Actuaries develop checklist for appointment of financial services Directors to ensure Boards do better

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- **Financial services companies need Boards with specific skills and capabilities to avoid misconduct uncovered by Hayne.**
- **Board recruitment models should recognise the special needs of banks and insurance companies.**
- **Chairs should have CEO experience.**
- **Unblemished careers not essential; experience during tough periods counts.**

Two actuaries have developed a skill and capability checklist to help Australian bank and insurance companies appoint Directors with the right qualifications to prevent misconduct uncovered by the Hayne Royal Commission.

Barry Rafe, a former Actuaries Institute President and experienced director and board advisor, and Ian Laughlin, a former APRA deputy chair, said their Dialogue* paper, *The Special Needs of Financial Services Boards*, provides a practical toolkit for Board appointments, specifically aimed at bank and insurance companies.

The Hayne Royal Commission revealed misconduct in the sector that resulted in the resignation of chief executives, Board members and Chairs, along with about $10 billion in payments to right wrongs. It highlighted acute failures. The Dialogue paper asks whether Directors enabled that behaviour because they failed to understand their businesses.

Financial service businesses are extremely complex, with long-term contractual obligations to customers, significant information asymmetry, short-term profit pressures and frequently, a third-party intermediary between the business and customer. Customers often have a large financial exposure to these institutions.

And while there has been substantial change in the membership of financial services company Boards since Royal Commissioner Kenneth Hayne handed down his findings in February 2019, there is evidence that the misconduct identified reflects Directors' lack of knowledge, "clearly reflecting systemic gaps between the essential Board skills and capabilities, and Board appointments", the paper states.

Identifying those gaps is essential to ensuring mistakes are not repeated. The Dialogue provides an aid to help financial services Boards recruit the correct mix of Directors. It states that assessment for a new Board member should be considered within a set of clearly defined criteria, and "if not, why not?"

Using the aid would likely lead to a Board with at least three Directors with deep operational experience, earned working in the financial services sector. These Directors should have hands-on experience to help guide them through the trade-offs management routinely make when running a bank or insurance company.

Boards should include Directors from other sectors; the Chair should be a former CEO; and those with 'golden' or unblemished careers may not be as valuable to the Board as those who have survived an insolvency or major crisis.

"Risk aversion to Director selection may result in Boards lacking Directors with foresight for emerging challenges and a lack of experience to be able to effectively recognise and manage them," the paper states.

Directors must understand broader community expectations and provide ethical leadership.

Mr Rafe said Boards are not made overnight. "They evolve over time, as Directors come and go." To continue to remain effective, "Boards therefore need to have a long-term plan involving Director assessment and skills/capabilities matching for the changing needs of the organisation."

Financial services profits come from leveraging other people's money, remuneration is high and linked to profits, and issues may take years to emerge clearly. Therefore, the Board must closely consider management priorities, decisions, behaviour, and culture.

"Boards are obliged to act in the best interests of the company but in financial services there are other legal and moral obligations to protect the interests of customers," Mr Laughlin said. "The skills and capabilities of the Board and individual Directors can have profound implications for conduct and culture."

Key capabilities include understanding customer outcomes. Boards must be collegial within a high-trust environment that allows individuals to contest key information. Risk appetite and management must be well understood from the customer's perspective.

Elayne Grace, Actuaries Institute Chief Executive, said a growing number of actuaries sit on Australian and international company Boards. They bring skills that include objectivity, independence, and good governance, which are part of the profession's rigorous training.

President Jefferson Gibbs noted that actuaries have strong analytical training and bring those skills to Boards and senior executive ranks. "As businesses become more complex, which is a given, actuarial skills and highly ethical behaviour must come to the fore in managing some of our biggest and most complex corporations."

A copy of the Dialogue paper *The Special Needs of Financial Services Boards* can be found **here.**

Barry Rafe is Principal, Rafe Consulting; a former President of the Actuaries Institute, a Fellow of the Australian Institute of Company Directors (AICD); and a Board adviser on governance, finance and strategy, at the AIDC. He has served on for-profit and not-for-profit boards.

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