Who will regulate the regulators?

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The establishment of statutory regulators constitutes one of the most significant governance reforms of the last century. There is a global surge in the popularity of such agencies as an alternate mode of governance. To deliver on this potential, regulators need to be well governed. Governance of these agencies centres around their governing boards (GB). Five design features relating to GB can significantly improve the governance of regulators.

First, the law typically creates a board governed by a board, an authority by an authority, a council by a council, a commission by a commission, etc. For example, the Securities and Exchange Board of India Act, 1992 establishes a board, namely, the Securities and Exchange Board of India. The general superintendence, direction, and management of the affairs of this board vests in a board of members. In simple words, the former board is an entity, while the latter is its governing body (GB). Most statutes, however, do not distinguish between the two. This is not just a problem of semantics but has the potential for mix-up or reversal of roles, making it difficult for the GB to steer the entity, establish its objectives, and hold it accountable for delivering on its objectives.

Second, it is normally difficult for an entity to take decisions about itself or its working with complete objectivity or hold itself accountable for its conduct or performance. That is why decisions about a company, for example, and process design are placed in the board of directors.

Conceptually, the GB's primary responsibility is to act as a hands-on principal to hold the management accountable. It may, however, be hard for a GB to hold the management accountable if it has only managers as members. The GB, therefore, needs to have appropriate external representation. Most statutes do not provide for this representation and the required interface between the regulator and society in the regulator's governance.

There are a few options. The presence of a few eminent persons in the GB as part-time members (PTMs) is one of the more effective options. They attend its meetings, vote on issues, and take decisions on its behalf along with other members of the governing body. They have skin in the game while not being beholden to the management. PTMs on a regulator's GB are roughly analogous to independent directors on corporate boards. The international best practice in corporate governance is that for effective accountability, there must be at least an equal number of independent directors as the number of management directors. Therefore, the number of PTMs should match the number of whole-time members (WTMs) on the GB for the PTMs to have an effective voice in the GB's meetings. The process of selection of PTMs, as well as of WTMs, needs to be robust and inspire confidence.

Third, the government typically has a few official nominees on the GBs of regulators. The views of such nominees, being the representatives of the minister who is accountable to the legislature, carry disproportionately more weight in the decision-making process. Further, the government is often a market participant as well as subject to pulls and pressures from various interest groups. It may not always be possible for the official nominee to take an objective position in all matters coming up before the GB. It is advisable, therefore, that the GB does not have any nominee from the government, particularly when the latter is empowered to give directions to the regulator on matters of policy and even supersede the GB. Ideally, a regulator may not have any nominee at all.

The nominees generally have a conflict of interests as they look at every proposal that comes before the GB from the perspective of the organisations they represent and espouse the interests of the organisations which have nominated them.

Fourth, the independence of a regulator critically rests on the professional strength of the leaders, namely, WTMs (including the chairperson) to withstand the influence of articulate interest groups and the pressures of fear and favour from any quarter. A term of 3-5 years for these positions comes in the way of such strength. An individual, who has the demonstrated capability, would not join a regulator for a 3-5 years tenure. A successful advocate does not wind up his profession and join as a judge for five years. Further, the said tenure with the retirement age of 65 years typically leads to selection of individuals who have retired or are about to retire. A term of three years is very short and by the time the members acquire the required knowledge, expertise, and efficiency, one term will be over. Sixty is not an appropriate age to learn entirely new things and achieve mastery. The leadership position with a regulator is full of stress and tension and is not very conducive for an individual at 60. If the regulators are to maintain true independence, they must attract younger individuals, who have demonstrated their capability in the relevant field, for a reasonable period of service.

Fifth, a regulator in India typically performs three functions, namely, quasi-legislative, executive, and quasi-judicial. The statute should envisage a separate organisational unit responsible for each of the distinct types of functions and powers. These units should operate at an arm's length from one another to act as mutual checks and balances to address public law concerns relating to separation of powers.

The statute should mandate the GB only to perform quasi-legislative functions and to provide direction to the organisation. GB should be enabled to delegate executive and administrative tasks to different functionaries in the organisation, who would discharge the duties and functions on behalf of the regulator, in the manner prescribed. Such delegation would enhance the organisational capacity to ensure timely service delivery as well as promote greater accountability.

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