



Submission to the New Zealand Productivity Commission Inquiry into Regulatory Institutions and Practices

Introduction

1. One of the key performance indicators (KPI) identified during the formation of the Ministry of Business, Innovation and Employment (MBIE) was Regulatory Excellence. This KPI involved the establishment of a cross-organisational function "with the role of analysing systemic regulatory weaknesses / challenges in areas that MBIE is responsible for, and identifying interventions to address them."
2. MBIE's thinking about regulatory system performance occurs in the following context:
 - a. MBIE is one of the most significant regulatory agencies in New Zealand, with primary responsibility for designing and overseeing at least 16 regulatory systems
 - b. MBIE has a significant reach in both internally implementing those regulatory systems and through its oversight of Crown Entities that play a key role in implementing those systems
 - c. MBIE has significant responsibilities for "matrix" regulatory systems that apply in other regulatory systems eg of an estimated 98 occupational regulation schemes, MBIE is responsible for 40, and MBIE is responsible for Cabinet's occupational regulation framework
 - d. A number of the regulatory systems that MBIE is primarily responsible for have had systemic failures in recent years, providing a strong foundation to learn lessons from those failures and apply those lessons to other regulatory systems
 - e. MBIE has the ability to look across its own regulatory systems to consider cross-cutting issues or opportunities eg the over-lap between workplace health and safety with building standards or the resources sector, the interface between immigration, skills and labour market standards.

Focus of this submission

3. In light of the above context, MBIE's submission addresses two issues:
 - a. what MBIE has learnt from failures in the regulatory systems that it's responsible for

- b. how MBIE is responding to those failures, through the establishment of the Regulatory Systems programme.
4. This submission does not directly respond to the questions in the Commission's Issues Paper, rather it offers general observations that the Commission can consider in progressing this Inquiry. This submission concludes by offering some observations about the interface between the Inquiry and MBIE's Regulatory Systems programme, and where MBIE considers the Inquiry could focus to provide particular value.

What has MBIE learnt about regulatory system performance

5. MBIE, and its predecessor agencies, have been responsible for a number of regulatory systems where the intended regulatory systems' outcomes were not achieved. Three notable examples of failures in the regulatory systems¹ MBIE is responsible for are:²
- a. Financial market regulation
 - b. Health and safety
 - c. Building standards regulation.
6. Attached is a paper³ which draws upon these examples to present MBIE's analysis of the changes to the regulatory landscape and in particular the role of regulators as a particular facet of regulatory design. This paper concludes with the suggestion that what is required is "a responsive, or "really responsive" regulator that understands the regulatory environment and applies a range of fit-for-purpose strategies for achieving desirable regulatory outcomes efficiently and effectively."

Processes have been in place to scrutinise regulatory systems, but these have not prevented regulatory failures

7. There are a range of existing processes, which scrutinise the performance of regulatory systems, including accountability arrangements, Performance Improvement Framework Assessments, the Treasury-led Best Practice Regulation assessments and regulatory impact assessment requirements. More recently the Government has introduced Regulatory Stewardship requirements and regulatory disclosure statement requirements.
8. MBIE supports all of these existing processes, and has drawn upon these processes in its own thinking about how to assess regulatory systems.
9. A lot of attention is now paid to regulatory system performance, and the range of mechanisms that assess regulatory system performance and should identify vulnerabilities has been increasing over time. While some of the

¹ Other areas where there have arguably been regulatory system failures with some similar features, although not necessarily of the same magnitude, include the regulation of foreign charter fishing vessels and of immigration advisers.

² Attachment One includes a list of references to official documents relating to the failures of these systems, which the Commission may wish to review to identify common themes both in the failures and in the government responses.

³ Searancke, G (2013) *Risks & Disasters: Dealing with the "Elephant in the Room" – Governing the Regulators*. Ministry of Business, Innovation and Employment, Wellington. Paper for NZ Law Society.

current processes were not in place at the time of regulatory systems' failures, some were. We question whether the current processes alone may have revealed weaknesses within the regulatory systems which increased the risk of failure⁴, and could, therefore, have prevented system failures, or whether something more is needed.

10. One of the key challenges for the Commission in the Inquiry will be in designing ex-ante indicators for identifying the both good regulatory system performance and the risk of regulatory system failure, in an environment where the effectiveness of some of the existing processes has not yet been fully assessed or demonstrated.

MBIE's hypotheses about why regulatory systems can be at risk of failure

11. Based on MBIE's knowledge and experience, particularly through reflecting on why the systems MBIE has responsibility for have failed, MBIE is developing a number of hypotheses for why regulatory systems may not meet their objectives, which may in the worst cases result in systemic regulatory failures. MBIE suggests that the Commission considers the hypotheses in paragraph 13 below both as part of formulating an understanding of influences and incentives on regulatory regimes, and in formulating its recommendations for this Inquiry.
12. MBIE has also identified a number of practices that it thinks need to be in place or conditions that need to be met, for regulatory systems to perform well, which are identified separately in paragraph 14 below. In many cases, the hypotheses about regulatory system failures could relate to the absence of these practices or conditions.
13. From our experience indicators that a regulatory system is not meeting its objectives or may be at risk of systemic regulatory failure include:
 - a. there is low use of business intelligence generally eg analysis of administrative data, drawing on front-line knowledge and experience, and drawing on experts and stakeholders' knowledge and experience. This can result in there not being a robust evidence on which to base regulatory intervention, and also in determining whether regulatory regimes are, or continue to perform, effectively
 - b. the role of operational policy is not universally understood, done well or valued – this may limit the effective translation of policy into quality service delivery, education and enforcement and inhibit feedback loops on the workability, or otherwise, of regulatory regimes
 - c. the presence of cultural and attitudinal barriers which prevent issues and risks that have been identified with regulatory regimes being raised up and addressed, either from the front-line or within senior-level discussions or even with Ministers. A corroborating indicator would be evidence that the response to issues and risks being raised has resulted in a cultural tendency to work-around systemic issues rather than addressing them. Given this seems to be a key component

⁴ See Mumford, P. (2011) *Best Practice Regulation – Setting Targets and Detecting Vulnerabilities*. Policy Quarterly – Volume 7, Issue 3 – August 2011, 36, at 41.

of all of our regulatory failures, we question whether these barriers may exist within a regulatory systems, or may extend across the public service more generally

- d. with the benefit of hindsight, poor judgments or inappropriate policy assumptions have been made about the approach to take to regulatory systems (eg whether prescriptive or principles based regulation is more appropriate), or the approach may have been the right one but not implemented effectively. For example, principles based regimes often require a level of prescription in regulation or guidance, in the case of both the health and safety and building standards systems, this was not provided, which contributed to the regulatory failures in those systems
- e. Regulatory intervention is not considered as part of a package of broader system related measures ie how to use a mix of regulatory and non-regulatory incentives / mechanisms to address issues. This could be because in some instances regulatory intervention is easier and within Government control, whereas influence and negotiation can take longer and be harder to achieve
- f. Neither the international and / or the New Zealand context is not adequately taken into account in the design of regulatory frameworks. For example, sufficient thought is not given to achieving a sophisticated balance between the many benefits of using international frameworks and standards for business (eg ease of doing business across borders, use of other capability, experience and jurisprudence) and the links between regulatory frameworks with conditions and other social issues unique to New Zealand. Alternatively, the characteristics of New Zealand markets, including whether the scale of those markets impacts on competitive features, may not be sufficiently well understood. This may mean insufficient consideration is given to whether other actions in addition to the promotion of competition is necessary to ensure the optimal regulatory outcomes
- g. the mandate and ownership for regulatory systems is unclear or mixed, which results in some issues slipping between the responsibilities of different parties. Our view is that informal relationship mechanisms for managing multiple mandates that rely on individuals can operate effectively for a time but not in an enduring manner, and that we need to be more clever at using legislation, and accountability tools to create the right incentives to encourage in-going collaboration
- h. organisational norms and values which are not fully aligned with regulatory systems' objectives because the regulatory objectives sought to be delivered, and expectations on regulators, are unclear, or there is not sufficient capability, or accountability, or monitoring of the delivery of regulatory outcomes.

14. Practices or conditions present in regulatory systems which are performing well are likely to include:

- a. the regulatory system's objectives are clearly stated and understood at all levels within the regulatory system, including by any Crown Entities

and other delegated regulators (eg Territorial Authorities, industry associations or occupational regulation bodies) involved in the regulatory system

- b. adequate resourcing and timeframes are provided to implement the regulatory system fully, and resourcing is reviewed on a regular basis to ensure it remains adequate
- c. Where there are crown entities involved in a regulatory system there is regular, quality, interaction between the monitoring/policy agency and the boards around not only performance of the entity, but also performance of the regulatory regime
- d. There is: good business intelligence; recognition, and use of, the compliance pyramid; a quality operational policy function; and a good understanding of intervention mechanisms and the appropriate use of regulatory frameworks
- e. There is a culture of being able to raise issues and risks with regulatory systems within government agencies and entities and clear procedures for working through these and addressing them;
- f. the regulatory system is subject to continuous or regular review and assessment of its performance, to ensure the system's objectives continue to be met – the review process should include assessments of:
 - i. whether political will and interpretation of the regulatory system's objectives has changed over time
 - ii. the contribution of Crown Entities and other delegated regulators involved in a regulatory system to the regulatory system's objectives
 - iii. whether the levers available to influence any Crown Entities' approach have been used to their fullest potential eg setting explicit expectations, actively engaging with the Board and considering recommending the use of Ministerial Directions⁵
 - iv. whether any features of a regulatory system that reflect path-dependency, or approaches to regulatory design from the time that a system was implemented, should be updated to reflect developments in best practice approaches to regulatory design or any contextual changes
- g. a balance is struck between regulator independence and political requirements for checks and balances on regulators.

15. MBIE considers that it is best to treat regulatory regimes as "living" and requiring on-going attention rather than operating systems on a "set and forget" basis or relying on mandatory statutory reviews in "x" years. To assist in achieving this we believe the following mechanisms could be considered:

⁵ Similar issues should be assessed regarding the use of levers to influence other delegated regulators.

- a. exploring the idea of the use of a form of “Statements of Intent” for regulatory systems, which formally sets out the expected outcomes or objectives of the systems and the contributions that different parties are expected to make to those objectives, and monitoring of the performance of regulatory systems against those Statements of Intent and key indicators. This would include using this tool to work with Crown Entities to monitor performance of regulatory outcomes.
 - b. Having a good understanding of the intervention logic of when and how to use legislation, regulation and tertiary instruments, so that regimes are flexible and can move over time, and there is a balance between given those with the technical expertise the ability to continue to evolve standards, with more significant policy issues still being able to be the responsibility of elected officials.
 - c. That where issues with regimes are identified which need to be addressed to keep regimes working effectively and resolve unexpected regulatory impacts on business or others, but where these are too small to get priority through the busy legislative process, there are omnibus bills or broad common purpose bills which allow these amendments to proceed. We note that the statutes amendment bill does not often enable this given its requirements that it contain only minor or technical policy issues
16. While mandatory statutory reviews have a theoretical appeal, in our experience these often become pro-forma, having insufficient attention paid to monitoring and evaluation ahead of the review date, or inhibiting regular maintenance of the regulatory system (eg issues can be parked for the statutory review rather than being addressed earlier through other mechanisms, such as omnibus bills or stand-alone regulatory changes). The Commission could consider whether processes to ensure regulatory systems are well implemented and maintained can be effectively supplemented by statutory review processes, while mitigating the above risks.

MBIE’s Regulatory Systems Programme

17. Reflecting the expectation that MBIE will analyse systemic regulatory weaknesses / challenges in areas that it’s responsible for, and identify interventions to address those challenges, MBIE has established a portfolio programme on Regulatory Systems as one of its 13 Portfolio Priorities for 2013/14.
18. The primary objectives for the Regulatory Systems programme are to ensure that MBIE has robust processes to know whether the regulatory systems it’s responsible for are performing well, by:
- a. systematically identifying the best elements of regulatory practice from individual regulatory systems, and extending those practices across all the regulatory systems that it’s responsible for
 - b. applying robust processes to identify and respond to opportunities to improve regulatory system performance and risks.

19. Secondary objectives for the Regulatory Systems programme, presented within MBIE's ways of working framework, are to:

Shape

- i. ensure that MBIE is "ahead of the game" in assessing regulatory system performance, thinking about issues before they arise
- ii. enable MBIE to provide leadership across the broader public sector in regulatory system performance and influence broader regulatory thinking

Collaborate

- iii. better understand and utilise the connections between and within MBIE's regulatory systems, including the connections from policy functions through operational policy and into implementation and the on-going operational delivery
- iv. ensure that MBIE's key regulatory staff have a shared understanding of the main drivers of end-to-end regulatory system excellence and the broader New Zealand regulatory context

Deliver

- v. enable MBIE to draw on lessons from well-performing regulatory systems and past regulatory system failures, then apply those on a business-as-usual basis
- vi. ensure that MBIE regularly assesses where regulatory systems are contributing well to MBIE's targets, where there are opportunities to improve system performance, and where systems present risks to achieving MBIE's targets
- vii. better understand the capability MBIE requires to deliver on its end-to-end regulatory functions.

20. The Regulatory Systems programme will involve:

- a. undertaking an initial assessment of all the regulatory systems⁶ that MBIE is responsible for, to describe how the regulatory system operates to achieve its outcomes, and to identify positive features within a system, opportunities and risks
- b. identifying where priorities are to review in-depth the performance of those regulatory systems and developing processes to regularly review, over time, all of the regulatory systems that MBIE is responsible for
- c. looking across all of MBIE's regulatory systems to identify any systematic strengths, opportunities and risks

⁶ The assessment processes will use the Map of regulatory system in Attachment Two. This will be supported by a description of good regulatory system performance, and criteria and indicators for the assessment of regulatory systems, which are currently being developed. MBIE would be happy to share this material with the Commission as it is developed.

- d. a range of internal MBIE staff and representatives of Crown Entities involved in the relevant regulatory systems, with processes to ensure that honest, robust and constructively critical assessments of regulatory performance can occur safely – these processes need to over-come the cultural barriers that may exist for issues and risks being raised (see paragraph 13.c above)
- e. a range of external stakeholders, both in relation to individual regulatory systems and the systematic review across all of MBIE's regulatory systems
- f. reviewing MBIE's approach to the use of different regulatory instruments (eg legislation, regulation, rules, and codes of practice) and non-regulatory instruments (eg authoritative guidance) to ensure the right instruments are used to achieve the desired regulatory outcomes
- g. reviewing MBIE's approach to operational policy functions to ensure that policy objectives are effectively translated into regulatory delivery functions
- h. considering how MBIE approaches systemically approaches issues of regulatory system hygiene or maintenance, to ensure that relatively minor or more administrative issues are regularly addressed and do not lead to more systemic issues.

Interface between the Inquiry and MBIE's Regulatory Systems programme

21. There are synergies between the Productivity Commission Inquiry and MBIE's Regulatory Systems programme, which MBIE would like to continue to explore with the Commission as the Inquiry progresses. These include:
- a. sharing information about approaches to assessing and improving regulatory system performance
 - b. sharing learnings from the assessment of individual regulatory systems, to identify themes that the Commission may consider in formulating its recommendations
 - c. participating in round-table discussions and workshops for both MBIE's Regulatory Systems programme and the Commission's Inquiry.

Where could the Inquiry focus to provide particular value

22. MBIE welcomes the focus in the Commission's Inquiry Terms of Reference on developing recommendations to inform the design and establishment of new regulatory regimes and regulatory institutions, and on system-wide recommendations to improve the operation of regulatory regimes over time. MBIE also welcomes the focus on considering improvements to regulatory systems over time.
23. MBIE considers that guidance on the features of good regulatory systems, and how to design, implement, monitor and assess regulatory systems and institutions will be particularly valuable. This guidance material should be

useful for a wide range of stakeholders who have an interest in objectively assessing the performance of regulatory systems, including Ministers, agencies and Crown Entities involved in providing policy advice on and implementing regulatory systems, regulated parties and broader stakeholders.

24. MBIE also considers there would be particular value in:

- a. guidance on how Ministers, agencies and Crown Entities can systemically approach issues of regulatory system hygiene or maintenance, both to prevent risks of regulatory failures and to identify and implement opportunities for improvements to regulatory systems
- b. guidance on how to strike the right balance within regulatory systems between the use of different regulatory and non-regulatory instruments, and how to choose the right instrument, to achieve the desired regulatory outcomes
- c. identifying who should own this guidance and ensure it is used and kept up to date.

Attachment One: References to official documents relating to the failures of regulatory systems

Financial market regulation

Two key reports relating to finance company failures are:

- [Report of the Commerce Committee inquiry into finance company failures](#)
- [Government response to report of the Commerce Committee](#).

Capital markets report and the resulting government action plan available on the [Ministry's website](#).

Documents related to the establishment of Financial Markets Authority are available on the [Ministry's website](#). The key document is the [April 2010 Cabinet paper](#).

All the policy and related documents relating to the reforms that led to the Financial Markets Conduct Act 2013 are available on the [Ministry's website](#).

Health and safety

Key documents related to the Royal Commission on the Pike River Coal Mine Tragedy are the:

- [Final Report of the Royal Commission](#)
- [Government response to the Royal Commission](#)
- [Updated Pike River Implementation Plan](#)
- [Independent investigation report to the Chief Executive of MBIE](#).

Key documents relating to the [Independent Taskforce on Workplace Health and Safety](#), including the Government response are:

- [Working safer - a blueprint for health & safety at work](#)
- the [Overview Cabinet paper](#), which describes problems with the health and safety regulatory system and the Government response
- the [Effective regulatory framework Cabinet paper](#), which addresses regulatory elements of problems with the health and safety system.

Building standards regulation

The 2002 Report of the Overview Group on the Weathertightness of Buildings is available on the [Ministry's website](#). This report is the key initial diagnostic of the building control failure, which provided the foundation for the 2004 reforms.

Other key reports and papers available on-line include the:

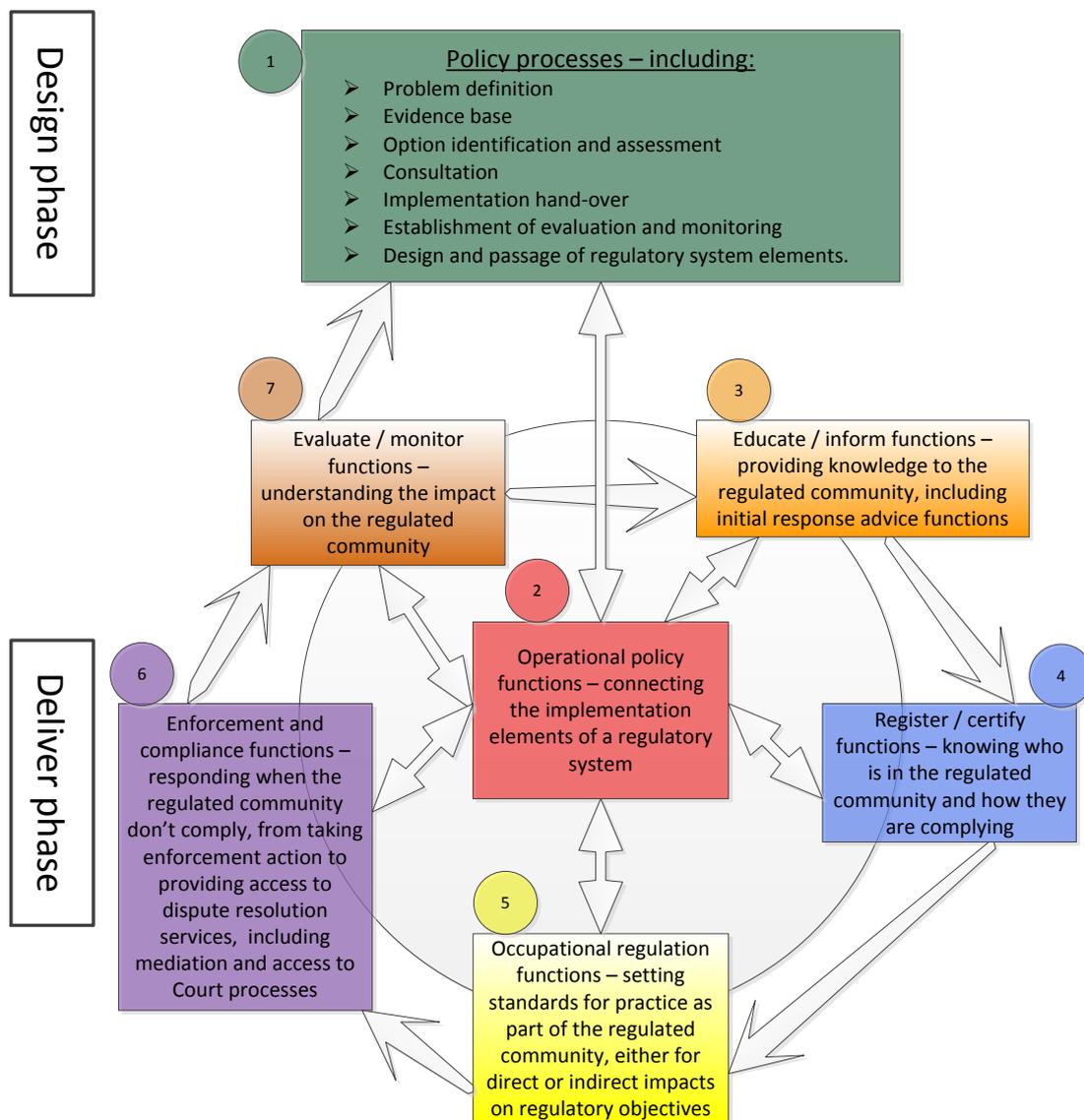
- [Report of the Government Administration Committee Inquiry into the Weathertightness of Buildings in New Zealand](#)
- [Best Practice Regulation – Setting Targets and Detecting Vulnerabilities](#) – this paper provides an ex-post assessment of whether the application of the Treasury Best Practice Principles and Performance Indicators would have detected the weaknesses in the 1991 building control regime
- [Regulating the Building Industry – A Case of Regulatory Failure](#) – this paper analyses the costs and benefits of the building control system failure
- [Weathertight Buildings and Performance-based Regulation: What Lessons can be Drawn from a Complicated and Evolving Situation?](#) – this paper provides a policy perspective on performance-based regulation in the building sector.

A subsequent review of the Building Act was carried out in 2009 – 2010. Papers relating to this review are available on the [Ministry's website](#), including [Cabinet papers](#).

Copies of the following papers are also attached:

- May, Peter J (2010) Performance-Based Regulation. Jerusalem Papers in Regulation & Governance. Working Paper No. 2, April 2010 Working Paper No. 2 April 2010. This paper provides an update of May, Peter J (2003) '*Performance-based regulation and regulatory regimes: The saga of leaky buildings.*' Law and Policy 25(4): 381–401, which was the first academic diagnostic of the building control failure.
- Mumford, P. (2011) Enhancing Performance-based regulation: lessons from New Zealand's building control system, Wellington: Institute of Policy Studies. This paper is the second academic diagnostic of the building control failure.

Attachment Two: Map of regulatory system



Note: this map does not address:

- the role of regulated parties, industry bodies and intermediaries
- overlaps between regulatory functions.

These will be essential elements in understanding how any regulatory system operates in practice.