The ASIC Governance Blues

The current governance/management crisis at Australia's financial market conduct regulator ASIC has attracted much media attention. It may have arisen from what are simply lax internal accounting, compliance, and reporting procedures regarding payments made by ASIC to providers of services (rent assistance, tax advice) benefitting senior executives in excess of approved amounts.

Or it may be more substantive and reflect a governance structure inadequate for ensuring integrity. The amounts are very small beer compared to many of the "rorts" seen in the private sector (or government) – but the failure of internal controls is a very bad look for a regulator.

What the crisis has brought to the fore (as well as salacious gossip about internal conflict) is the question of whether the current structure of management and governance within the regulator is ideal. And one source of concerns is that management and governance are hard to separate within such regulatory agencies – more so than in the private sector.

The ASIC governance structure (and also that of APRA, the ACCC, and other government statutory authorities) involves a "commission" structure. A small group of full-time executives (appointed by the government as commissioners, and one designated as CEO) are responsible for both the governance and management of the organization.

This contrasts with the conventional corporate structure found in the private sector. There, a Board (in theory appointed by the shareholder owners, but often a self-perpetuating "mates club") is separate from the day-to-day management of the business which is undertaken by the CEO and other full-time executive employees. The Board is responsible for monitoring company performance, determining strategy (including approving funding plans), and hiring and firing the CEO.

The Australian Financial System (Murray) Inquiry (of which I was a member) considered the question of appropriate governance structures for our financial regulators. We noted that a Board structure involving part-time external directors was put in place when APRA was established in 1998 but discarded within a few years. This reflected the recommendation of the HIH Royal Commission, which suggested that the existing Board structure blurred accountability between management and Board regarding APRA's performance.

The AFSI decided that a Board structure for the regulators was not obviously appropriate.

Why not? Well, it is very hard to imagine the Federal Treasurer giving up the powers to appoint (and sack) the CEO, determining funding level, or setting mandates and performance objectives (ie strategy). So what would a Board be left to do?

Essentially, what is left is monitoring of the performance of the regulators. While the regulators are required to report to the Minister and are subject to other forms of accountability, the Inquiry came to the view that establishing a Financial Regulator Assessment Board (FRAB) would be the best way to ensure monitoring of performance against their mandates.

That was one of the two (out of forty-four) recommendations rejected by the government! But it has resurfaced following the Hayne Royal Commission Report into Misconduct in the Banking, Superannuation and Financial Services Industry. Recommendation 6-14 of that Report was for the establishment of a new oversight authority, differing in some details from the AFSI recommendation, but otherwise similar to the FRAB.

In its response to the Hayne report the government accepted this recommendation (despite having earlier rejected the similar AFSI recommendation). Consultation on draft legislation occurred in early 2020, but the Bill has not yet been brought to parliament.

Whether having such an oversight authority will help resolve internal management and governance failings is an open question. In the 2015 ASIC Capability Review (led by Karen Chester – subsequently appointed as an ASIC Commissioner), a significant recommendation was "to realign internal governance arrangements by elevating the current Commission role to that of a full time non-executive function (not an external board), with a commensurate strategic and accountability focus, free from executive management responsibilities."

One feature of such a realignment of roles was to reduce the identification of commissioners with specific divisional activities and facilitate an independent determination of internal allocation of resources and financing between divisions. This was not immediately taken up by ASIC, but is reflected in the changed governance/management structure implemented by ASIC in 2018.

Has that change worked? If newspaper reports on internal ASIC conflicts are to be believed, not really.

The proposed Assessment Authority would not help with uncovering compliance failings such as those prompting the current crisis – that is more appropriately a concern of the Auditor. Its focus is to be the broader one of how governance and management enable the agency to achieve its mandate and performance expectations set by the government. This includes the suitability of internal resource allocations for achieving those goals.

It is difficult to imagine that the creation of the Assessment Authority would not also prompt a concurrent reconsideration and restructuring of internal governance and management arrangements.

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