



## ROCpod episode 2 – The importance of good governance

### Speaker Key

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**AN** Welcome to *ROCpod: Talking with the Registered Organisations Commission*, the official podcast of the ROC about the regulation of unions and employer associations. And in this monthly podcast we'll share essential information, uncover handy hints and tips and reveal our best tools for proactive compliance with the complex legislative requirements.



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**CH** Welcome to episode two of *ROCpod: Talking with the Registered Organisations Commission*. My name is Caroline Hamilton, I'm the Senior Communications Adviser with the ROC.

Today I'm joined by Professor Ian Gow from the Faculty of Business and Economics at the University of Melbourne and director of the Melbourne Centre for Corporate Governance and Regulation. Welcome Ian.



00:01:04

**IG** Thank you. Welcome Caroline.

**CH** And today we're talking about the subject of good governance and how it relates to registered organisations. The ROC is focused on promoting good governance in registered organisations so members of those organisations can have confidence in how they're being managed. So Ian tell me, what is governance and why is it important?

**IG** I think there's been debates about precisely what governance is.

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**IG** But I think it can be understood as the rules, the laws, the norms and even culture surrounding how decisions are made and how resources are allocated in complex organisations. And I think we have a tendency when we talk about governance to think of the archetypal public company but once you start seeing governance the way I see it you see governance everywhere.

So if you think about what's going on in Britain right now, they're facing significant challenges in terms of governance of the country when those really are governance issues, who has the rights to make decisions about whether to enter Brexit or not.

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**IG** But a country is a very complex organisation. But you'll see governance operating at the level of how is the local cricket club organised, how are resources allocated between the senior team and the junior team and who makes decisions, the parents or the coaches and things like that.

So I think governance can be understood as a very wide-ranging idea applying to many different kinds of organisations.

**CH** What are the principles of good governance?

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**IG** I think in some ways one of the myths of governance is that there's a universal set of good governance principles. So what works for one organisation is the right governance principle for every organisation.

When we think of public companies, there're obviously a lot more of them than there are other kinds of organisations, we do have a sense that there's some ideas of better governance and some ideas of worse governance. But I think often it's actually more difficult to say precisely what is good governance in the details as widely understood.

Nonetheless, I think there are certain ideas that are pretty universal in terms of good governance.

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**IG** And some of the ideas you might see, for example, in the ASX Corporate Governance Principles. Some of those do apply to other kinds of organisations, so having a clear purpose to an organisation, having an organisation understand what it's about. And then having fairly well-defined rights and responsibilities around how the organisation goes about achieving those goals. That's the generic idea of good governance.



**CH** And so, just touching on that, what other lessons can registered organisations learn from governance in the corporate sector?



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**IG** I think it makes sense to say look at something like the ASX Corporate Governance Principles. I think you'll find even in the private sector in terms of public companies there'll be debate about how good some of those principles are, but I think there's a broad consensus that they're broadly in the right direction.

So definitely the broad corporate governance principles are something that one could go and look at and say, okay how does this apply to my organisation?

But I think often the right way to think about governance is almost a case study approach.



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**IG** And a lot of the case studies that you will look at in terms of corporate governance, typically what you tend to see is where governance has broken down.

Often there are lessons from some of those cases that apply to many different kinds of organisations in terms of, we were expecting the board of directors to do something or the governance mechanism was assuming that they were doing one thing but they weren't doing, that kind of thing. There was a failure there.

And so often some of the case studies are very applicable to understanding governance.



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**IG** Because I think one challenge with governance is we have a tendency to talk about principles, so Structure of the board to be effective and add value is one of the ASX Corporate Governance Principles.

And it's hard to disagree with that at some level. But understanding precisely what that means often means getting into the specifics and saying, okay here's an example where something failed and this is a governance mechanism that might have addressed that failure.

And I tell students it's amazing what you can actually learn nowadays from going and watching good documentaries on HBO or Netflix, literally this is almost a show about corporate governance.



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**IG** Netflix wouldn't advertise it that way but it's amazing what you can learn nowadays just watching good quality documentaries in terms of understanding how



organisations as complex as say HSBC, a large bank, how they had trouble, how Enron had problems around about the turn of the century.

But even relatively small organisations... Theranos is a fascinating case. I think there's already one documentary made about that and then there's a Hollywood movie in production about that one.



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**IG** I think studying those case studies and saying, okay even though the issues that organisation faced may not precisely map to what my organisation faces I think there's often some generalisability of the lessons learned in those cases.

**CH** The legislation that governs registered organisations, the RO Act, requires a committee of management to be in place in each registered organisation. What role do you see them having to play in governance?



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**IG** I think the basic idea is there's a divide between the higher order purposes of the organisation, what was it set up for, what are the members wanting and so forth and the reality that on a day to day basis the members can't be actively involved in management.

So it's clearly an analogue to the board of directors in a public company. And the way boards of directors have been understood is essentially they are the body that makes the decisions on a day to day basis that have control over the organisation in practice.



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**IG** In a very large company, the reality is you actually almost have three levels, so you have the shareholders who are responsible for appointing the board. And then the board is part-time, very busy and the organisation's very complex and so there's a lot of delegation from that board of directors to the actual management.

But in principle the board of directors is responsible and so the committee of management is the analogue to that for a registered organisation. And I think the same basic ideas apply.



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**IG** The difference may be that depending on the scale of the organisation, the board of management might be very involved in the day to day aspect of things in small organisations.

But then in larger organisations you may see similar ideas that you see in large public companies which is the board of management is there to oversee what's going



on on a day to day basis but they don't necessarily have their fingers in all the details of what's going on in the organisation. So that's the direct analogue I guess.

**CH** Some of our registered organisations are quite small, depending on their structure. When you have a small organisation how can you go about achieving good governance, for example separate duties when there are very few officers?



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**IG** Sometimes there's a distinction between corporate governance which I view, as I mentioned earlier, as the higher-level idea of, what is the purpose of the organisation? And how do we structure the decision rights and who gets to vote and all these kinds of things, and what you might consider as control.

And when I say control, I mean ideas like separation of duties and who has control over the bank account and who can write cheques and all those kinds of things.



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**IG** I think for a small organisation, these two ideas almost coalesce to some degree. So in a small organisation it's often very difficult to separate the control issues from the corporate governance issues because often the organisation doesn't have a huge amount of resources, there isn't a huge number of people.

So it's almost that the first order aspect of corporate governance is just establishing good controls.

And some of this would have been talked about in your earlier podcast, how do you set up good controls, how do you separate duties, how do you make sure that the organisation's being run for the benefit of the members, not for the benefit of the individuals who are actively involved in the management?



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**IG** And so those corporate governance and control issues almost merge at that point in some ways.

But even in large organisations often very similar ideas apply in the sense that many, say Silicon Valley organisations for example, they're quite large but they have very active founding members who have very significant control rights.



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**IG** And so the issues around what decisions get to be made by those founders and what's off-limits in some sense, they again blur the line between being corporate governance and being control issues in a lot of ways.

**CH** So the obvious question there is what happens if good governance processes aren't



in place within an organisation?

- IG** I think if good governance processes aren't in place they will often manifest in control issues. So if the purpose of the organisation isn't clear, there may be ambiguity in terms of, is what's happening serving the purpose of the organisation?



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- IG** A good case study in Australia might be CPA Australia. I think the vision there was... And this was a case study that was very prominent late 2017 through to 2018. Well worth reading about if you can go through news articles.

This was a case where, at some level there were control issues, was the CEO of that organisation being paid too much, was the board not doing its duty in terms of overseeing the compensation of the CEO?



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- IG** But I think there's manifestation, deeper corporate governance issues. And with that organisation there was legitimate disagreement about what the organisation was trying to achieve.

I think Alex Malley who was the CEO back at the time of the events I'm talking about had a vision that CPA Australia could be a bigger organisation, could be more ambitious in terms of what it was achieving. And for a lot of members that was not serving what they were after.

So a challenge with that organisation was the members had different interests. Some members would have been looking to CPA to basically provide a brand that they could operate under.



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- IG** Others would be looking for CPA Australia to provide education opportunities so they could learn things. Others would view it as a way that they could attend meetings and just get more involved in the profession in some ways.

And in an organisation where the purpose of the organisation is unclear, that's where you tend to have more challenging governance issues. And how those governance issues actually manifest might end up looking like control issues.

And in that case, as I mentioned, the big control issue was was the board sufficiently independent in negotiating the compensation contract of the CEO?



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- IG** Or were they perhaps, as was alleged, almost serving the interests of the CEO at that point?



**CH** Do you have any other advice or tips for registered organisations to achieve good governance if it's something they want to start turning their minds to? Or to even just make sure, do a bit of a health check to see if they've got the right systems and processes in place?



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**IG** I think there's a multipart answer to that. One thing is, because many of the organisations would be smaller, I think you want to dot the i's and cross the t's in terms of having the control systems in place.

And I think one good thing that registered organisations have in their favour in some sense is by making the investment to have Tier 1 financial reporting. A lot of the issues that surround financial reporting relate to setting up good controls.

And a lot of those basics will be in place almost as a consequence of that choice. And then once those details are sorted out the next level is to step up a bit and say, okay how are we thinking about things from a corporate governance perspective?



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**IG** And again, I think a challenge with corporate governance is a tendency for us to talk very much about generalities but I think that's almost the nature of the game.

And in the case of registered organisations it's, okay what are we trying to do as an organisation, what do our members want? Are we structured appropriately so that we can be fairly confident that the organisation is driven to achieving those objectives and those goals of the members?



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**IG** And then also if things go wrong, what are the things that might go wrong? I mentioned the control issues, people spending money on personal travel or something like that, those basic control issues are certainly one thing.

I don't think it would be front of mind, but from a higher-level corporate governance perspective or governance perspective, you might also be thinking about, well what are the potential conflicts between the interests of different members?

In some organisations, members have very similar interests and it's very clear and that's great from a corporate governance perspective. But then in other organisations there can be conflict in the sense that one set of members has one set of interests and another set of members has a different set of interests.



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**IG** And then the question might be, okay if this conflict rises to a head in some sense, do we have the corporate governance processes to handle that?



And again, as I said, you can see this in terms of a cricket club or, to pick something that's current, what's going on in Britain. Do they have the governance processes in Britain to handle the complexity of what they're going through right now?

And that's a question you can actually ask in advance in some sense and say, okay do we as an organisation have the processes to resolve conflict and to make sure that how decision rights are allocated is appropriate and clear in advance?



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**CH** Thank you again for joining us today Ian. We really appreciate you taking the time to talk with us.

**IG** Thank you.

**CH** In summary, governance is about rules, laws and culture around how decisions are made. Universal good governance principles include having a clear purpose to an organisation, having an organisation knowing what it is about and having well defined rights and responsibilities.



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**CH** If you're wondering how governance applies in your organisation, you should start by looking at your rules, policies and structure. If you're unsure where to find your rules, you can locate them on the Fair Work Commission's website, [www.fwc.gov.au](http://www.fwc.gov.au)

There are lessons to learn from the corporate sector such as the broad governance principles issued by the ASX. A good way to look at governance is to take a case study approach.



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**CH** This largely relates to where good governance has broken down.

For registered organisations there is a general understanding the committee of management is responsible for strategic management. And, depending on the size of the organisation, involvement in the day to day decisions including control processes, for example the separation of duties and who has control over the bank account.

If good governance processes are not in place, this will often manifest itself in a breakdown in issues of control.



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**CH** The committee of management is responsible for ensuring that the organisation is being run for the benefit of the members and not the individuals actively involved in the management of the organisation.

More information on running a registered organisation can be found on our website



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