

# **Stalled RBA governance board vital to manage AI's threat to the financial system**

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I was appointed to the panel to review the Reserve Bank of Australia. Before starting the Review, I did not think I would favour changing the board structure of the RBA, but I changed my mind after our consultations within and outside of the RBA. Most media focus has been on the composition and nature of the proposed monetary policy board, which is natural given the effect board decisions have on the public. However, the broader debate overlooks the critical importance of the proposed governance board.

The RBA is a Commonwealth Corporate Entity with around 1,400 staff members. While a small employer compared to Australia's great companies, it is an institution with complex operations and risks, many of which are essential to the sound functioning of the Australian economy. In addition to highly visible monetary policy decisions, it provides banking services to the Government, manages Australia's foreign exchange reserves, provides Australia's banknotes, runs critical payments infrastructure and sets payments policy.

The Review found corporate governance oversight relatively unchanged since the establishment of the RBA. Although the RBA had found ways to make governance arrangements work, they fell short of best practice. The Governor is the sole accountable authority responsible for managing the RBA and is the key decision-maker on corporate matters. Internal Executive and Risk Management Committees support the Governor. Before the Review, the Deputy Governor was in charge of day-to-day operations and oversight of Finance, Audit, Human Resources, Risk and Compliance, Information and the Secretary/Legal department. The Reserve Bank Board provides little management oversight, and its role under current statutory arrangements is ambiguous and needs to be clarified. Current arrangements concentrate responsibility on one individual; we found this to be unfair and has the potential to create risk.

While the RBA has adopted the recommendation of appointing a Chief Operating Officer to oversee some management functions previously performed by the Deputy Governor, taking the next step of establishing the Corporate Governance Board is essential for the effective functioning of the RBA, as is corporate governance best practice as set out in the ASX Corporate Governance Council guidelines .

The recommendation for establishing the Governance Board is critical because the operations of the RBA are becoming more complex. One reason for our recommendation was concern about large risks coming from technology, such as cyber security. In the past decade, the number of IT staff employed by the RBA has almost doubled, reflecting technology's role in the Australian financial system.

Just fifteen months after handing the Review to the Treasurer, a new risk has emerged around AI technology. If we were to write this Review today, we would probably specifically mention risks associated with AI in the list of responsibilities of a governance board. While a Monetary Policy Board needs to take the effects of AI on inflation and employment into account, the impact of AI on the functioning of the Australian financial system presents a different (massive) set of issues best addressed outside of a Monetary Policy Board. It shows that future risks may arise quickly, be unanticipated, be substantial and that Australian policy institutions must be vigilant.

Practicalities on how the two new boards should be populated are addressed in the Review. The recommendations are to ensure continuity of decision-making on both boards by asking current board members to continue their term on one of the new boards and for the Government to consult with the Shadow Treasurer to ensure broad bipartisan support for the new arrangements. Current Board members are probably best placed to decide on which board they can best contribute.

It is apparent from the media that monetary policy settings in the current high-inflation environment are uncertain, with little consensus on which way interest rates should move. While the Australian public now has a Reserve Bank Board with structures in place with more time and resources to test the logic of monetary policy decisions, the Governor and the Reserve Bank Board still have their work cut out in deciding monetary policy. Establishing the Governance Board will clarify responsibility for monetary policy versus corporate governance decisions and enable the monetary policy board to focus on difficult monetary policy decisions.

An RBA Governance Board overseeing resourcing, succession planning, risk management and technology for one of Australia's most vital institutions is critical to the Australian people.

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