC Review, the Australian Government has said it will release a consultation paper seeking the views of the sector on turning these duties back on – see Commonwealth of Australia, *Government Response to the Australian Charities and Not-for-profits Commission Legislation Review 2018* (6 March 2020) 12. Note that s 184 (which imposes criminal liability for breach of ss 181–183) and s 588G (insolvent trading duties) are, however, still in force. The state Trustee Acts do not impose duties relating to conflicts and members of management committees of unincorporated associations are not subject to statutory duties.

⁴⁷ Section 80(2) outlines the details of disclosure to the next general meeting and s 80(3) sets out exceptions.

⁴⁸ See also *Associations Incorporation Act 1991* (ACT) (n 41) s 65(1). Section 42(1) of the *Associations Incorporation Act 2015* (WA) (n 41) refers to ‘in a matter being considered at a management committee meeting’.

⁴⁹ See, eg, *Associations Incorporation Act 1991* (ACT) (n 41) s 65(2); *Associations Incorporation Reform Act 2012* (Vic) (n 41) s 80(3); *Associations Incorporation Act 2015* (WA) (n 41) s 42(3). Section 191(2) of the *Corporations Act* has an extensive list of exceptions.

In order to bring coherence and certainty to this area of the law, it is necessary to determine what the concept of ‘material personal interest’ entails and whether it differs from the general law standard of real sensible possibility of conflict.

In *McGellin v Mount King Mining NL*⁵⁰ Murray J equated materiality with something having the capacity to influence the vote of the particular director upon the decision to be made.⁵¹ If it has this effect, then it is not relevant whether the interest is direct or indirect, vested or contingent.⁵² According to Murray J, it is the substance of the interest, its nature and capacity to have an impact upon the ability of the director to discharge their fiduciary duty that will be important.⁵³ The term ‘material’ therefore relates to the substance of the interest (rather than the likelihood of it causing a conflict). Murray J stated that: “‘Material’ in this context, I think, means that the interest involves a relationship of some real substance to the matter under consideration or the contract or arrangement that is proposed.”⁵⁴

The Australian Securities and Investments Commission (‘ASIC’) has stated the following: ‘The word ‘material’ implies that the interest needs to be of some substance or value, rather than merely a slight interest. An interest of small value does not warrant further notice or inquiry.’⁵⁵

The concept of material personal interest in s 191 of the *Corporations Act* has been the subject of detailed scholarly research.⁵⁶ Particular queries have arisen as to whether the term material personal interest in s 191 of the *Corporations Act* includes conflicting duties and how the concept of material personal interest differs from that of real sensible possibility of conflict.

As to the first question, it has been shown elsewhere⁵⁷ that the better view is that conflicting duties are included. This is because (1) a close review of the Parliamentary materials surrounding s 191 demonstrates no intention to exclude conflicting duties from the disclosure requirements; (2) evidence indicates that those responsible for reforming the statutory disclosure provisions viewed conflicts of interest as including conflicting duties and there was thus no need to explicitly include reference to conflicting duties; and (3) conflicting duties have the potential to inhibit directors’ exercise of their powers and duties in good faith in the interests of the company and,

⁵⁰ (1998) 144 FLR 288.

⁵¹ Ibid 304.

⁵² Ibid.

⁵³ Ibid.

⁵⁴ Ibid. For further discussion of the term ‘material’ see Peter Watts, *Directors’ Powers and Duties* (LexisNexis, 2nd ed, 2015) 226-9 [8.5]; RP Austin and IM Ramsay, Lexis Advance, *Ford, Austin & Ramsay’s Principles of Corporations Law* (online at 26 December 2019) [9.130.3].

⁵⁵ ASIC, *Regulatory Guide No 76: Related Party Transactions* (30 March 2011) RG 76.33 (‘ASIC RG 76.33’), referring to *Grand Enterprises Pty Ltd v Aurium Resources Ltd* (2009) 256 ALR 1, 15–16.

⁵⁶ See Rosemary Teele Langford and Ian Ramsay, ‘Is a Conflict of Interest under the General Law the same as a Material Personal Interest under the Corporations Act?’ (2018) 36 *Company and Securities Law Journal* 284; Rosemary Teele Langford and Ian Ramsay, ‘Does S 191 of the Corporations Act Include Conflicting Duties?’ (2019) 36 *Company & Securities Law Journal* 587.

⁵⁷ Langford and Ramsay, ‘S 191 of the Corporations Act’ (n 56).

from a policy perspective, should therefore be disclosed in the same way as conflicts of interest.⁵⁸ The word ‘personal’, however, arguably indicates that the relevant interest must affect the director personally in the sense that it affects their ability to make decisions in the best interests of the company.

A second question surrounds whether the term ‘material personal interest’ is the same as the term ‘real sensible possibility of conflict’. This raises the question of the difference between the terms ‘material’ and ‘real sensible possibility of’. It can be seen that both terms qualify the relevant interest or conflict. However, the words ‘material’ and ‘real sensible possibility of’ have different functions. ‘Material’ relates more to the impact on the decision-maker and the substance or extent of the interest. The words ‘real sensible possibility of’ relate to the likelihood of the conflict arising. In other words, ‘material’ qualifies the interest (or conflict) and ‘real sensible possibility of’ qualifies the likelihood of the conflict arising. However, in *McGellin Murray J* seemed to conflate the concepts when referring to the general law test in stating that the conflict of interest must ‘of itself, be of a real or substantial kind’.⁵⁹ In *European Pacific Resources Pty Ltd v Aurifax Mining NL* ‘material’ was equated with ‘more probable than not’⁶⁰ — in other words, the Court used the term ‘material’ to qualify the likelihood of the interest arising.

In addition, cases applying the general law conflicts rule have considered the substantiality or materiality of the interest. For example, Mason J in *Hospital Products* excluded restitutionary relief where ‘the interest of the fiduciary is remote or insubstantial’.⁶¹ In so doing, Mason J⁶² referred to the comments of Judge Learned Hand in *Phelan v Middle States Oil Corporation*⁶³ that ‘the rule does not apply when the putative interest, though in itself strong enough to be an inducement, is too remote, or when, though not too remote, it was too feeble an inducement to be a determining motive ...’⁶⁴ These passages demonstrate an interconnection between the likelihood of the conflict arising and the substantiality or materiality of the interest itself in the determination of whether there is a real sensible possibility of conflict. Ultimately the question is arguably whether there is a real sensible possibility that the

⁵⁸ See *Beach Petroleum NL v Abbott Tout Russell Kennedy* (1999) 48 NSWLR 1, 46 [196], 47 [198], [201]–[202]; *Pilmer* (n 20) 199 [78]; *Transvaal Lands* (n 24) 503; cf *Grand Enterprises* (n 55) 16 [69], 16–18 [72]–[81].

⁵⁹ See *McGellin* (n 50) 304.

⁶⁰ (Supreme Court of New South Wales Equity Division, Brownie J, 27 June 1994) 8.

⁶¹ *Hospital Products* (n 21) 103. Mason J referred to the statement of Upjohn LJ in *Boulting v Association of Cinematograph, Television and Allied Technicians* [1963] 2 QB 606 (CA) 637–8 that the Court would require more than a ‘theoretical or rhetorical’ possibility of conflict. By contrast, in the early case of *Transvaal Lands* (n 24) 503 it was held that the interest could be insubstantial.

⁶² *Hospital Products* (n 21) 104. These comments were also cited with approval by McHugh, Gummow, Hayne and Callinan JJ in *Pilmer* (n 20) 199.

⁶³ 220F(2d) 593, 602 (2nd Cir, 1955).

⁶⁴ See also Owen J in *Bell Group (No 9)* (n 20) 559–60 [4509]–[4512], who suggested that ‘tests for the identification of the “interest” and for the “possibility of a conflict” [could] be applied bearing in mind a similar rationale’.

interest, taking into account the likelihood of it arising and its size, has the capacity to influence the responsible person's focus on acting in good faith in the interests of the entity.

In summary, although 'material' has a different meaning to 'real sensible possibility of', the prohibitions relating to material personal interests and conflicts are very similar. An interest that is not material is unlikely to give rise to a real sensible possibility of conflict and, as outlined above, material personal interests have been equated with conflicts.⁶⁵ One notable difference between the terms is that s 191 (and equivalents in the associations and co-operatives legislation) refer to a director or responsible person *having* a material personal interest whereas breach of the general law conflicts rule arises at an earlier point, viz where a director has a real sensible possibility of a conflict.

It is submitted that the touchstone should be the test adopted by Murray J in *McGellin*, namely something having the capacity to influence the vote of the responsible person. This would mean it would need to be something of substance (ie, material) and also be sufficiently likely to have that capacity (in the sense of a real sensible possibility).⁶⁶

As to whether non-pecuniary or third party conflicts are included within statutory sections, such as s 191 of the *Corporations Act*, which refer to the concept of material personal interest, ASIC RG 76.33 states:

To be personal, an interest need not be pecuniary ... However, it will not be personal if it is an interest of someone else only. For example, where the interest at stake is only that of a beneficiary of a trust of which the director is a trustee: see *Grand Enterprises* at 16. An interest may not be personal if it affects a director as a member of a wide group or class, such as ordinary customers of a bank or shop, in the same manner and to the same degree that it affects the other members of the group or class.

In *Grand Enterprises*⁶⁷ Barker J held that a personal interest would not ordinarily include the situation where a director holds shares on trust for someone else or sits on the board of two companies involved in a transaction without having a major shareholding.⁶⁸ Further factors could, however, cause such interests to be personal interests.⁶⁹ The interests involved in that particular case (a small holding of less than one per cent and shares held through multiple interposed entities which were not controlled by the director) were not personal interests.⁷⁰

The word 'personal' within the term 'material personal interest' indicates that the non-pecuniary or third party interest must affect the responsible person personally in the sense that it affects their ability to make decisions in the best interests of the

⁶⁵ For further detailed analysis of this equation see Langford and Ramsay, 'Conflict of Interest under the General Law' (n 56).

⁶⁶ Langford, *Company Directors' Duties* (n 16) ch 7.

⁶⁷ *Grand Enterprises* (n 55).

⁶⁸ Ibid 16 [69].

⁶⁹ Ibid.

⁷⁰ Ibid 16–18 [72]–[81].

entity. These points support the approach propounded by Murray J, in *McGellin*, that the interest must have the capacity to affect the director's vote. ASIC's comment that an interest 'will not be personal if it is an interest of someone else only' is consistent with these points.

B Directly and Indirectly Interested

An example in this second category of provision is s 208(1) of the *Co-operatives National Law*, which states:

- (1) A director of a co-operative who is or becomes in any way, whether directly or indirectly, interested in a contract or proposed contract with the co-operative must declare the nature and extent of the interest to the board of directors under this section.

It is notable that the statutory duties in the co-operatives legislation refer to being directly or indirectly interested in a contract or proposed contract with the co-operative.⁷¹ Section 31(1) of the *Associations Incorporation Act 2009* (NSW) refers to 'a direct or indirect interest in a matter being considered or about to be considered at a committee meeting'.

As outlined above, there is unfortunately no jurisprudence relating to the sections in the co-operatives and incorporated associations legislation that refer to direct and indirect interests. Guidance must therefore be sourced elsewhere.

The terms 'direct and indirect', in a local government context, were given a narrow interpretation in *Ford v Andrews*.⁷² In that case Gavan Duffy J stated:

A man is directly interested in a contract if he is a party to it, he is indirectly interested if he has the expectation of a benefit dependent on the performance of the contract; but in either case the interest must be in the contract, that is to say, the relation between the interest and the contract must be immediate and not merely connected by a mediate chain of possibilities.

The more recent High Court case of *Re Day (No 2)* establishes that the interest does not have to be legal or equitable or legally enforceable.⁷³

The equivalent section in the *Corporations Act 2001* is s 191, which requires directors to disclose material personal interests. Historically, however, companies legislation imposed a duty on directors who were in any way, whether directly or indirectly, interested in a contract or proposed contract to declare the nature of this interest at a directors' meeting.⁷⁴ For example, s 123(1) of the *Uniform Companies Acts* (1961–62) provided:

⁷¹ See, eg, *Co-operatives National Law* (n 41) s 208(1); *Co-Operatives Act 1997* (Qld) (n 41) s 227(1); *Co-Operatives Act 2009* (WA) (n 41) s 220(1).

⁷² (1916) 21 CLR 317, 335.

⁷³ (2017) 263 CLR 201, 254 [190], 267–8 [253], 269 [258].

⁷⁴ See, eg, *Companies Act 1928* (UK), s 81; *Companies Act 1929* (UK), s 149(1); *Companies Act 1948* (UK), s 199(1); *Companies Act 1938* (Vic), s 149(1)(a)(i); *Uniform Companies Act 1961–1962*, s 123.

Subject to this Section every director of a company who is in any way, whether directly or indirectly, interested in a contract or proposed contract with the company shall as soon as practicable after the relevant facts have come to his knowledge declare the nature of his interest at a meeting of the directors of the company.

Early commentary on s 123 is instructive in that it associates the section with the general law conflicts rule.⁷⁵ For example, Afterman refers to the lack of guidance as to what constitutes a ‘material interest’ and the need for qualification in terms of reasonableness, referring to *Boardman v Phipps*.⁷⁶ This elision of the statutory and general law duties can also be seen in *Castlereagh Motels Ltd v Davies-Roe*,⁷⁷ in which Wallace P (addressing s 123 of the *Uniform Companies Act 1961–1962*) said:

The general intendment of the provisions is to assist in ensuring proper administration of the affairs of the company by preventing a director abusing his knowledge and powers for his own benefit and being put in a position where his duty may conflict with his interests and severe penalties are imposed for breaches of the provisions.⁷⁸

Likewise in *Woolworths v Kelly*,⁷⁹ Samuels JA (in considering s 123) referred to key cases concerning the fiduciary duty (such as *Aberdeen v Blaikie Bros*) and stated that the provision ‘is therefore intended to ensure that directors observe the obligations which their position as fiduciaries demands ...’⁸⁰ In summary, jurisprudence concerning s 123 of the *Uniform Companies Acts* (which, like some legislation in relation to co-operatives and incorporated associations, refers to direct and indirect interests) demonstrates elision of (rather than differentiation between) the statutory and general law duties. Interestingly, s 31(1) of the *Associations Act 2009* (NSW) provides that disclosure need only be made if ‘the interest appears to raise a conflict with the proper performance of the committee member’s duties in relation to the consideration of the matter’.

It is notable that ss 175 and 177 of the *Companies Act 2006* (UK) employ similar terms. Section 175 provides that ‘[a] director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or may possibly conflict, with the interests of the company’. Section 177 provides that directors who are ‘directly or indirectly interested in a proposed transaction or arrangement with the company’ must declare the nature and extent of that interest to the other directors.

It therefore appears that judicial consideration of ss 175 and 177 could inform interpretation of the terms ‘directly or indirectly interested’ in the co-operatives

⁷⁵ See, eg, Roman Tomasic, James Jackson and Robin Woellner, *Corporations Law: Principles, Policy and Process* (Butterworths, 3rd ed, 1996) 347.

⁷⁶ Allen B Afterman, *Company Directors and Controllers: Their Duties to the Company and the Shareholders* (Law Book Company, 1970) 74–5.

⁷⁷ (1966) 67 SR (NSW) 279.

⁷⁸ Ibid 284.

⁷⁹ (1991) 22 NSWLR 189.

⁸⁰ Ibid 211. Mahoney JA also refers to fiduciary principles at 225–31.

legislation (and in s 31(1) of the *Associations Incorporation Act 2009* (NSW)). However, two factors render such jurisprudence less relevant. The first is that there is an exception to both ss 175 and 177 where interests ‘cannot reasonably be regarded as likely to give rise to a conflict of interest’.⁸¹ The second is that s 170(4) of the Act provides that ss 175 and 177 are to be interpreted and applied in the same way as common law rules or equitable principles, and that regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general law duties. In this respect case law prior to the introduction of the *Companies Act* applied a standard of real sensible possibility of conflict.

It is possible that the words ‘directly or indirectly interested’ incorporate interests of third parties more clearly than concepts such as ‘material personal interest’ or conflicts of interest. For example, ss 175 and 177 of the *Companies Act 2006* (UK) have been seen to encompass situations where a director represents a major shareholder in a company whose interests conflict with those of the company⁸² and in some cases where a director’s spouse enters into a transaction with the company.⁸³ In the context of ss 175 and 177 such interests must still amount to a real sensible possibility of conflict. This constraint does not apply to the sections in the co-operatives legislation. However, drawing upon the way in which s 123 of the *Uniform Companies Acts* has been equated with the general law standard, it is possible that this may also be the case as concerns the co-operatives provisions.

As with the provisions relating to material personal interests, the provisions concerning direct and indirect interests refer to the responsible person having such an interest — these provisions therefore arise at a slightly later point than the general law conflicts rule.

C Holding an Office or Having an Interest in Property whereby Directly or Indirectly Duties or Interests might be Created that could Conflict with the Directors’ Duties or Interests

The third category, found in s 208(5) of the *Co-operatives National Law*, refers to directors holding an office or having an interest in property whereby, whether directly or indirectly, duties or interests might be created that could conflict with the directors’ duties or interests as director.⁸⁴

The references to ‘duties or interests that might be created, that could conflict with the directors’ duties or interests as a director’ incorporates the case law and analysis

⁸¹ See ss 175(3) and 177(6)(a).

⁸² See *Companies Act 2006: GC 100 Guidance on Directors’ Conflicts of Interest* (2008) [1.2].

⁸³ Explanatory Notes, *Companies Act 2006* (UK) [83].

⁸⁴ See *Co-operatives National Law* (n 41) s 208(5); *Co-operatives Act 1997* (Qld) (n 41) s 227(5); *Co-operatives Act 2009* (WA) (n 41) s 220(5). Section 208(5) of the *Co-operatives National Law* states: ‘A director of a co-operative who holds an office or has an interest in property whereby, whether directly or indirectly, duties or interests might be created that could conflict with the directors’ duties or interests as director must, under subsection (6), declare at a meeting of the board of directors the fact and the nature, character and extent of the conflict.’

in Section III above relating to the general law duty to avoid conflicts. The section is broad because it also includes the words ‘directly or indirectly’. It also includes potential conflicts by reason of the word ‘might’. On the other hand, it is limited to conflicts created by virtue of holding an office or holding an interest in property. Directors of co-operatives are, however, also subject to duties in category 2 (analysed in Section IVB above).

D Direct or Indirect Pecuniary Interest in a Contract or Proposed Contract with the Association

The Northern Territory and South Australian incorporated associations legislation employs the terms ‘direct or indirect pecuniary interest’ (in a contract or proposed contract) with the association.⁸⁵ For example, s 31(1) of the *Associations Act 2003* (NT) provides:

A member of the committee of an incorporated association who has a direct or indirect pecuniary interest in a contract, or proposed contract, with the association:

- (a) must, as soon as the member becomes aware of the interest disclose the nature and extent of the interest to the committee; and
- (b) must disclose the nature and extent of the interest at the next annual general meeting of the association required to be held by the association.

This excerpt also highlights the fact that some sections require disclosure to members as well as to other responsible persons.

This is arguably the narrowest of the statutory sections, given that interests are limited to pecuniary interests, and that such interests must be ‘in a contract or proposed contract with the association’. Nevertheless there is no threshold of materiality and the interests can be indirect. Members of management committees of such associations should, however, also be aware of their obligations at general law and under ACNC Governance Standard 5.

The High Court considered the phrase ‘direct or indirect pecuniary interest’ in s 44(v) of the Commonwealth Constitution in *Re Day (No 2)*.⁸⁶ In terms of the word ‘interest’, Nettle and Gordon JJ held that the interest does not have to be legal or equitable or legally enforceable⁸⁷ but that it must be in existence at the critical time and not merely a possibility of acquiring an interest.⁸⁸ The key point is whether the

⁸⁵ See *Associations Act 2003* (NT) (n 41) s 31(1); *Associations Incorporation Act 1985* (SA) (n 41) s 31(1).

⁸⁶ *Re Day (No 2)* (n 73).

⁸⁷ Ibid 267–8 [253], 269 [258]. Keane J, at 254 [190], also held that it does not have to be a legally enforceable agreement or entitlement to money.

⁸⁸ Ibid 268 [254].

‘interest in the agreement *could* conceivably influence the person’.⁸⁹ Kiefel CJ, Bell and Edelman JJ found that s 44(v) looks to the practical effect of an agreement on a person’s pecuniary interests and the possibility of a conflict of duty and interest.⁹⁰ Gageler J saw the notion of an indirect interest in a contract as being an expectation of a benefit dependent on performance of the contract.⁹¹

In terms of pecuniary interests, Gageler J stated that ‘pecuniary means that the interest must be, or be capable of sounding in, money or money’s worth. And it must obviously be more than trivial’.⁹² Nettle and Gordon JJ equated the term pecuniary with ‘not insubstantial financial gain or loss’, also noting that ‘pecuniary interest’ means ‘interest sounding in money or money’s worth’.⁹³ Further, their Honours stated that:

A ‘financial gain or loss’ is not to be equated with the receipt of money. It is sufficient if the person’s ‘pockets ... might be affected’ ... [I]t is sufficient if the interest affects what the person has to pay out, or if it affects the financial reward that the person is likely to receive, whether in the form of money, other consideration, or relief from making a financial outlay. Nor is there any requirement that the interest be legal or equitable or legally enforceable.⁹⁴

The key point, in their view, seemed to be whether ‘through the possibility of a not insubstantial financial gain or loss ... that person could conceivably be influenced in the exercise of their functions, powers and privileges, or in the performance of their duties’.⁹⁵ This is similar to the approach taken by Murray J in *McGellin* in relation to material personal interests, although such interests are not limited to pecuniary interests.

E Comparison with General Law Standard

The statutory proscriptions relating to conflicts are all encompassed within the general law concept of real sensible possibility of conflict. Indeed, there has been elision of the statutory and general law concepts. The general law concept is wider than sections relating to material personal interests and direct and indirect interests because such sections refer to the responsible person actually having the relevant interest, whereas a real sensible possibility of conflict can arise at an earlier point. Sections in the co-operatives legislation relating to duties and interests that might be created, and that could create conflict, are for that reason potentially broader than the concept of material personal interest, although there must be a nexus with the director’s office or

⁸⁹ Ibid 269 [258], 270 [264]. At 268 [255], referring to the words of Gavan Duffy J in *Ford v Andrews* (n 72) 355, their Honours asked whether the relation between the pecuniary interest (direct or indirect) and the agreement is immediate or merely connected by a chain of possibilities.

⁹⁰ *Re Day (No 2)* (n 73) 222 [54].

⁹¹ Ibid 236 [109], also referring to Gavan Duffy J in *Ford v Andrews* (n 72).

⁹² *Re Day (No 2)* (n 73) 236 [111].

⁹³ Ibid 267 [252].

⁹⁴ Ibid 267–8 [253] (citations omitted).

⁹⁵ Ibid 267 [252].

an interest in property. Sections relating to direct and indirect pecuniary interests are narrower than, but encompassed within, the general law concept.

V ACNC GOVERNANCE STANDARD 5

ACNC Governance Standard 5 sets out governance obligations of responsible persons. However, the ACNC has limited direct power in relation to responsible persons for constitutional reasons⁹⁶ and Governance Standard 5 requires charities to take reasonable steps to ensure that their responsible persons comply with certain obligations.⁹⁷

Governance Standard 5, contained in reg 45.25(2), provides:

A registered entity must take reasonable steps to ensure that its responsible entities are subject to, and comply with, the following duties:

- (a) to exercise the responsible entity's powers and discharge the responsible entity's duties with the degree of care and diligence that a reasonable individual would exercise if they were a responsible entity of the registered entity;
- (b) to act in good faith in the registered entity's best interests, and to further the purposes of the registered entity;
- (c) not to misuse the responsible entity's position;
- (d) not to misuse information obtained in the performance of the responsible entity's duties as a responsible entity of the registered entity;
- (e) to disclose perceived or actual material conflicts of interest of the responsible entity;
- (f) to ensure that the registered entity's financial affairs are managed in a responsible manner;
- (g) not to allow the registered entity to operate while insolvent.⁹⁸

Paragraphs (f) and (g) are arguably subsets of the duty in paragraph (a).

The focus of this article is on paragraph (e), which indirectly requires responsible persons to disclose perceived or actual material conflicts of interest. A note to Governance Standard 5 specifies that related party transactions constitute a perceived or actual material conflict. In terms of defences, Protections 1 and 4 of Governance Standard 5 apply in relation to paragraph (e). Protection 1 relates to reliance on information provided by employees, professional advisers and other responsible persons. Protection 4 relates to absence (for example, due to illness).

If a responsible person has an actual or perceived material conflict of interest, they must disclose that conflict.⁹⁹ Regulation 45.25(3) sets out to whom disclosure should

⁹⁶ See Ramsay and Webster (n 8); Nicholas Aroney and Matthew Turnour, 'Charities and the New Constitutional Law Frontier' (2017) 41(2) *Melbourne University Law Review* 446.

⁹⁷ Reasonable steps could include having the duties set out in a contract of employment or letter of appointment, as part of a board charter, a code of conduct based on the duties, or specifying the duties of the responsible entities in the registered entity's governing rules (although there is no prescribed or mandatory form): see Explanatory Statement, *Australian Charities and Not-for-profits Commission Amendment Regulation 2013 (No 1)* (Cth) 11–12.

⁹⁸ Section 205-30 of the *Australian Charities and Not-for-Profits Commission Act 2012* (n 2) defines responsible entities to include directors, trustees and other persons involved in a charity's governing body.

be made. It is then up to the body to whom disclosure is made to determine how the conflict should be managed. Depending on the nature and extent of the conflict, this may mean that the responsible person is able to be present, participate in the relevant decision and vote on the matter, or that the responsible person must abstain from participation and/or being present and/or voting.¹⁰⁰ Conflicts need to be recorded, ideally in a register of interests.¹⁰¹ Those to whom disclosure is made, and who make the decision as to how the conflict is managed, should remember their own duty (imposed at general law, under statute and under paragraph (b) of Governance Standard 5) to act in good faith in the interests of the entity. Responsible persons should also be very wary of conflicts of interest that constitute misuse of position or misuse of information. Such misuse is proscribed by paragraphs (c) and (d) of Governance Standard 5, and may result in breach of statutory duties or the fiduciary duty to avoid profits from position.

One criticism of Governance Standard 5 is that the requirement to disclose actual or perceived material conflicts is inadequate in that the requirement should be to manage the conflict. This was raised in some submissions to the ACNC Review.¹⁰²

The ACNC provides guidance on conflicts in a guide entitled *Managing Conflicts of Interest: A Guide for Charity Board Members*.¹⁰³ It expresses the following rationale:

It can be difficult to make a decision in the best interest of your charity if that decision conflicts with your personal interests or those of your friends, family or other organisations you are involved with. A failure to manage any conflicts of interest can easily result in a breach of this duty.¹⁰⁴

⁹⁹ It is notable that, although disclosure and consent are universally adopted as a means of managing conflicts, the efficacy of disclosure has recently been questioned: see, eg, Australian Securities and Investments Commission and the Dutch Authority for the Financial Markets, *Disclosure: Why It Shouldn't be the Default* (REP 632, October 2019).

¹⁰⁰ See Australian Charities and Not-for-profits Commission, *Managing Conflicts of Interest: A Guide for Charity Board Members* (2015) ('ACNC Conflicts Guidance Note') 15-17.

¹⁰¹ Ibid.

¹⁰² See, eg, Australian Charities and Not-for-profits Commission, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (undated); Beyond PMSA, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (28 February 2018); Illawarra Legal Centre, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (February 2018); Queensland Law Society, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (28 February 2018).

¹⁰³ See ACNC Conflicts Guidance Note (n 100).

¹⁰⁴ The ACNC Conflicts Guidance Note states that: 'The problem of conflicts of interest is that your duty to act in the best interest of the charity may be undermined by another interest you have, making it difficult to know if you are meeting your duties ... These conflicts can sometimes cause problems because they present a risk that you will make a decision based on, or affected by, these external influences, rather than in the best interests of the charity': ibid 3; see also at 5.

This highlights the relevance of the duty to act in good faith in the interests of the entity.¹⁰⁵ A further rationale is protecting the charity's reputation. The ACNC Conflicts Guidance Note states:

Failing to manage conflicts of interest can damage the reputation of your charity. They can cause others (such as funders, donors, volunteers, members and beneficiaries) to question whether decisions made by the board have been made in the best interests of your charity or whether the board members have the necessary expertise for their role.¹⁰⁶

...

Your charity's reputation is one of its most valuable assets. Many charities rely on their good reputation to attract donations, funding and clients. As a board member, you have a responsibility to ensure that your charity's reputation is not compromised by poorly-managed conflicts of interest.¹⁰⁷

Other rationales stated in the guide are accountability and transparency and board dynamics.¹⁰⁸

A Perceived or Actual Material Conflicts of Interest

Regulation 45.45(2)(e) uses the words 'perceived or actual material conflicts of interest'. A key question that arises is what these words mean.

The ACNC Conflicts Guidance Note is instructive. It outlines three types of conflict, namely actual, potential and perceived conflicts. It then provides explanations and examples. The Guidance Note refers to *actual* conflicts as 'real' conflicts and states: 'You are being influenced by a conflicting interest'. The example given is where a charity is considering whether to give a grant to a kindergarten that a responsible person's child attends and the responsible person cannot make the decision impartially. The Guidance Note states in relation to *potential* conflict: 'You could be influenced by a conflicting interest.' The following example is given: 'You've taken up employment with another charity and you may, at some point, apply for a grant as an employee of one charity and a board member of another.' A *perceived* conflict is where a responsible person 'could appear to be influenced by a conflicting interest'. The following example is given: '[Y]ou are reviewing quotes for a service and one of the potential providers is the employer of your sibling. While you believe that you can make an impartial decision in the best interests of the charity, it could be perceived as being made in your own interest'.

The following points can be noted. First, the ACNC Conflicts Guidance Note includes the concept of potential conflict, which is not included in the wording of Governance Standard 5. This raises an issue as to whether potential conflicts can also be described as actual or perceived conflicts. It also raises the issue of the difference between the concepts of actual, potential and perceived conflicts.

¹⁰⁵ For discussion see Section III above.

¹⁰⁶ See *ACNC Conflicts Guidance Note* (n 100) 5.

¹⁰⁷ See *ibid.*

¹⁰⁸ *Ibid* 5-6.

Second, the Guidance Note refers to making decisions impartially. This raises issues of whether concepts of bias are being imported into the Standard and the difference between conflicts and bias. This issue is critically analysed in Section VA1(f) below.

Third, the ACNC Guidance Note gives examples of conflicts that involve non-pecuniary and third party interests. This raises the issue of the extent to which the duty to avoid conflicts encompasses non-pecuniary and third party interests, as discussed in Section III above. This is contested at general law. Fourth, the Guidance Note clearly includes conflicting duties. These points are now critically examined, followed by critical evaluation of whether the term ‘perceived conflict’ should be removed from Governance Standard 5.

1 *Meanings*

The ACNC Conflicts Guidance Note defines a conflict of interest as follows:

A conflict of interest occurs when your personal interests conflict with your responsibility to act in the best interests of your charity. The term ‘personal interests’ does not need to be your own interest, but may also arise from the interests of your family friends, or other organisations you are involved with. It also includes a conflict between your duty to the charity and another duty that you have (for example, to another charity).¹⁰⁹

This is helpful given that, as pointed out by Smith, case law does not define the term.¹¹⁰

The Guidance Note also poses the following question:

Would a reasonable person (properly informed about the nature of your personal interests) believe that you might be influenced by your personal interests when making decisions on behalf of the charity?¹¹¹

This touchstone test is significant because it resembles the test employed in relation to the fiduciary duty to avoid conflicts, namely real sensible possibility of conflict. As extracted in Section III above, in *Boardman v Phipps*¹¹² Lord Upjohn stated that this ‘means that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict’.¹¹³

(a) *Actual Conflicts*

The concept of ‘actual conflict’ is used by the ACNC Conflicts Guidance Note to describe a ‘real’ conflict that is influencing a responsible person in their decision-making. This could also be referred to as an ‘active’ conflict, in that the interest is having an active influence on the responsible person in the exercise of their

¹⁰⁹ Ibid 3.

¹¹⁰ See Section III above.

¹¹¹ See *ACNC Conflicts Guidance Note* (n 100) 3.

¹¹² *Boardman v Phipps* (n 18).

¹¹³ Ibid 124.

discretion. This differs from the meaning of the term ‘actual conflict’ in equitable jurisprudence — in *Bristol and West Building Society v Mothew* Millett LJ used the term ‘actual conflict’ to describe a situation where a fiduciary cannot fulfill their duties to one principal without breaching their duties to another.¹¹⁴ The concept of actual conflict employed by the ACNC does not require as acute a conflict as does the concept of actual conflict propounded by Millett LJ.

It was shown that statutory sections relating to material personal interests refer to the responsible person *having* a material personal interest. This can be equated with the concept of actual conflict, in the sense that an actual conflict is one that is impacting on the responsible person (rather than one that might arise in the future).

(b) *Potential Conflicts*

There are several ways in which the term ‘potential conflict’ could be interpreted. In contrast to the concepts of actual conflict and perceived conflict, the concept of ‘potential conflict’ appears to be forward-looking in the sense of whether, looking forward, conditions are in play that could lead to a conflict in future. As extracted above, the ACNC Conflicts Guidance Note sees a potential conflict as one that could influence a responsible person in the future. There is therefore a time element in that a perceived conflict can be present and past but a potential conflict looks to the future.

A different meaning is adopted by Davis and the Parker Commission. Davis states:

A conflict of interest is potential if and only if P has a conflict of interest with respect to a certain judgment but is not yet in a situation in which he must make that judgment. Potential conflicts of interest, like time bombs, may or may not go off. A conflict of interest is actual if and only if P has a conflict of interest with respect to a certain judgment.¹¹⁵

The Parker Commission states:

Potential conflict is the situation that arises between the moment the public office holder realizes that he or she has a private economic interest in some matter at hand and the moment the public office holder exercises a public duty or responsibility and places himself or herself in a position of real conflict of interest.¹¹⁶

The term ‘potential conflict’ is arguably encompassed by the general law concept of real sensible possibility of conflict, given that the general law concept is forward-looking in the sense of ‘real sensible possibility of conflict’. The general law concept also encompasses the meanings of potential conflict specified by Davis and the Parker Commission. The concept of potential conflict has been used in relation to the UK

¹¹⁴ *Mothew* (n 38) 19.

¹¹⁵ See Michael Davis, ‘Conflict of Interest’ in Ruth Chadwick (ed), *Encyclopedia of Applied Ethics* (Elsevier, 2nd ed, 2012) 575, cited in Smith (n 40).

¹¹⁶ See *Commission of Inquiry into the Facts of Allegations of Conflicts of Interest Concerning the Honourable Sinclair M Stevens* (1987) 18, cited in Smith (n 40).

statutory section relating to direct and indirect interests¹¹⁷ and these are terms used in the statutory provisions in the co-operatives legislation.

Whether the concept of a potential conflict is encompassed within the terms ‘actual and perceived conflicts’ — which are the words used in Governance Standard 5 — is another question. Arguably a potential conflict falls within the ambit of the concept of real sensible possibility of conflict but does not necessarily fit within the concepts of actual or perceived conflicts. This means that, even if potential conflicts (referred to in the ACNC Conflicts Guidance Note) are not actual or perceived conflicts (for the purposes of Governance Standard 5), they are part of the general law duty. The term ‘potential conflict’ is, however, arguably wider than statutory prohibitions on material personal interests, given that these prohibitions relate to *having* a material personal interest.

(c) *Perceived Conflicts*

The Oxford English dictionary defines the word ‘perceived’ as: ‘To apprehend with the mind; to become aware or conscious of; to realize; to discern, observe’, and ‘[g]rasped with the mind or the senses, understood; apprehended; observed’, and also ‘interpreted or viewed in a particular way, supposed’.

The ACNC Conflicts Guidance Note elaborates further on the concept of perceived conflict, stating:

While some concepts may be obvious, there are others that might only have the potential to influence you, or others may perceive to influence you, even if they don’t. Perception is just as important as your intention because it affects your reputation and that of the charity.

As mentioned, it also states under the heading of ‘perceived’:

You could appear to be influenced by a conflicting interest ...For example - you are reviewing quotes for a service and one of the potential providers is the employer of your sibling. While you believe you can make an impartial decision in the best interests of the charity, it could be perceived as being made in your own interest).

In this respect, a 2011 Treasury Consultation Paper stated:

[A] responsible individual should seek to avoid conflicts of interest wherever possible. Full and prior disclosure of any conflict, or potential conflict, or the appearance of potential conflict, must be made to the decision-making body.¹¹⁸

It is clear that ‘perception’ is about how something appears regardless of whether there is actually a conflict. This reflects the fact that one of the rationales of the

¹¹⁷ See *Davies v Lynch-Smith* [2018] EWHC 2336 (Ch) [72]; *Cullen Investments Ltd v Brown* [2017] EWHC 1586 (Ch) [244].

¹¹⁸ See Australian Government, The Treasury, *Review of Not-for-Profit Governance Arrangements* (Consultation Paper, December 2011) [126].

proscription on conflicts in Governance Standard 5 is protection of the charity's reputation.

A key issue that arises in relation to the concept of perceived conflict is by whom the conflict is perceived. The word 'perceived' appears to import a subjective test. In this respect the perceptions of a number of stakeholders may be relevant.¹¹⁹

By contrast, the general law standard of real sensible possibility of conflict is objective. However, it appears that an objective standard is intended. The Explanatory Statement to the ACNC Amendment Regulation 2013 (No 1) says:

Registered entities need to ensure that their responsible entities disclose material conflicts of interest even if the conflict is only perceived. When considering what is a perceived material conflict of interest, it is based on an objective standard and a responsible entity must consider what a reasonable person or court would consider to be a perceived material conflict of interest.¹²⁰

A question arises as to the difference between the concept of perceived conflict and that of real sensible possibility of conflict (which is the standard adopted at general law). In this respect the ACNC Conflicts Guidance Note includes the following 'Quick Tip':¹²¹

Quick tip — the impartial observer test: 1. You are a member of a charity's board. 2. You have some personal interests. 3. Would an impartial observer think that you are likely to, or may be likely to, be improperly affected by these personal interests? If you answer yes to the final question, then it is likely that you have a conflict of interest.¹²²

If this is the sense in which the term perceived conflict is intended, then there is no material difference between perceived conflict and real sensible possibility of conflict, because an objective test is used to determine perception of a conflict. However, this is not obvious from the wording of Governance Standard 5.

A search of case law demonstrates that the term 'perceived conflict' is used in settings where the appearance of independence and impartiality are important. These settings include insolvency law (as concerns the appointment, resignation and

¹¹⁹ The Explanatory Statement to the ACNC Amendment Regulation 2013 (No 1) refers to a number of stakeholders in stating: 'Registered entities have a general responsibility to their donors, beneficiaries, volunteers and members (where applicable) as per their NFP character and the public at large, in part because they are in receipt of tax concessions or public funds': Explanatory Statement, *Amendment Regulation 2013 (No 1)* (n 99).

¹²⁰ The ACNC has noted that it will 'interpret the duties in line with existing interpretations': Australian Charities and Not-for-profit Commission, *ACNC Governance Standards Guidance* (August 2013) 18.

¹²¹ See ACNC *Conflicts Guidance Note* (n 100) 14.

¹²² See also Australian Charities and Not-for-profit Commission, *Governance for Good: The ACNC's Guide for Charity Board Members* (Version 3, May 2018) 15. Robinson notes that the 'reasonable apprehension of bias rule' is also concerned with what a reasonable observer might perceive: see Mark A Robinson, *Judicial Review: The Laws of Australia* (Thomson Reuters, 2014) 429 [2.5.870].

removal of liquidators, voluntary administrators, and receivers and managers),¹²³ local government and administrative law,¹²⁴ solicitors' duties,¹²⁵ and employment law.¹²⁶ The term is also used in university policies on conflicts of interest.¹²⁷

Another context in which the term 'perceived' is used is cases in which directors disclosed that they had a conflict and stepped aside but courts nevertheless found that directors could not avoid breach of duty by asserting a perceived conflict.¹²⁸ A common factor in these cases is that the courts held that disclosure of the perceived conflict was insufficient to absolve directors of breach of duty — positive action was required of them in the form of extended disclosure (for example, of the risks inherent in the transaction) and also potentially action to prevent the transaction from proceeding.

It is unclear exactly why the term 'perceived conflict' was included in Governance Standard 5 given that, as shown in Sections III and IV above, this term is not used in equivalent general law or statutory formulations of the conflicts rules. There was also opposition to inclusion of the term 'perceived conflicts', both at the time that the Governance Standard was drafted and during the five year review process. For example, Moores Legal argued that the term 'perceived material personal interest' was 'subjective and likely to be problematic in practice', going beyond existing requirements, and therefore 'introduc[ing] a new duty that is not contained in the

¹²³ See, eg, *Advance Housing Pty Ltd (in liq) v Newcastle Classic Developments Pty Ltd* (1994) 14 ACSR 230; *Australian Securities and Investments Commission v Letten* [2010] FCA 140; *Australian Securities and Investments Commission v Dunner* (2013) 303 ALR 98; *Australian Securities and Investments Commission v Franklin* [2014] FCA 68; *Hughes v Westgem Investments Pty Ltd (recs and mgrs apptd) (No 3)* [2012] WASC 360; *Walley; re Poles & Underground Pty Ltd (admin apptd)* [2017] FCA 486. See also *Ziziphus Pty Ltd v Pluton Resources Ltd (recs and mgrs apptd) (in liq)* [2017] WASCA 193, [83].

¹²⁴ See, eg, *Dunbar v City of Stirling* (2006) 47 SR (WA) 50; *Port Hedland Regional Aboriginal Corp v Ngarda-Ngarli-Yarndu Regional Council* [2002] FCA 1415; *Isbester v Knox City Council* (2015) 255 CLR 135; *Kirby v Dental Council of New South Wales* [2018] NSWSC 1869; *De Luca v Simpson* (2012) 193 LGERA 1.

¹²⁵ See *Trad v Harbour Radio Pty Ltd* [2017] NSWCA 60; *QGC Pty Ltd v Bygrave* (2010) 186 FCR 376.

¹²⁶ See *Johnson v Greyhound Racing Control Board* (1993) 51 IR 37; *Nolan v Executive Director, Land Management Policy, Department of Environment and Primary Industries* [2015] VSCA 301.

¹²⁷ See, eg, 'Conflicts of Interest', *University of Southern Queensland* (2018) <<https://www.usq.edu.au/hr/empcond/conflicts>>, which states: 'It is important to understand that the mere perception that a conflict of interest has occurred could undermine the University's integrity.' See also United Nations Ethics Office, '2019 Leadership Dialogue — Conflicts of Interest: Why Do they Matter?' (Presentation, 2019) available at <<https://www.un.org/en/ethics/ethics-training/leadership-dialogue.shtml>>.

¹²⁸ See, eg, *Permanent Building Society (in liq) v Wheeler* (1994) 11 WAR 187, 241. See also *Fitzsimmons v The Queen* (1997) 23 ACSR 355, 358; *Groeneveld Australia Pty Ltd v Wouter Noltén (No 3)* (2010) 80 ACSR 562, 576 [58]; *Duncan v Independent Commission Against Corruption* [2016] NSWCA 143, [435], [625].

Corporations Act, with therefore no body of common law to provide guidance regarding its practical meaning'.¹²⁹

A review of key consultation documents leading to the establishment of the ACNC and the framing of the Governance Standards shows the following.

First, a key aim was to ensure accountability to a wide range of stakeholders. Thus, the 2011 Treasury Consultation Paper stated that:

The object of governance rules is to ensure compliance, transparency and accountability of NFP entities to their volunteers, donors, beneficiaries, the public at large, and members (where applicable). Further, the rules should create a framework to protect the entity and its mission or purpose from mismanagement, and ensure that the entity is focused on its mission, and not the goals or interests of others.¹³⁰

There was also recognition of the public support received by not-for-profits:

Improvements in disclosure generally result in improvements in transparency, which in itself safeguard against mismanagement. Given that NFPs are in receipt of public support, there is placed upon them high community expectations, thereby making transparency and accountability very important. In addition, NFPs rely heavily on their reputation in the community, and a lack of transparency may lead to a loss of donations and lower levels of volunteering.¹³¹

These considerations support a higher standard being imposed on responsible entities.

On the other hand, the documents also state that the duties in Governance Standard 5 were intended to 'be substantially the same as the duties of directors under the *Corporations Act*'.¹³² For example, the Explanatory Statement to the ACNC Amendment Regulation 2013 (No 1) states that the duties in Governance Standard 5

have been derived from the common law and the *Corporations Act* and they have well established meanings. Consequently, it is intended that the meaning of these duties be interpreted with reference to the existing common law and relevant legislation.¹³³

This is obviously not the case in relation to the term 'perceived conflict' given that the equivalent duty in s 191 of the *Corporations Act* (critically analysed in Section IVA above) requires directors who have a material personal interest in a matter that relates to the affairs of the company to give the other directors notice of the interest (subject to exceptions).

¹²⁹ Moores Legal, *Submission to the Treasury: Australian Charities and Not-for-profits Governance Standards – Draft* (15 February 2013) 5; see also PilchConnect, *Submission to the Treasury: Australian Charities and Not-for-profits Governance Standards* (15 February 2013) 15; Australian Institute of Company Directors, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (28 February 2018).

¹³⁰ Treasury, *Review of Not-for-Profit Governance Arrangements* (n 118) [32].

¹³¹ Ibid [106].

¹³² See Australian Government, The Treasury, *Governance Standards for the Not-for-Profit Sector* (Consultation Paper, December 2012) 22.

¹³³ Explanatory Statement, *Amendment Regulation 2013 (No 1)* (n 97) 11.

There is therefore no clear explanation for inclusion of the term ‘perceived conflict’. The following considerations can be speculated. The first is the fact that the ACNC legislation and regulations were drafted to be accessible to the sector, and therefore in plain English. A principles-based drafting approach was adopted in framing the Governance Standards. The second is that high standards were expected due to the view that charity stewardship called for a fiduciary duty towards assets dedicated to public benefit — these standards can be undermined by perceived as well as actual conflicts. In this respect the first object of the ACNC Act concerns public trust and confidence and the aim of Governance Standard 1 is to give the public confidence that charities are acting to further their purposes.¹³⁴ The third is that, as mentioned above, the term ‘perceived conflict’ is intended to protect the charity’s reputation, as compared to the general law conflicts rule which protects the decision-maker’s focus on the interests of the entity.

(d) *Non-Pecuniary and Third Party Interests*

The ACNC Conflicts Guidance Note is very clear that non-pecuniary and third party interests are included within the ambit of the conflicts that need to be disclosed. The Guidance Note divides conflicts into direct financial interests, indirect financial interests and non-financial or personal conflicts.¹³⁵ The ACNC Guidance Note provides the following description of an indirect financial interest: ‘Your family or close friend, or another organization in which you are involved, may stand to benefit financially as a result of a decision made by your board.’¹³⁶

In explaining non-financial or personal conflicts, the ACNC Conflicts Guidance Note states:

Not all conflicts of interest are about money. In some cases, your personal or religious opinions, values or beliefs may be in conflict with a proposed action or decision of your board. In some situations, the conflict may arise simply because you want to do a favour for a friend. Alternately, a proposed decision of your board may result in your family or friends receiving a non-financial benefit they would otherwise not be entitled to receive.¹³⁷

The inclusion of non-pecuniary and third party interests is consistent with the Treasury consultation documents, which mention the ‘interests of responsible individuals and those associated individuals and entities (eg, their wife or a commercial entity)’.¹³⁸ The inclusion of non-pecuniary and third party interests is arguably warranted given that such interests can affect a responsible person’s focus on the interests and purposes of the charitable entity, and impact on its reputation.

¹³⁴ See *Australian Charities and Not-for-profits Commission Act 2012* (n 2) pt 1-2, div 15-5; *Australian Charities and Not-for-Profits Commission Regulation 2013* (n 6) s 45-5.

¹³⁵ See *ACNC Conflicts Guidance Note* (n 100) 12–13.

¹³⁶ Ibid.

¹³⁷ See *ibid* 13.

¹³⁸ See *ibid*.

There is, however, a need for a ‘de minimis’ limit.¹³⁹ In the context of paragraph (e) of Governance Standard 5 this limit is achieved by the word ‘material’.¹⁴⁰ The next section of this article probes the meaning of that term.

The pragmatic inclusion of non-pecuniary and third party conflicts in the ACNC Guidance Note can be contrasted with the position at general law and under statute, given that the extent to which the general law and statutory duties concerning conflicts encompass such conflicts and interests is less clear.

(e) *Material*

A question arises as to the meaning of the term ‘material’ and what limitation that term brings in terms of the extent of the conflicts that need to be declared under Governance Standard 5. As outlined in Section IVA above, in the company law context, the term ‘material’ has been equated with something having the capacity to influence the vote of a director on the decision in question — as something of ‘some real substance’.¹⁴¹ This test was also referred to in the 2011 Treasury Consultation Paper.¹⁴²

It is, however, noteworthy that, in comparison with many statutory provisions that require disclosure in relation to matters relating to the affairs of the entity or to a decision, there is no such qualification in paragraph (e) of Governance Standard 5. The proscription in paragraph (e) is therefore broader in this respect.

(f) *Bias*

The references to impartiality in the ACNC Conflicts Guidance Note raise an issue of whether public law concepts of bias are being imported into the regulation of conflicts. The clear inclusion of non-pecuniary and third party interests is further evidence that this might be the case. This, in turn, raises the issue of the overlap between proscriptions on conflicts and bias.¹⁴³ It should be noted that, given that the Governance Standard has a legislative basis, there is no inherent problem in importing concepts more closely associated with bias (if that is the case).

¹³⁹ Smith (n 40) suggests that the test could be whether a reasonable and informed observer would have a concern.

¹⁴⁰ Conaglen writes that the need for a real sensible possibility of conflict has been said, potentially, to justify a de minimus exception where the interest is very small (citing *Fenwick v Naera* [2015] NZSC 68, [58], [158] and *Collinge v Kyd* [2005] 1 NZLR 847, [59]), but also notes that a small interest has been held to be sufficient in other cases (citing *Transvaal Lands* (n 24) 503): see Matthew Conaglen, ‘Fiduciaries’ in John McGhee (ed), *Snell’s Equity* (Sweet & Maxwell, 33rd ed, 2015; 2019 supp) [7-018].

¹⁴¹ *McGellin* (n 50) 304; ASIC RG 76.33 (n 55).

¹⁴² Treasury, *Review of Not-for-Profit Governance Arrangements* (n 118) [121.2].

¹⁴³ For discussion see Smith (n 40); Matthew Conaglen, ‘Public-Private Intersection: Comparing Fiduciary Conflict Doctrine and Bias’ [2008] *Public Law* 58.

The public law concept of bias assesses whether there is any reason to think that the decision-maker might not be impartial or independent.¹⁴⁴ It includes pecuniary interests, political interests, prejudices and many types of normal business relationships.¹⁴⁵ As explained by Conaglen:

Furthermore even where the decision-maker does not have an interest in the outcome of the proceedings, bias law still intervenes if there is an appearance of bias: The question is whether the fair-minded and informed observer, having considered the facts, would conclude that there was a real possibility that the tribunal was biased.¹⁴⁶

The fact that the term ‘perceived conflict’ has connections with bias law resonates with the fact that a tenet of bias law is that ‘justice must be seen to be done’.¹⁴⁷

(g) *Conflicting Duties*

The ACNC Guidance Note is explicit that conflicting duties are encompassed within paragraph (e). This is entirely appropriate. Conflicting duties are a core part of the general law duty to avoid conflicts, as outlined in Section III above.

As outlined above, the inclusion of conflicting duties within the term ‘material personal interest’ in s 191 of the *Corporations Act 2001* has been subject to doubt (due to the word ‘personal’) but research demonstrates that the better view is that conflicting duties are indeed covered.¹⁴⁸ In addition, Governance Standard 5 does not use the word ‘personal’; rather it is phrased in terms of ‘perceived or actual material conflicts’.

(h) *Comparison with Other Concepts*

The concept of actual material conflict falls within the general law concept of real sensible possibility of conflict. Although it has been noted that the terms ‘material’ and ‘real sensible possibility of’ perform different functions, they are often equated with each other. An actual conflict also falls within statutory sections that employ the term ‘material personal interest’, but these sections may incorporate a nexus with the entity (such as decisions at meetings) and may be subject to exceptions. An actual material conflict is also likely to be encompassed within statutory sections relating to

¹⁴⁴ See *Ebner v Official Trustee in Bankruptcy* (2000) 205 CLR 337, 343 [2]; *R v Bow Street Metropolitan Stipendiary Magistrate; ex parte Pinochet Ugarte (No 2)* [2000] 1 AC 119, 133 (Lord Browne-Wilkinson); Conaglen, ‘Public-Private Intersection’ (n 143).

¹⁴⁵ *Ebner* (n 144) 348–9 [24]; Judith Bannister, Gabrielle Appleby and Anna Olijnk, *Government Accountability: Australian Administrative Law* (Cambridge University Press, 2015) 503–4; Lord Woolf et al, *De Smith’s Judicial Review* (Sweet & Maxwell, 8th ed, 2018) [10-045]–[10-058].

¹⁴⁶ Conaglen, ‘Public-Private Intersection’ (n 143).

¹⁴⁷ Robinson (n 122) 432, refers to ‘the fundamental principle that justice must both be done, and be seen to be done’ (referring to *Johnson v Johnson* (2000) 201 CLR 488, 492–3 [12] (Gleeson CJ, Gaudron, McHugh, Gummow and Hayne JJ); *Ebner* (n 144) 344–5 [6] (Gleeson CJ, McHugh, Gummow and Hayne JJ).

¹⁴⁸ See Section IVA above.

direct and indirect interests but extends further than the term ‘direct and indirect pecuniary interests’.

A potential material conflict can be, and has been, equated with real sensible possibility of conflict. This concept, however, goes beyond sections that refer to material personal interests because these sections relate to actually having a material personal interest, whereas a potential conflict arises at an earlier point. It also extends beyond sections referring to direct and indirect interests for the same reason, despite the fact that these concepts have been equated in case law.

The term ‘perceived conflict’ does not fall within the general law standard of real sensible possibility of conflict unless an objective interpretation of perception is adopted, as asserted by the ACNC. If assessed objectively, however, a perceived conflict does fall within the general law concept of real sensible possibility of conflict given that this is assessed by reference to a reasonable person’s consideration of the facts and circumstances. Inclusion of the term ‘perceived conflict’ appears to protect the charity’s reputation, whereas the concepts of actual and potential conflicts — and real sensible possibility of conflict — safeguard the decision-maker’s ability to act in good faith in the interests of the entity. Inclusion of the word ‘perceived’ means that this requirement is broader than statutory sections referring to material personal interests and direct and indirect interests, in that the responsible person does not actually have to have a conflict for the disclosure requirement to be triggered — it is enough if there is a perceived conflict.

On this basis it can be seen that the concept of real sensible possibility of conflict encompasses the concepts of actual, potential and perceived material conflicts used in Governance Standard 5 and the ACNC Conflicts Guidance Note. These concepts do, however, differ from statutory duties, as outlined in the preceding paragraph. It will be argued below that the concept of real sensible possibility of conflict encompasses all of the statutory duties, as well as the concepts employed in Governance Standard 5 and the ACNC Guidance Note. The concept of real sensible possibility of conflict is therefore the guiding principle for responsible persons.

Given that the term ‘real sensible possibility of conflict’ encompasses actual, potential and perceived material conflicts of interest, and that it is a well understood legal concept, it could be recommended that this term be used instead in Governance Standard 5. However, the terms ‘actual, potential and perceived’ are arguably a very apt plain English translation of real sensible possibility of conflict. These terms are preferable to the term ‘material personal interest’ which, as shown in Section IVA above, does not necessarily cover potential or perceived conflicts.

(i) *Should the Concept of Perceived Conflict be Removed from Governance Standard 5?*

In light of the above analysis, a corollary question is whether the term ‘perceived conflict’ should be removed from Governance Standard 5. The ACNC Review recommended that Governance Standard 5 be retained but that the word ‘perceived’

be removed. The reasons given were ‘consistency with the *Corporations Act*’¹⁴⁹ and to ‘address the most obvious concerns raised in submissions and consultations’.¹⁵⁰ The Law Council of Australia submitted that the term ‘perceived conflict’ was not ‘clearly established in law’ and was ‘capable of varied interpretation’.¹⁵¹

In this respect removing the word ‘perceived’ would not render the Standard the same as that used in the *Corporations Act* — s 191 states: ‘A director of a company who has a material personal interest in a matter that relates to the affairs of the company must give the other directors notice of the interest’ (subject to exceptions). It has also been shown above that, despite different wording, the obligations imposed under general law, statute and ACNC Governance Standard 5 can be reconciled so that the apparent incoherence is less than it appears.

It is submitted that the concept of perceived conflict should remain in Governance Standard 5 for the following reasons. First, the concept of perceived conflict can be equated with the general law concept of real sensible possibility of conflict if an objective bystander’s perception is employed. This is the way in which explanatory documents conceive perception.

Second, removing the word ‘perceived’, and leaving only ‘actual material conflicts’, would lower the standard imposed by Governance Standard 5 to below the standard imposed by the general law and statutory duties. This is inconsistent with the high standards expected of charities due to their public context and the public support that they receive. It has also been shown that disclosure of perceived conflicts protects the charity’s reputation. A charity’s reputation is an important facet of a charity’s interests. Moreover, whether or not inclusion of the word ‘perceived’ at the time that the Governance Standards were drafted was warranted, removing the concept of perceived at this point potentially sends a message that standards are being lowered.

A further point is that perceived conflicts do not result in penalties or necessarily give rise to disqualification from participating in decision-making — such conflicts must be disclosed. In addition, the ACNC’s Regulatory Approach should be borne in mind — a perceived conflict is unlikely to result in loss of a charity’s registration but would more likely give rise to inquiry, conversation, clarification or advice with a view to a charity and its responsible persons adopting the highest standards.¹⁵²

With all due respect to the ACNC Review Committee, there is therefore arguably no clear need to remove the term ‘perceived conflict’ from paragraph (e) of Governance Standard 5. In its recently released response to the ACNC Review, the Australian Government declined to accept this recommendation on the basis that ‘the

¹⁴⁹ ACNC Review (n 2) 50.

¹⁵⁰ Ibid 48.

¹⁵¹ Law Council of Australia, *Submission to the Treasury: Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation* (28 February 2018) 10.

¹⁵² See Australian Charities and Not-for-profits Commission, *Regulatory Approach Statement* (December 2018).

requirement for registered entities to disclose perceived conflicts of interest enhances transparency and mitigates the risk of poor behavior.¹⁵³

It is, however, recommended that the ACNC Guidance Note be amended to draw attention to responsible persons' other duties in relation to conflicts, as outlined in this article. The interaction between these other duties and the concepts of actual, potential and perceived conflicts could also be articulated.

VI CONCLUSION

This article has tackled the palpable incoherence and uncertainty endemic in the way that conflicts of interest of responsible persons of charities are regulated. This results from multiple obligations phrased in different terms arising from general law, statute and ACNC Governance Standard 5. This incoherence is reflected in the recommendation that the word 'perceived' be removed from Governance Standard 5 due to its alleged inconsistency with the equivalent duties in the *Corporations Act* (which are currently 'turned off').

Despite the myriad ways in which conflicts proscriptions are expressed, this article has demonstrated that they are arguably all encompassed within the concept of 'real sensible possibility of conflict' provided that the term 'perceived conflict' is assessed objectively. The real sensible possibility of conflict test can, in turn, be described in less technical terms, as whether the interest has the capacity to influence the vote of a responsible person in a not insignificant way.

This position is reached by the following steps. Section IVA demonstrated that the concept of material personal interest is broadly equivalent to the general law concept of real sensible possibility of conflict. However, due to the way in which the statutory sections are worded (in that they are expressed in terms of a responsible person having a material personal interest), a real sensible possibility of conflict arises at an earlier point, meaning that the general law prohibition is broader.

Section IVB demonstrated that the terms 'direct and indirect interest' are not significantly different to the general law standard of real sensible possibility of conflict and that elision has occurred. Statutory sections referring to direct and indirect pecuniary interests are narrower than, but encompassed within, the proscription on real sensible possibility of conflict. A key point to note is that the statutory sections are limited by a nexus to the affairs of the entity or a matter being considered at a committee meeting. By contrast Governance Standard 5 and the general law duty are not.

Section V showed that the terms actual and potential material conflicts are encompassed within the general law concept of real sensible possibility of conflict. Section V also showed that, although the term 'perceived conflict' has overlap with bias law and reflects additional rationales to the general law duty, it can, if objectively assessed, be equated with the test propounded in *Boardman v Phipps*. This is the

¹⁵³ See Commonwealth of Australia, *Government Response to the Australian Charities and Not-for-profits Commission Legislation Review 2018* (6 March 2020) 11.

approach propounded in the ACNC Conflicts Guidance Note, which refers to the impartial bystander.

The extent to which non-pecuniary and third party conflicts are included in the general law conflicts rule and statutory provisions is less clear than the interpretation adopted in the ACNC Guidance Note. It has, however, been argued that non-pecuniary and third party interests may constitute a material personal interest (if they have the capacity to influence the responsible person's vote) or a real sensible possibility of conflict. Moreover, even if such interests do not fall within the conflicts rule, they raise the duty to act in good faith in the interests of the entity and may also infringe proscriptions on misuse of position and information.

The overall guiding principle for responsible persons as concerns their multiple obligations relating to conflicts is therefore to avoid, or otherwise disclose and manage, situations in which there is a real sensible possibility of conflict.