Regulatory institutions and practices

Draft report

March 2014
The Productivity Commission aims to provide insightful, well-informed and accessible advice that leads to the best possible improvement in the wellbeing of New Zealanders. We wish to gather ideas, opinions, evidence and information to ensure that our inquiries are well-informed and relevant. The Commission is seeking submissions on the questions, findings and recommendations contained in this report by 8 May 2014.
The New Zealand Productivity Commission
Date: March 2014

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Terms of reference

IMPROVING THE DESIGN AND OPERATION OF REGULATORY REGIMES

Purpose
1. The purpose of this inquiry is to develop recommendations on how to improve the design of new regulatory regimes and make system-wide improvements to the operation of existing regulatory regimes in New Zealand. The inquiry is not a review of individual regulators, specific regulations or the objectives of regimes.

2. The aim is to improve the design and operation of regulatory regimes over time and ultimately improve regulatory outcomes.

Context
3. This Government is focused on delivering better regulation. We have improved the processes around introducing new regulation, increased our understanding of the stock of existing regulation, and conducted a number of significant regulatory reviews. There is more that can be done to improve the design and operation of regulatory regimes in light of the recent need to develop new or amended regulatory regimes and regulators to manage instances where regulation has not achieved its intended outcomes.

4. The demands on regulatory regimes are often more complex than in the past. The range of regulatory regimes, the nature of the risks involved, the expectations of the community, and the regulatory tools available to achieve regulatory objectives, are wide and varied. It is crucial that government has a good understanding across regulatory regimes of their issues, challenges, similarities and differences and how to improve their design and operation.

Scope
5. Having regard to the above purpose and context, the Commission is requested to undertake an inquiry that addresses the parameters set out below.

An overview of regulatory regimes and their regulators
6. Develop a high-level map of regulatory regimes and regulators across central government, including their organisational form.

7. Develop a set of thematic groupings which can be used to broadly categorise regulatory regimes by their objectives, roles or functions. For example core objectives might include health and safety, environmental protection, or economic efficiency.

Understanding influences and incentives on regulatory regimes
8. Outline and explain key factors which act as incentives or barriers to regulatory regimes and regulators producing the outcomes stated in legislation. For example these factors may include:

- institutional form of the regulator
- quality of the regulatory design and clarity of mandate, functions and duties
- resourcing and funding
- capability
- approach to consultation and engagement with stakeholders
- accountability mechanisms, including the ability to challenge regulatory decisions
- performance measurement and reporting
- external monitoring
- approach to risk management and innovation
9. Undertake a series of case studies to compare and contrast the approaches taken to these factors across different regulatory regimes. A key part of this analysis would be to identify strengths and weaknesses of different approaches taken to these factors to support broader insights into the design and operation of regulatory regimes.

10. This analysis should be undertaken in the context of existing guidance about good practice for the performance of different regulatory functions.

**Recommendations**

11. Develop guidance that can be used to inform the design and establishment of new regulatory regimes and regulatory institutions, and the allocation of new regulatory functions to existing institutions. The guidance should take into account other existing work in this area to avoid duplication, such as the State Services Commission’s *Reviewing the Machinery of Government*.

12. Develop system-wide recommendations on how to improve the operation of regulatory regimes over time. The recommendations may include how to both build on strengths and address weaknesses in current practices and may lead to general comments about key differences between regimes within thematic groupings. The recommendations will not be specific to particular regulations or regulators.

13. The Commission should also specifically consider how improvements can be made to the monitoring of regulator performance across central government.

14. In developing the recommendations, the Commission should take account of any key features or characteristics of New Zealand’s regulatory environment that differ from other jurisdictions. For example, these may include differences in scale, resourcing, or the need to coordinate with overseas regulatory regimes.

**Other matters**

15. The Commission should prioritise its effort by using judgement as to the degree of depth and sophistication of analysis it applies to satisfy each part of the Terms of Reference.

**Consultation requirements**

16. In undertaking this inquiry the Commission should consult with key interest groups and affected parties, including on the selection of case studies in paragraph 9 above. Consultation should include both regulators and those subject to regulation.

**Timeframe**

17. The Commission must publish a draft report and/or discussion paper(s) on the inquiry for public comment, followed by a final report, which must be submitted to each of the referring Ministers by 30 June 2014.

**Referring Ministers**
Hon Bill English, Minister of Finance
Hon John Banks, Minister for Regulatory Reform
About the draft report

This report contains the Commission’s draft guidance that can be used to inform the design and establishment of new regulatory regimes and regulators. This report also makes system-wide recommendations on how to improve the operation of regulatory regimes in New Zealand over time. The inquiry is not a review of individual regulators, specific regulations or the objectives of regimes.

This report asks questions and then gives draft findings and recommendations. The Commission welcomes information and comment on any part of this report and on any issues that participants consider relevant to the inquiry’s terms of reference.

Key inquiry dates

Submissions due on the draft report  8 May 2014
Engagement with interested parties on the draft report  March – May 2014
Final report to the Government  30 June 2014

Why you should register your interest

The Commission seeks your help in gathering ideas, opinions and information to ensure this inquiry is well informed and relevant. The Commission will keep registered participants informed as the inquiry progresses.

You can register for updates at www.productivity.govt.nz/subscribe-to-updates, or by emailing your contact details to info@productivity.govt.nz.

Why you should make a submission

Submissions provide information to the inquiry and help shape the Commission’s recommendations in the final report to the Government. Inquiry reports will quote or refer to relevant information from submissions.

How to make a submission

The due date for submissions in response to this report is 8 May 2014. Late submissions will be accepted, but lateness may limit the Commission’s ability to consider them fully.

Anyone can make a submission. Your submission may be written or in electronic or audio format. A submission may range from a short letter on one issue to a substantial response covering multiple issues. Please provide relevant facts, figures, data, examples and documents where possible to support your views. The Commission welcomes all submissions, but multiple, identical submissions will not carry more weight than the merits of your arguments. Your submission may incorporate relevant material provided to other reviews or inquiries.

Your submission should include your name and contact details and the details of any organisation you represent. The Commission will not accept submissions that, in its opinion, contain inappropriate or defamatory content.

Sending in your submission

Web: www.productivity.govt.nz/make-a-submission
Email: info@productivity.govt.nz
The Commission appreciates receiving an electronic copy of posted submissions, preferably in Microsoft Word or searchable PDF format. Please email the files to info@productivity.govt.nz.

What the Commission will do with the submissions

The Commission seeks to have as much information as possible on the public record. Submissions will become publicly available documents on the Commission’s website. This will occur shortly after receipt, unless your submission is marked “in confidence” or you wish to delay its release for a short time. Please contact the Commission before submitting “in confidence” material, as it can only accept such material under special circumstances.

Other ways you can participate

The Commission welcomes feedback about its inquiry. Please email your feedback to info@productivity.govt.nz or contact the Commission to arrange a meeting with inquiry staff.
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KEY

| Q | Questions |
| F | Findings |
| R | Recommendations |
Overview

The Government has asked the Commission to examine how the design and operation of regulatory regimes and their regulators can be improved – ultimately to improve regulatory outcomes. Specifically, the Commission has been asked to develop guidance that can be used to inform the design and establishment of new regulatory regimes and regulators. It has also been asked to develop system-wide recommendations on how to improve the operation of regulatory regimes in New Zealand over time.

Why this inquiry is important

Regulation touches the lives of New Zealanders in many ways. It is indispensable to the proper functioning of economies and societies. Regulation, when implemented well, underpins markets, protects the rights and safety of citizens, and their property, and assists the efficient and equitable delivery of public goods and services (Organisation for Economic Co-operation and Development [OECD], 2011). In this way, regulation is an important tool for preserving and advancing the public interest.

This report demonstrates that New Zealand has a large and complex regulatory sector, comprising as many as 200 regulatory regimes. More than 10,000 people work in regulatory roles. Yet there is surprisingly little information about regulation and its effects or about the wider regulatory system, and its performance (Chapter 3). This is in stark contrast to the voluminous data that is produced, disseminated and scrutinised about New Zealand’s fiscal management (taxing and spending).

There is also a question of whether New Zealand’s regulatory regimes are unnecessary complex and whether they could be simplified, recognising that capability and expertise, for regulators and regulated alike, is likely to be an ongoing issue. There are limits to how much complexity a small country like New Zealand can sustain.

There has been a growing interest in regulation in New Zealand. This interest stems from a number of important developments:

- individual freedoms and human rights have taken on greater importance in New Zealand society, as signalled by such developments as the passing of a Bill of Rights Act in 1990 and Human Rights Act in 1993;
- there has been a growing awareness of the role that good-quality regulation and institutions can play in promoting economic growth, and that bad regulation can impede productivity and growth;
- reforms over the last quarter of the twentieth century changed the way in which government organises itself, provides services and delivers policy; and
- society is much more diverse, with a broader range of attitudes to risk and expectations about what government can do.

These changes have made regulation a more visible and important government activity. They have also underlined the importance of making sure that the design of regulatory institutions and their operation achieves important public policy goals. If regulation has misplaced objectives, is used when it is not needed, or is poorly designed and executed, then it can fail to achieve policy objectives and have unintended consequences that harm the wellbeing of New Zealanders.

Regulatory failure occurs where regulations fail to improve outcomes, or even make outcomes worse, than if there had been no regulation. The two main ways regulation can fail are failures of design or failures of operation. Poorly conceived and implemented regulatory arrangements can also impose significant costs. Such costs affect business productivity and profitability, and the wealth of individuals and families. Ultimately this will harm the country’s economic performance and wellbeing.

Good regulatory design and practice can reduce the likelihood of regulatory failure. The institutional arrangements and regulatory practices that make up the architecture of regulatory regimes shape how
regulators and those regulated behave, the quality of decision making, and ultimately the success of regulatory regimes in achieving the desired outcomes. Indeed, developments in the theoretical literature point to a move “towards a growing emphasis on institutional design and a coupling of this with a more detailed differentiation of motivations and behaviours as these are encountered in the body of politicians, regulators, and the regulated that makes up the regulation community” (Baldwin, Cave & Lodge, 2012, p. 11).

This inquiry seeks to better understand what regulatory institutions and practices look like in New Zealand and how they can be improved. The inquiry examines:

- which organisational forms are best suited to particular circumstances;
- the appropriate level of independence;
- how regulators are governed, held to account, make decisions, engage with industry and the public, and carry out their regulatory practices;
- how regulators are resourced; and
- how regulators develop the capability needed to regulate efficiently and effectively.

Getting these right not only means the objectives of regulation will more likely be achieved but, importantly, it builds legitimacy and trust in the regulator and regulatory regime and, with that, a higher level of trust by society.

Key features of New Zealand regulation

Regulation is the product of an interaction between a number of actors within and outside of government, and can best be thought of as a system. To develop proposals for improving regulation, it is important to understand the features that affect the regulatory system. These features can include constitutional arrangements, history, cultural practices and expectations, geography, levels of national wealth and economic structures. Five main features have a significant impact on how regulation is made and implemented in New Zealand:

- a centralised and statute-driven system, with comparatively few checks and balances;
- resource constraints, driven by New Zealand’s small population, distance and relatively low incomes;
- a weak review and evaluation culture;
- the acknowledgement of Māori interests in regulation; and
- the increasing role of international regulatory standards.

These features lead to some system-wide themes in how regulation is developed and implemented in New Zealand:

- A number of important regulatory regimes in New Zealand are young and are still settling down. Electricity and telecommunications are the most prominent examples. This has created perceptions of risk and instability.
- Regulatory regimes in New Zealand can easily become rigid and obsolete. This reflects the strongly statute-driven system in New Zealand and the weakness of review and evaluation systems. As a result, New Zealand regulation can struggle to keep up with changes in technology or public expectations.
- New Zealand has applied different regulatory models across similar issues, rather than applying a coherent and consistent approach. This increases compliance costs on firms operating across multiple regimes, and limits the ability of regulators to learn from each other’s experiences.
Although official recognition of Māori interests in regulation has increased since the 1980s, questions remain over how best to recognise Māori interests and Treaty of Waitangi principles, and mechanisms for ensuring effective participation by Māori in the implementation of regulation are still developing.

New Zealand is notable for having regulatory systems that score highly on numerous international measures of quality, while also being the subject of criticism for instability and inconsistency (Chapter 2).

Better understanding New Zealand’s regulatory system

The Commission has found that the lack of regular and detailed reporting about the state of New Zealand regulators and regulation is a key gap in the current regulatory management system. More comprehensive and comparable information about New Zealand regulators should be collected to help offset barriers to identifying and making systemic improvements to regulatory practice. In particular, such information could:

- help designers of regulation compare and contrast regulatory approaches and features;
- help regulators identify better practice among their peers that they might adopt in their own operations;
- be used to identify trends or patterns in implementing regulation or in the performance of regulators; and
- improve knowledge about the scale and scope of regulatory activity in New Zealand and enable more informed debate about regulatory matters.

Standardised reporting requirements should be designed to allow analysis of the structure, scope, efficiency, effectiveness, and responsiveness of regulators, as well as of the burden that regulation imposes on regulated parties. More transparency would increase the accountability of New Zealand regulators. Chapter 3 provides an indicative suite of reporting information – feedback is sought on the type of information that regulators should be required to report.

Standardised reporting on regulatory activity and impacts should be embedded into existing accountability processes, such as agency annual reports. The Treasury and the State Services Commission (SSC), as the central agencies responsible for the public sector accountability framework, should develop standardised reporting requirements for annual reports.

Information from standardised reporting could be formally integrated into the Treasury’s regulatory management systems. In particular, it could be used to identify any parts of the regulatory system that need improving, and underpin strategies to make those improvements across the system.

Improving regulatory institutions and practices

The report examines the design features listed in Figure 0.1. Separate chapters consider each feature to determine how they can improve the capability of regulators to make sound decisions that maintain and advance the public interest.

These design features are interconnected, and in a well-designed system will be mutually reinforcing. For example, if roles are clearly defined, this will make it easier for regulators to develop effective cultures and regulatory practice. Likewise, the level of regulatory independence will determine the accountability, performance and monitoring framework that is most appropriate.
Role clarity

Clear regulatory roles and objectives are critical to regulator accountability and focus, compliance by regulated firms, predictable decisions and enforcement, and the legitimacy of the regime. Regulatory regimes with clear objectives are more likely to enjoy high levels of compliance and credibility, and regulators with clear and well-understood roles can more easily be held to account (Chapter 4). But achieving “clarity” is not a simple or straightforward task due to the complex issues regulation often deals with, the multiple stakeholders in any regulatory regime, and the large amount of existing regulation.

Manifestations of poor role clarity include: the expansion of regulatory scope beyond its original mandate; duplicated or contradictory regimes; gaps in regulation, monitoring or enforcement; or inconsistent enforcement. Most businesses that the Commission surveyed found contradictory or incompatible regimes and regulators poorly managing duplicated compliance requirements.

Regulatory regimes may lack clarity because:

- the regulatory standards used (outcome-, principle-, process- or input-based) do not fit the industry or activity being controlled;
- policymakers give insufficient guidance about the desired objectives;
- regulators have functions that create conflicts of interest; and
- little attention was paid (when designing the regulatory regime) to the role of other regulators or the interaction of different regimes on regulated firms.
Actions that can improve the clarity of regulator roles, functions and objectives include:

- ensuring that the regulatory standard used is appropriate;
- applying greater discipline on those who design regulatory regimes;
- avoiding perverse incentives when allocating regulatory functions to agencies; and
- establishing processes to minimise or resolve problems arising from overlapping regimes.

Issues to be considered in selecting the right regulatory standard are the level of harm that would arise from non-compliance, capability levels in the regulator and the regulated industry, and the levels of trust between the industry and regulator.

If a range of capability levels exists within a regulated industry, “deemed-to-comply” models can help to provide flexibility for more capable firms and certainty for less capable organisations. Deemed-to-comply models allow more capable firms to develop their own compliance strategies, while also providing detailed guidance for other firms on how to comply.

Legislative frameworks that minimise the number of objectives and conflicts and provide a clear hierarchy of objectives help to support consistent and predictable decision making by regulators.

**Regulatory independence and institutional form**

The institutional form of regulators, and the degree of independence with which they are expected to undertake their regulatory functions, are key considerations for designers of regulatory regimes.

There is widespread agreement of the desirability of independent regulators. Independence is multi-faceted and is significantly more than formal legal designation.

Independence supports regulators adopting effective regulatory strategies. It does this because independent regulators generally have more information and are better able to appraise risks than the media or the public. Designers of regulatory regimes need to carefully appraise the arguments for and against regulator independence. Arguments for political control need to be weighed carefully against the benefits of providing a credible long-term commitment to an impartial and stable regulatory environment.

For most regulatory regimes, the arguments for providing more independent regulation will be stronger than the arguments for less independent regulation. It will usually be appropriate for regulatory powers to be exercised independently of political control so they are not used for partisan purposes.

Regulators often have to work with legislation that is outdated or not fit-for-purpose. Their independence could be enhanced by:

- ensuring greater consistency in the allocation of legislative material between primary legislation and types of secondary legislation;
- looking for opportunities to delegate more rule-making to regulators, particularly in areas with rapid technological change.

If rule-making power is to be further delegated, checks on regulators will need to be strengthened. One key check is the Regulations Review Committee of Parliament, which reviews regulations and can recommend their cancellation, if they are unfair, unusual or onerous. However, this cancellation power is seldom used. The Commission considers that the Committee should play a more active role, and makes some recommendations about what that role should include. The Commission is also seeking public comment on how the Committee’s place in the regulatory system could be further strengthened.

Political imperatives will inevitably diverge sometimes from those of independent regulators. While political interference in independent regulatory regimes is undesirable, providing transparent mechanisms for political intervention is preferable to undertaking more fundamental regulatory reform to solve political
imperatives. Providing such mechanisms can actually enhance the independence of regulators. This also allows ministers to be properly held to account for their actions.

Choices about institutional form are in practice more important for what they signal about expected independence, rather than the legal constraints and freedoms associated with particular agency forms. As such, careful attention must be paid to establishing clear expectations, norms and cultures in new independent regulators.

Government has signalled an intention to consider reallocating some functions currently undertaken by Crown entities (which are operationally independent) into a new type of institutional form known as departmental agencies. The Commission has a number of concerns with this proposed new institutional arrangement for regulators (Chapter 5).

Regardless of the advantages or disadvantages of particular institutional forms, the disruptive effect of institutional change on the smooth operation of regulatory functions must be acknowledged. During periods of institutional change, leaders need to have clear strategies for ensuring regulatory functions continue to operate effectively.

**Governance, decision rights and discretion**

The internal governance of a regulator (the systems of direction and control), where decision rights sit within the organisational structure (who makes decisions and how they are made), and the discretion available to the regulator in making decisions, all affect the quality of decision making and the achievement of regulatory objectives (Chapter 6). Selection of governance structures in regulatory agencies appears in some cases to be ad hoc.

There is evidence of some confusion around the role that some members of Crown entity boards are expected to play. Individuals with expertise in the regulated industries can make a valuable contribution to regulator governance. However, updated guidance and induction material for members of Crown entity boards should make clear that members are not appointed to act as the representative or agent of any external group, and that good practice for managing conflicts of interest apply.

In most cases multi-member decision-making bodies will offer advantages, including the incorporation of different perspectives, better balancing of judgement, and reducing the likelihood of maverick judgments or capture. However:

- regulatory decisions may appropriately be vested in ministers where they involve significant value judgements not amenable to analysis, or have significant fiscal implications;
- day-to-day administrative decisions may be appropriately taken by individual officials (and internal review of these decisions can be a useful quality check).

In any system of authority there is tension between certainty and flexibility: between having definite rules and applying them consistently and even-handedly, and enabling decisions to be made according to the specific circumstances of the case and within a broader framework of goals and values.

The exercise of discretion is constrained by legal and non-legal methods of control, including judicial review and the common law principles of administrative law, cultural and institutional constraints, and transparency.

**Regulatory culture and leadership**

Organisational culture affects the way that regulatory agencies carry out their functions and is therefore important to regulatory success. Regulator culture refers to the shared norms, values and beliefs that influence the behaviour of the agency staff. These norms, values and beliefs are heavily influenced by:

- the beliefs, values and assumptions of the *founding leaders* of the organisation;
- the *learning experiences* of staff in the performance of their duties; and
- new beliefs, values, and assumptions brought in by *new staff, particularly new leaders*.
It is important to distinguish the impact of culture from the numerous other factors that motivate regulator behaviour. It is often too easy to attribute organisational dysfunction to “culture” issues rather than wider regulatory practices, structures and institutional issues.

Box 0.1  Inquiry participants’ views on what constitutes a good regulatory culture
Submissions to the inquiry suggested that effective cultures:

- embrace the regulator’s role as an educator and facilitator of compliance, as opposed to an enforcer of rules;
- encourage internal debate and robust, evidence-based decision making;
- behave with a high degree of individual accountability;
- encourage the exchange of information in an environment of trust; and
- appropriately match the interface with regulated parties to the type of regulation being implemented.

While generic conclusions are difficult, the Commission’s analysis suggests the following.

- There is evidence of risk-averse cultures within New Zealand regulators. This may be appropriate for achieving the regulator’s statutory objectives or, alternatively, may have emerged to protect the reputation of the regulatory body.
- Previous restructuring of regulatory organisations has required significant cultural shifts. The new culture has often been pivotal to the success of any structural changes.
- Stakeholders often perceive the quality of engagement as a “window” to the culture of a regulator. In making this connection, it is important to assess whether the regulator’s approach to engagement is driven by its values and beliefs, or whether it is driven by some other factor – such as the legislative environment or available resources.
- A common understanding of the purpose and mission of a regulatory body is the first step in developing culture. While the Commission’s survey suggests that chief executives believe corporate culture influences the behaviour of front-line staff, other survey evidence indicates that central government regulatory workers in New Zealand do not perceive that top managers communicate a clear organisational mission.

The culture of a new regulatory body can be shaped in a number of ways.

- Government can seed a “desirable” culture by appointing founding leaders with values, beliefs and experiences compatible with those it believes are most conducive to achieving the desired regulatory outcomes. Selecting the “right people” does not guarantee that the “right” culture will emerge, but the actions of founding leaders are key to embedding culture.
- Monitoring bodies and central agencies can use formal and informal mechanisms to reinforce favourable cultures in new regulatory bodies.

While legislation can codify certain actions (such as consultation), it does not guarantee that a regulatory body will develop deeply held values around the importance of the behaviours. The culture of the organisation will evolve as its members discover what works and what doesn’t work.

Effective consultation and engagement

When implementing regulation, effective engagement can help to reassure stakeholders and the wider community that good regulatory process is being followed, and that the decisions of regulators are robust, well-informed and well-reasoned. This promotes confidence that the decisions of regulators are in the
public interest and that they are evidence-based and impartial. This in turn helps build trust in the regulatory system and in the regulator. It also helps strengthen the legitimacy of the regime and improve the durability of regulator decisions.

Conversely, insufficient engagement can weaken community confidence and trust in both the regulatory regime and the regulator’s ability to deliver sound decisions. Low community confidence can undermine the objectives of regulation by deterring compliance or making the decisions of regulators more likely to be challenged.

The choice of engagement mechanism is influenced by the goal of the interaction, and by the relative efficiency of alternative engagement mechanisms. Goals can range from merely informing stakeholders of their regulatory obligations, to involving them in regulatory decisions, to empowering them to make decisions. The strengths and weaknesses of different strategies are examined in Chapter 8.

In general, the greater the level of public participation, the more critical it becomes to ensure a common understanding of the goals of the engagement process. Failure to do so can result in unrealistic expectations around how much participants can affect the decisions of regulators.

When designing a regulatory regime, a key consideration is whether engagement strategies should be left to the discretion of the regulator, or whether statutory provisions are required to promote regulatory objectives of Parliament or protect fundamental principles of natural justice. (Notably, of the more than 50 statutes that the Commission examined, over half contain some form of statutory consultation requirement). This decision should be made in the context of other features of the regulatory regime – particularly the extent of discretionary powers assigned to the regulator, the level of regulator independence, and the strength of accountability mechanisms. The issues to consider when contemplating statutory obligations to consult are set out in Chapter 8.

Inquiry participants have raised concerns around the current engagement practices of some New Zealand regulators. These include insufficient time for engagement, a perception that regulators enter engagement processes with predetermined views, and concerns that some regulators lack the capacity to engage affectively. The Commission has also heard positive feedback around the approaches adopted by some regulators – notably the New Zealand Transport Agency and the Environmental Protection Authority (EPA).

Inquiry participants also advocated more extensive use of advisory groups and greater involvement of consumers in decision making (that is, through mechanisms such as “constructive engagement” and “negotiated settlements”). Such approaches change the very nature of the regulatory decision-making process and the role of the regulator, and are not without drawbacks. These include that stakeholders can lack the expertise, resources or time to effectively engage in technical decisions, it can be hard to ensure that the views of the broader community are represented, and it can generate unrealistic expectations around the extent to which stakeholders can affect the decisions of regulators.

**Regulation and the Treaty of Waitangi**

The continuing evolution of the relationship between the Treaty partners, and how the principles of the Treaty are interpreted by the courts, can generate considerable uncertainty for those applying Treaty principles in regulatory regimes where Māori have an interest and where the Crown has a duty of active protection.

References to the principles of the Treaty of Waitangi can be found in statutes where Māori have a relationship with the land, water, important sites, wāhi tapu and other taonga. However, “other taonga” can also encompass te reo, health and history. Most of these statutes contain regulatory provisions and create obligations on a range of parties that are not the Crown.

The inclusion of Treaty clauses can be seen as an insurance policy for both Māori and the Crown. A Treaty clause is a legal acknowledgement of Māori interests and rights, and provides a clearer definition of the Crown’s responsibility with respect to those rights (to the extent that the absence of a specific clause might be interpreted more broadly).
Chapter 9 sets out important factors that officials should consider when recommending the inclusion of Treaty clauses in statutes that establish regulatory regimes or regulatory agencies. There is a question as to whether an overarching approach to Treaty principles in legislation would be preferable to the current “case-by-case” approach to the inclusion of Treaty clauses in legislation, with specific Treaty clauses in individual statutes where more guidance is required on how the Treaty principles are to be applied. The question for this inquiry is whether a different approach would improve the quality of regulation.

Excellence in regulatory practice cannot be legislated for. Good practice in upholding Treaty principles of partnership, mutual respect and good faith depends on senior leadership, good internal policies and processes, and guidance for regulatory staff and stakeholders.

The Commission has reviewed 10 examples of guidance from government agencies about how to apply Treaty principles. The overall quality of existing guidance material can be improved. The assessment framework used in reviewing the guidance material could be used as a tool to help regulatory agencies develop their own guidance about the application of Treaty principles.

Sharing good regulatory practice is one way to raise the standard of practice among regulators. Lessons from the experience of the EPA are identified that other regulators can adopt to improve their regulatory practice with respect to the principles of the Treaty of Waitangi. An important lesson for other regulators is that the investment in developing trust through good relationships can pay off in reduced costs and better regulatory decision making.

**Decision review**

In New Zealand, the courts have a constitutionally important role to supervise the Executive’s actions, ensuring that the Executive acts reasonably, fairly, and within the bounds of the laws established by Parliament. Unlike in other countries, New Zealand courts have no role in supervising Parliament. Courts have no ability to strike down or invalidate legislation passed by Parliament.

Judicial scrutiny of the exercise of Executive power is particularly important in the area of regulation, given the coercive nature of those powers. Where Parliament provides for appeals, courts also provide a forum for parties to test that regulators have made “correct” decisions.

Appeals of regulatory decisions involve the courts scrutinising the merits and correctness of those decisions. Judicial review involves the courts scrutinising the process and legality of decision making. These are distinct processes. “Merits reviews” are appeals that look at the correctness of a decision.

Appeal rights of administrative decisions exist only where Parliament expressly provides for them. There is a perception that New Zealand statutes provide limited access to appeal of regulatory decisions, but this is not supported by research undertaken by the Commission. Most regulatory regimes provide for appeals, and only a small minority of regimes provide limited or no access to appeals.

Judicial review is an inherent power of the High Court, and so does not need to be provided for in statute. The Commission has found no evidence that judicial review is ineffective in ensuring the lawfulness and reasonableness of the Executive’s actions. Attempts in legislation to exclude judicial review of the Executive are wholly undesirable.

The breadth of judicial review and appeals can vary widely in New Zealand, but in practice significant overlap exists between judicial review and appeal. In New Zealand the scope of judicial review is comparatively broad and can sometimes include scrutinising the substantive merits of the Executive’s decisions.

The overlap between judicial review and appeal means that judicial review already adequately provides many of the advantages that submitters to the inquiry ascribed to merits review or appeals. This includes sharpening the incentives on decision makers to come to the correct decisions.

Appeal rights should be provided where the designers of regimes are confident the appeals will improve regulatory outcomes and support the objectives of the regulatory regime. This requires taking into account the costs and uncertainty that appeal rights create.
In deciding whether to provide for appeal rights of complex or highly technical regulatory regimes, designers need to critically assess the institutional capability and expertise of the court or tribunal reviewing the decision, relative to the decision maker at first instance.

A range of mechanisms is available that may support the institutional capability of the court or tribunal reviewing the decision to deal with appeals of complex and highly technical decisions. Two mechanisms are using technical experts as lay judges and providing for more inquisitorial processes.

The Legislation Advisory Committee (LAC) guidelines on review and appeal provide a good list of considerations to take into account when designing review and appeal provisions in regulatory regimes. The LAC notes that appeals:

- scrutinise and correct individual decisions, with the aim of providing redress; and
- maintain a high standard of public administration and public confidence in the legal system.

Even so, the LAC notes that the value of appeals must be balanced against the considerations of cost, delay, significance of the subject matter, competence and expertise of the decision maker at first instance, and the need for finality. It is unclear how much the LAC guidelines influence decisions about provision of appeals in the design or review of regulatory regimes.

**Regulatory practice**

A central concern in the design of a regulatory regime is ensuring its effective implementation and administration, so that the intent of the regime is met. However, the approach taken to monitoring, enforcement and operational compliance activity is typically left to the expert discretion of the regulator. Successful implementation of regulatory regimes will depend on the strategies, tools and methods regulators deploy.

Regulators around the world, including in New Zealand, have drawn heavily on theory in designing compliance and enforcement strategies, tools and methods. In particular, regulators have tended to adopt:

- Responsive regulation approaches, in which regulators select their compliance tool based on the attitude of regulated firms towards compliance. For firms that are willing to do the right thing, the regulator may select a low-cost tool (such as education); for firms that are unwilling to comply, the regulator may select high-powered tools (such as prosecutions).

- Risk-based approaches, in which regulators focus on identifying and assessing the risk of harm from non-compliance and target their resources towards reducing the greatest harms.

In practice, implementation of either approach has involved considerable challenges, for example:

- regulators can face barriers to using high-powered tools, such as prosecutions; and

- a risk-based approach does not necessarily solve the issue of what risks to prioritise, how to deploy regulator resources, or what enforcement tool to use.

Both risk-based and responsive approaches are evident in New Zealand regulator strategies, although agencies differ in the extent to which they prioritise reducing harm or maximising compliance, and the extent to which the two objectives are integrated or treated separately.

Regulatory scholars Robert Baldwin and Julia Black have developed the concept of *really responsive regulation* – a more nuanced institutional approach to regulatory practice and compliance, which sees regulators being attentive and responsive to a broad range of factors in undertaking their regulatory practices.

There is evidence that some New Zealand regulators are demonstrating elements of the really responsive approach. However, evidence also suggests that New Zealand regulators are not paying enough attention to how their regimes perform over time.
Regulating is a deeply challenging task. For regulatory practice in New Zealand to be more effective, and consistently effective, regulators will need to share experience and practice more. Also, more detailed and targeted guidance about regulatory practice is needed. Formal recognition of regulator forums or networks could offset barriers to knowledge sharing through:

- partial government funding of regulator networks, tied to a business case and performance measures;
- the Cabinet’s Expectations for Regulatory Stewardship being revised to clarify that regulators should seek to raise their own, and the wider sector’s, performance by sharing experience; and
- active monitoring by the Treasury and portfolio departments (of Crown entities) of regulator participation in communities of practice.

**Workforce capability**

Regulators need staff who as a group combine generic and specific competencies, including specific technical expertise, personal competencies such as communication skills, and an understanding of the compliance role and the role of the regulator. As the Ministry of Transport notes, “having an amalgam of very different skill sets can be what matters for regulatory success” (sub, 39. p. 6).

Gaps in these competencies can undermine the credibility of regulation and the achievement of regulatory outcomes. The precise mix of competencies needed is likely to vary between regulators and even within a regulator at different times. It is management’s responsibility to identify the required mix and to develop strategies and programmes to deliver it.

It is estimated that more than 10,000 people are employed in regulatory roles in New Zealand. There is limited data about their competencies and any gaps in those competencies.

That said, the Commission’s survey of business revealed the business perception of the competency of regulators. Only 23% of the firms surveyed agreed or strongly agreed with the proposition that “regulatory staff are skilled and knowledgeable” and only 25% agreed or strongly agreed that “regulators understand the issues facing your organisation”.

The situation was more encouraging regarding communication by regulators. In the last two years, 40% of the businesses surveyed spent significant time and resources on finding out about regulatory requirements and 25% applied for consents and approvals. Of those surveyed, 43% said that interactions with regulatory compliance officers were friendly and non-combative, and 37% agreed with the statement that “regulators communicated well with your organisation”.

People who work in regulatory agencies and their chief executives seem to have different views about the adequacy of staff competencies and training. The Commission’s survey of 23 chief executives found that only 5 agreed with the statement that there are “significant capability or skill gaps among regulatory staff”, while 10 disagreed with the statement, and 7 neither agreed nor disagreed and 1 did not know. However, the Victoria University of Wellington survey of Public Service Association workers found that, compared with local government and district health board regulatory workers, and non-regulatory workers in central government, central government regulatory workers tend to:

- disagree that they are given a real opportunity to improve their skills through training;
- be less likely to perceive that they have sufficient job-related training;
- show lower levels of agreement that their supervisors have helped them get extra job-related training or that they receive ongoing training that helps them do their jobs better;
- be less satisfied with the number and quality of training and development programmes available; and
- disagree that training and educational activities enable them to do their jobs more effectively.

Chapter 12 sets out a number of recommendations that are intended to build on the process of change already underway in developing the capability of the regulatory workforce in New Zealand. These
recommendations are designed to reinforce capability development as a core management responsibility, promote clarity about the roles of those seeking to improve workforce capability, and put greater focus on workforce capability in reviews of regulator performance.

The recommendation and improvements already underway will contribute to the achievement of better regulatory outcomes through:

- a compliance sector that is focused on competency development;
- a well-respected national qualifications framework for regulatory work;
- an effective process for improving the competencies of the existing workforce and for training new people to be effective regulators;
- greater workforce mobility between regulators; and
- more effective collaboration between regulators in relation to competency development.

**Funding regulation**

Regulators can be funded from various sources, including Crown contributions, levies on the regulated industry, or through fees imposed either on the beneficiaries of regulation or on those who cause the “problem” that needs to be regulated. The way that regulators are funded can affect the efficiency of resource use, equity and the achievement of policy outcomes.

Many countries, including New Zealand, have established frameworks whose purpose is to help those designing and implementing regulation to select the appropriate sources of funds. While in principle there can be benefits from regulators recovering some costs through fees or levies, case-by-case assessment is required to secure these benefits in practice. The framework for choosing between sources of funding needs to encourage this to happen.

The Commission’s analysis suggests that while there is no major problem with the approach to funding regulators in New Zealand, and indeed New Zealand’s framework for funding regulators has many positive features, there are opportunities to improve it – which would equally apply to new and existing regulators.

In principle, recovering some costs of regulation through fees is beneficial, but poor implementation can undermine the benefits. The Commission’s survey of businesses and submissions to the inquiry both reveal concern in the business community about the quality of the consultation before regulatory fees or levies are introduced, weak constraints on the level of charges, and the structure of charges. Other jurisdictions use a variety of approaches to reduce these risks.

Chapter 13 examines what lessons can be learned from the approach to cost recovery used by other jurisdictions. There are examples in other jurisdictions of:

- more rigorous consultation and impact assessment before fees are introduced;
- more detailed advice about how to implement cost recovery;
- stricter requirements for performance standards and reporting against those standards; and
- penalties for failure to achieve the standards.

There is scope to improve New Zealand’s approach to cost recovery – to both new and existing regulators – through strengthening the governance and accountability framework (Box 0.2).

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**Box 0.2 Potential improvements in costs recovery framework**

Improvements in New Zealand’s approach to cost recovery can be made through strengthening the governance and accountability framework. In particular:
Accountability and performance

Processes for holding regulators to account for their behaviour help ensure that agencies act efficiently, effectively and lawfully, and can create incentives for regulators to improve their performance.

Existing accountability processes provide multiple avenues to interrogate and challenge regulators about their behaviour, and a range of levers that ministers can pull to influence this behaviour. To influence a regulator in a timely and appropriate fashion, ministers must have a sound understanding of how well the regulatory organisation is performing.

Monitors of regulators have a key role to play in ensuring ministers are well informed about performance and risk levels. Where regulators are Crown entities, the relevant portfolio department acts as monitor. Where the regulator is a department, central agencies (The Treasury and the SSC) have monitoring functions. Effective monitors need good overall sector knowledge, so that they can understand the regulator’s operating environment and be independently aware of emerging issues and risks.

Monitoring is both a key link, and the weakest link, in the current accountability system. Some departments appear not to fully understand their monitoring roles and responsibilities, monitoring is not having enough effect on regulatory quality, and incentives on departments to monitor well are not strong enough. The Treasury and SSC are not perceived by regulators’ chief executives as playing a significant role in holding agencies to account for their regulatory functions.

Feedback from submitters also suggests that the accountability system may not be giving confidence to regulated parties and the public that regulators are acting lawfully, reasonably, proportionately and effectively.

Performance expectations for monitoring regulators are either too low or unclear, and incentives for effective monitoring could be strengthened. The Commission recommends that:

- more detailed and demanding guidance be prepared for departments and ministers on how to monitor Crown entities;
- the Treasury and the SSC work with departments to develop performance measures that better, and more consistently, reflect good practice in monitoring;
- departments develop and maintain explicit statements of their monitoring roles and responsibilities – in doing so, they should regularly review whether their monitoring approaches are giving ministers sufficient assurance that harm and risks are being effectively managed, permitting accurate performance
assessments, and promoting substantive dialogue with regulators about the fitness-for-purpose of their regimes; and

- the SSC and the Treasury play a more active oversight role for departmental regulators and more tightly integrate their new tools to assess regulatory stewardship performance into existing accountability processes, especially the performance reviews.

System-wide review

New Zealand has a large stock of legislation and regulation that is growing rapidly. Determining whether this stock of legislation and regulation is achieving the outcomes for which it was enacted, and is producing benefits that outweigh the costs, requires a process for evaluation. As the OECD notes, “one of the most important tasks facing governments today is updating of the accumulated regulations and formalities that have gone unexamined over years or decades. National regulatory systems require periodic maintenance. Periodic and systematic review of existing regulations is needed to ensure that outcomes are assessed, unneeded or inefficient rules are weeded out, and needed rules are adapted to new economic and social conditions” (OECD, 1997, p. 224).

The New Zealand Government is implementing a suite of initiatives to improve the management of this stock. It does not use many of the approaches to system-wide evaluation of regulatory regimes that are used in other countries, some of which have been identified as involving low effort and potentially high return in other countries.

To improve the effectiveness of these initiatives, the Government should:

- articulate in more detail its strategy for improving the management of the stock of legislation and regulation, indicating how the initiatives it is implementing fit within the strategy and how success will be measured;
- help departments satisfy the Cabinet’s expectations of the responsibilities of departments for keeping current the regulatory regimes that they are responsible for through improved reporting and transparency; and
- require departments to explain their plans for monitoring, evaluation and review in their papers for the Cabinet Legislation Committee and amend the Cabinet Guide to build in this requirement (their plans should be proportional to the significance of the regulation).

Implementation of the Government’s initiatives for keeping the stock of legislation and regulation current should be guided by principles, building an approach that:

- ensures that the scale and scope of evaluations is proportionate to the impacts of regulation;
- provides transparent reporting of the Government’s strategy, work programme and progress in achieving performance targets;
- clearly defines responsibility for managing the stock of legislation and regulation;
- is based on consultation with those affected by regulation;
- is driven by a need to prioritise effort where the payoff is expected to be largest; and
- is adequately resourced, so that people with the capabilities required to undertake effective evaluations can implement it.

Making it happen

The regulatory management system is a large and important part of New Zealand’s policy infrastructure. It should be seen as no less significant than the systems behind taxation and government spending. This report has reviewed the components of the system and has found system-wide deficiencies in each of them. New Zealand’s system cannot be described as broken, but it is “muddling through”. There is no
government strategy for regulation, no clear programme for its improvement, and no clear “owner” of the system. There is considerable scope to get more, and much better, performance out of the system, with significant benefits for the New Zealand economy and the wellbeing of New Zealanders.

To move the regulatory management system to the next level of performance:

- energetic and focused leadership is required from within the Cabinet, based on the premise that the regulatory management system is a key part of New Zealand’s policy infrastructure, combined with more transparent processes from both ministers and agencies;

- effort to improve the system must be focused not only on the front-end of regulation (the decision-making process), but also on organisational design, implementation, monitoring and review;

- regulators need stronger encouragement and support to fulfil their stewardship obligations. The system needs to rely less on goodwill and the sense of professional duty and more on exposing Boards and chief executives to performance expectations and incentives commensurate with the Government’s stated objectives;

- departmental monitors of regulators need a better understanding of their role, and the importance attached to the monitoring role needs to be increased; and

- agencies with key roles in ensuring the regulatory management system functions well need to be funded adequately.

Having a minister responsible for the regulatory management system is essential. The minister’s responsibilities should include:

- defining the overall objective of the regulatory management system and bringing focus and attention to it;

- strategic prioritisation of effort across the regulatory system;

- specifying and allocating tasks for improving the system; and

- promoting continuous improvement in regulatory design and practice.

The minister needs to be supported by a well-resourced and capable advisory support team. Currently this is located in the Treasury, but the Commission intends to examine other options in more detail in the final report.

Conclusion

This draft report provides guidance that will assist in designing new regulatory regimes and in improving the operation of existing regimes. Attention is focused on the role and contribution of the system to the wellbeing of New Zealanders and ways to encourage a more strategic approach to initiatives aimed at improving it. This means:

- sharpening the accountabilities of those who have important roles to perform in improving the system;

- redirecting effort to improve the system to where it can yield the highest dividends;

- increasing the attention devoted to improving organisational and workforce capability; and

- building mechanisms to encourage continuous improvement (“periodic maintenance”) of the system, to keep it current.

New Zealand is not so well off that it can afford to settle for second best in its foundational systems. Indeed, given the disadvantages of small scale and isolation, it needs to excel in such matters if it is to meet its aspiration to deliver first-class living standards to all New Zealanders. Achieving this will require focus, enthusiasm, capability and strong political support.
1 About this inquiry

Key points

- Regulation is indispensable to the proper functioning of economies and societies. It underpins markets, protects the rights and safety of citizens, and their property, and ensures the efficient and equitable delivery of public goods and services. In this way, regulation is an important tool for preserving and advancing the public interest.

- However, if regulation has misplaced objectives, is used when it is not needed, or is poorly designed and executed, then it can fail to achieve worthy policy objectives and have unintended consequences that harm the wellbeing of New Zealanders.

- Regulatory failure occurs where regulations fail to make outcomes better, or even make outcomes worse, than if there had been no regulation. The two main ways regulation can fail are failures of design and failures of operation.

- The Government has asked the Commission to examine how the design and operation of regulatory regimes and their regulators can be improved – ultimately to improve regulatory outcomes. Specifically, the Commission is asked to develop:
  - guidance that can be used to inform the design and establishment of new regulatory regimes and regulators; and
  - system-wide recommendations on how to improve the operation of regulatory regimes in New Zealand over time.

- Regulation has become an increasingly prominent tool for protecting the public and improving the performance of markets. The growing use of regulation as a way of achieving social and economic objectives poses a number of challenges in terms of complexity, accountability, accessibility and fairness. Good design of regulatory institutions and practices can help overcome these challenges.

- This inquiry is focused on better understanding what good regulatory institutions and regulatory practice look like in the New Zealand context and on ways to improve them. This focus goes to critical issues about what organisational form is best, the appropriate level of independence, how the regulator is governed, is held to account, makes decisions, engages with industry and the public, carries out its regulatory practices and, finally, how the regulator is resourced with the right workforce capability to deliver on its mandate.

- Getting these issues right not only makes it more likely that the objectives of regulation will be achieved but, importantly, it builds legitimacy and trust in the regulator and regulatory regime and, with that, a higher level of trust by society.

1.1 What the Commission has been asked to do?

The Government has asked the Commission to examine how the design and operation of regulatory regimes and their regulators can be improved – ultimately to improve regulatory outcomes.

What this inquiry will include

The Commission has been asked to provide:

- a “high-level map” of regulatory regimes and regulators across central government, and a typology of how regimes and regulators might be classified or distinguished;
• guidance to inform the design and establishment of new regulatory regimes and regulators; and
• system-wide recommendations on how to improve the operation of regulatory regimes over time.

In addition, the Commission has been asked to give particular attention to:

• any key features or characteristics of New Zealand’s regulatory environment that differ from other jurisdictions (for example, differences in scale, resourcing, or the need to coordinate with overseas regulatory regimes);
• ways to improve the monitoring of regulator performance across central government; and
• other existing work in this area to avoid duplication, such as the State Services Commission’s Reviewing the Machinery of Government.

See page iii for the full terms of reference.

What this inquiry will not include

The inquiry is not:

• a review of individual regulators, specific regulations or the objectives of regimes (this was explicitly excluded from the inquiry’s scope by the Terms of Reference given to the Commission); and
• about improving the policy-making process for developing new regulation or regulators, a topic of some focus by ministers and officials, with less attention given to other factors that contribute to regulatory success, such as regulatory institutions and practices.

The Commission has already commented on the policy-making process for formulating new regulation in its report *Towards better local regulation* (NZPC, 2013a).

What regulation is in scope

Various definitions of regulation exist, each displaying varying degrees of specificity and breadth. Black (2002) offers three definitions from the literature, each involving the exercise of some authority to affect behaviour. Regulation is:

• the promulgation of rules by government accompanied by mechanisms for monitoring and enforcement, usually assumed to be performed through a specialist public agency;
• any form of direct state intervention in the economy, whatever form that intervention might take; or
• all mechanisms of social control or influence affecting all aspects of behaviour from whatever source, whether those mechanisms are intentional or not.

The first definition best aligns with the scope of this inquiry. The Commission has focused on regulation that is implemented where the operation of markets fails to produce behaviour or outcomes that are aligned with the public interest. Traditional market failure rationales for regulating arise where there are:

• monopoly or anti-competitive behaviours;

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**Box 1.1 Defining regulatory regimes**

Any regulatory regime has three working components: standard setting (identifying the regulatory goal or target), monitoring compliance with the regulatory standard, and enforcement when there is non-compliance. Together, these three elements form the basis for controlling the behaviour of individuals and businesses.

information problems (asymmetries);

externalities (where the full costs and benefits of a private action are not fully accounted for and spill over to third parties and society); or

public goods (goods and services that are not produced by the market, or are under produced).

A focus on regulatory domains aimed at addressing traditional market failures confines the inquiry to areas where the case for intervention is often strongest, there are significant societal risks and, from a pragmatic perspective, the scope of the inquiry is manageable.

The regulatory instruments used cover the full range of legal and informal mechanisms through which government seeks to influence or control the behaviour of individuals and businesses —and regulate itself—to achieve desired economic, social and environmental outcomes. Regulation therefore includes primary legislation, government regulation (such as Orders in Council), deemed regulations, licences, codes and consents, rules, informal instruments and agreements for achieving compliance (see Table 2.1 on types of legislation).

Regulation can be carried out by government or quasi-government organisations. It can also be “decentred” and carried out by a diverse array of non-state organisations (Black, 2001). The latter include self-regulatory bodies such as professional bodies, industry groups, certification bodies, trade associations, corporations and industry-based certification bodies, community and voluntary bodies. For the purposes of this inquiry, the Commission will confine itself to public agencies as regulators that carry out two or more of the regulatory functions listed in Table 1.1, so enabling a focus on the major regulators.

Table 1.1 Types of regulatory functions

<table>
<thead>
<tr>
<th>Function</th>
<th>Description / examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Make rules or standards</td>
<td>Set standards, guidelines or rules to which regulated entities, individuals or activities must comply, reflecting the regulatory objectives set out in statute.</td>
</tr>
<tr>
<td>(under legislative or delegated authority)</td>
<td></td>
</tr>
<tr>
<td>Inform and educate</td>
<td>Provide general or targeted information to firms and individuals subject to regulation about compliance.</td>
</tr>
<tr>
<td>Approve/ban activities</td>
<td>Provide approval to carry out regulated activities (for example, issue consents, approve mergers, license individuals to practise in regulated profession), refuse to provide approval, or ban activities that are contrary to the objectives of the regulatory regime.</td>
</tr>
<tr>
<td>Promote and monitor</td>
<td>Actively seek information from regulated entities and/or collect market intelligence to assess compliance levels and identify potential risks.</td>
</tr>
<tr>
<td>compliance</td>
<td></td>
</tr>
<tr>
<td>Handle complaints from the public</td>
<td>Receive and process complaints from the public about the performance of regulated entities and their compliance with regulatory requirements. Where appropriate, require the regulated entity to make amends.</td>
</tr>
<tr>
<td>Enforce compliance where breaches suspected</td>
<td>Investigate cases where entities or individuals are suspected of having breached regulatory requirements, assess whether any breach has occurred and the impacts of any breaches. Where appropriate, issue penalties or enforcement action.</td>
</tr>
</tbody>
</table>

Notes:
1. This model is adapted from a framework from the Victorian State Services Authority, 2009.

1.2 Why getting regulation right is important

The Commission’s principal purpose is to provide advice to the government on improving productivity in a way that is directed at supporting the overall wellbeing of New Zealanders, having regard to a wide range of communities of interest and population groups in New Zealand society (New Zealand Productivity Commission Act 2010, s. 7).
Regulation is indispensable to the proper functioning of economies and societies. It underpins markets, protects the rights and safety of citizens, and their property, and ensures the efficient and equitable delivery of public goods and services (Organisation for Economic Co-operation and Development [OECD], 2011). In this way, regulation is an important tool for preserving and advancing the public interests. It is pervasive in everyday life, more than is often appreciated (Box 1.2). However, if regulation has misplaced objectives, is used when not needed, or is poorly designed and executed, then it can fail to achieve worthy policy objectives and have unintended consequences that harm the wellbeing of New Zealanders.

Regulatory failure occurs where regulations fail to make outcomes better, or even make outcomes worse, than if there had been no regulation. The two main ways that regulation can fail are failures of design or failures of operation. Poorly conceived and implemented regulatory arrangements not only fail to achieve stated objectives, but also impose significant costs that can undermine the very purpose of regulatory intervention. Such costs affect business productivity and profitability, and the economic circumstances of individuals and families. Ultimately this will harm economic performance and the wellbeing of New Zealand.

The institutional arrangements and regulatory practices that constitute the architecture of regulatory regimes shape the behaviours of regulators, the quality of decision making, behaviours of those regulated, and ultimately the success of regulatory regimes in achieving the desired outcomes. This inquiry is focused on better understanding what good regulatory institutions and regulatory practice look like in the New Zealand context and on ways to improve both.

This focus goes to critical issues about:

- what organisational form is best;
- the appropriate level of independence;
- how the regulator is governed;
- how the regulator is held to account;
- how the regulator makes decisions;
- how the regulator engages with industry and the public;
- how the regulator carries out its regulatory practices; and
- how the regulator is resourced with the right capability to deliver on its mandate.

Getting these things right not only means the objectives of regulation will more likely be achieved but, importantly, it builds legitimacy and trust in the regulator and regulatory regime and, with that, a higher level of trust by society.

**Box 1.2 A day in the life of a New Zealand family**

It’s 6 am and the kids barge through the door wearing their safety standard-compliant pyjamas. You reach over and turn on the clock-radio. The local station is playing its regular morning show, the content of which is subject to a code of practice for radio broadcasting.

Scratching your head you rise from your recently purchased mattress (which is covered by the Consumer Guarantees Act), make your way to the bathroom and turn on the light. The light complies with the energy performance standards administered by the Energy Efficiency and Conservation Authority. The price and reliability of the electricity used to power the light comes through a transmission network that is overseen by the Electricity Authority.

You turn on your shower. The quality of water flowing from the tap is regulated by the National Environmental Standard for drinking water, while the Commerce Commission regulates the amount you pay for the gas that heats the water.
You wash your hair with anti-dandruff shampoo approved for sale by the Minister of Health. The soap runs down a drain built in compliance with the New Zealand Building Code.

Once out of the shower, you dry yourself and reach for the shaving cream, or perhaps some makeup. The packaging proudly proclaims that the product was not tested on animals – a claim subject to scrutiny under the Fair Trading Act. You fill a glass of water and take your daily vitamin tablets – which are regulated under the Dietary Supplements Regulations administered by Medsafe.

Once dressed you make your way into the kitchen to get breakfast for the family – cereal topped with banana. The cereal has its nutritional value printed on the side of the carton. The information complies with the Nutritional Information Requirements of the Australian New Zealand Food Standards Code. The banana is from the Philippines, but it poses little threat to biosecurity due to New Zealand’s quarantine regulations.

You tip milk on the cereal. The quality of the milk is regulated under the food safety standards while the price you paid for it is monitored by the Commerce Commission.

After breakfast you take the kids to school. On the way out of the house you lock the door. Maybe you have recently purchased the house, having paid attention to some of the provisions in the Property Law Act. Or maybe you are renting the property under the conditions set out in the Residential Tenancies Act. Either way, you probably used the services of a real estate agent who was legally bound to act in accordance with the Real Estate Agents Act.

You buckle your children into a car seat that meets the Joint New Zealand/Australian standard and then start your vehicle (which of course has a current registration and warrant of fitness). You then drive (under the authorisation of your New Zealand driver’s licence) to your children’s school – being sure to obey local traffic regulations as you only have 10 demerit points left on your licence!

You drop your children off at school, where their teacher is registered by the New Zealand Teachers’ Council as being capable to deliver the New Zealand Curriculum and the newly-elected school board is charged with giving effect to the Government’s National Education Guidelines. As you drive away, you wonder how the project to earthquake strengthen the old school hall to the Ministry of Education’s building design standards is going.

At work, regulations administered by the Ministry of Business Innovation and Employment promote a safe working environment while the Human Rights Act seeks to protect you against discrimination from your co-workers. Your pay and conditions are covered by the Employment Relations Act which (among other provisions) protects the holiday entitlements you negotiated with your employer.

And all this before smoko – which of course is outside….

1.3 Regulatory developments and challenges

Regulation – that is, the promulgation of rules by government accompanied by mechanisms for monitoring and enforcement (Black, 2002) – has become a topic of increasing interest and concern for governments, industries and academics over the past 30 years. In New Zealand, this has led to:

- the progressive introduction of greater obligations on public service departments and ministers to test whether new regulation is necessary, proportionate and efficient (for example, Regulatory Impact Assessments);
- requirements for departments to regularly review the stock of existing regulation, to ensure it is still fit-for-purpose (for example, the Regulatory System Report 2013: Guidance for Departments);
- the establishment of a dedicated agency for regulatory management and quality (the Regulatory Impact Assessment Unit located within the Treasury);
establishment of a dedicated parliamentary Select Committee, the Regulations Review Committee, to review, hear complaints on, and (if necessary) recommend the amendment or revocation of secondary legislation;

the detailed consideration, by ministers, Parliament and an expert taskforce, of legislative tools for improving the quality of regulation.

The interest in regulation in New Zealand stems from a number of important developments.

Individual freedoms and human rights have taken on greater importance in New Zealand society, as signalled by such developments as the passing of the Bill of Rights Act in 1990 and Human Rights Act in 1993.

There has been a growing awareness of the role that good-quality regulation and institutions can play in promoting economic growth (as seen, for example, in the new institutional economics of Douglass North, Ronald Coase and Oliver Williamson).

Reforms over the last quarter of the twentieth century have changed how governments organise themselves, provide services and deliver policy. These changes have made regulation a more visible and important government activity (Yeung, 2010; Majone, 1994; Christensen, Lie & Laegreid, 2008).

Society is much more diverse with a broader range of attitudes to risk and expectations about what government can do.

In New Zealand, the reforms saw some traditionally publicly-provided services transferred to the private sector or commercially-focused state entities (for example, electricity and telecommunications) or devolved down to local or community bodies (for example, school education and some health services). A range of decisions once taken centrally by a minister or within a public service department are now taken by state providers, private firms and individuals. But governments have retained (and in some cases set rules or standards through regulation) their ability to affect the quantity, quality, safety and distribution of services.

These public sector reforms are part of an observed global international trend. Public management scholars have described this trend as governments “steering” rather than “rowing” (Osborne & Gaebler, 1992). Governments in the developed world now focus more on setting the rules of the game than deciding how the players will move. This has had a number of implications, and created a series of challenges.

Rules and standards in regulation are generally set in advance of operational decisions by firms and individuals, and are publicly-available. This has meant that in many cases the actions of governments are more predictable. However, public and ex ante rules are more easily contested than decisions taken within departments that are not transparent.

The control of activities or risks through regulation imposes costs on firms, individuals and the wider community. These costs include compliance or administrative burdens (such as time and money devoted to filling out forms, participating in audits, changing internal systems to comply with regulation) and opportunity costs (such as innovation or production foregone, because they were not permitted by the regulatory framework or because firms were uncertain whether they would be permitted). The design of regulatory systems can affect the level of these costs.

Effective regulation often relies upon specialised expertise (such as a detailed understanding of a particular industry, economic or legal training). This may limit the ability of the public and Parliament to assess the effectiveness or efficiency of the regulatory regime if the expertise is absent.

In many cases monitoring and enforcement of regulation has been delegated to legally independent organisations. This is usually done to prevent political interference in regulatory decisions. However, this delegation and legal independence can raise questions about how to ensure accountability to Parliament and the public.

As the delivery of services has been transferred to commercial or local bodies, consumers and consumer interests have taken on a prominent role in regulation. Many regulatory regimes have specialised
consumer complaints and redress mechanisms (such as the Health and Disability Commissioner and the Banking and Insurance Ombudsman), with a number aimed at promoting the “long-term benefit of consumers”. However, effective consumer participation in regulatory regimes can be challenging, especially where the regulatory area requires specialised expertise and producers are well organised and resourced.

- Independent regulatory authorities may wield coercive powers, such as the ability to block entry to a market or profession or to prevent profitable transactions and the scope to impose fines and penalties. As part of the wider legal system, affected individuals or firms may expect to have a right of appeal or review of regulatory decisions.

- In some cases, regulatory authorities are required to balance competing interests or objectives (for example, consumers and producers, development and environmental protection). Regulators often need to exercise discretion, so that they can judge a case on its merits. On the other hand, citizens and firms may wish regulators to spell out the principles, rules or processes they will apply to a case, so that more decisions are predictable. Discretion and certainty are a constant tension in regulatory regimes.

In summary, regulation has become an increasingly prominent tool for protecting the public and improving how markets perform. The growing use of regulation as a means to achieve social and economic objectives poses a number of challenges in terms of efficiency, accountability, accessibility and fairness.

There is a question as to whether New Zealand’s regulatory regimes are unnecessarily complex and whether they could be simplified. It is commonly thought that increasing complexity is inevitable in modern societies. But complexity can instead call for simple decision rules. Indeed, the Nobel prize winner Herbert Simon, the father of decision-making behaviour under uncertainty, argued that it was precisely because humans operate in a complex environment that they sought simple behavioural rules. Despite this logic, the tendency of governments and regulators is to think “more is more”. Andrew Haldane and Vasileios Madouros of the Bank of England wrote:

> The response to the financial crisis by banks and regulators has been swift and sizable. Gaps in risk management have been filled, deficiencies in regulation plugged, errors by regulators corrected. This is a self-healing and familiar response. Past crises have also been met by a combination of more risk management, more regulation and more regulators. More has been more. (Haldane and Madouros, 2012, p.7)

It needs to be recognised that the capacity of individuals and firms to comply is a function of the complexity of regulatory regimes. Capability and expertise, for both regulators and regulated alike, is likely to be an ongoing issue in New Zealand. Complicated rules require complicated processes and information, which increases the demands on those who are regulated.

> This observation has two implications. First, that assessments of capacity are relative to the demands made by the regulatory regime. Second, that one way to increase regulatee capacity is to simplify the regime. (Black & Baldwin, 2012, p. 137)

This inquiry provides an opportunity to look at New Zealand’s regulatory regimes to see where the regulatory management system can be improved. A trajectory of “more is more” is not inevitable. Improvements can be found, for example, in clarifying the roles and expectations of regulators, removing inconsistencies in regimes, improving workforce capability, introducing systematic processes for reviewing the existing stock of regulation, improving transparency – in short – by making the system simpler for those who design and implement it and for those who must comply with it.

### 1.4 The Commission’s approach

This inquiry examines the institutional arrangements and regulatory practices listed in Figure 1.1 to determine how they can best shape the incentives on regulators and improve regulator capability, ultimately leading to regulatory decisions that preserve and advance the public interest. Each of these design features is inextricably linked and can be thought of as a mutually reinforcing system. For example, poor role clarity will impact on regulator culture, leadership and regulatory practice. Likewise, the level of regulatory independence provided for will determine the accountability, performance and monitoring...
framework that is most appropriate, just as the capability of the regulator will shape the decision review mechanisms.

**Figure 1.1 The Commission’s approach to this inquiry**

![Diagram showing the Commission’s approach to this inquiry]

### 1.5 Gathering evidence

This draft inquiry report’s findings and recommendations have been informed by a range of evidence.

- **Submissions:** An Issues Paper was released in August 2013 calling for submissions and feedback from interested parties (54 submissions were received).

- **Engagement:** 92 meetings were undertaken with representatives from businesses, regulatory agencies, central government agencies and academia.

- **Roundtable discussions:** Roundtable discussions were held with officials who had been involved in designing new regulatory regimes, and with businesses subject to economic regulation and regulatory compliance professions.

- **Surveys:** The Commission drew on three surveys to gain information about regime and regulator performance in New Zealand and the experience and impact of regulation on business:
  - Colmar Brunton conducted an online Commission survey of 1,526 senior decision makers in New Zealand businesses (from a cross-section of industries), examining business experiences with government regulations (Colmar Brunton, 2013).
Victoria University of Wellington’s Industrial Relations Centre (VUW IRC) and the Public Service Association (PSA) surveyed 15,762 PSA members on their experiences working in government agencies. The Commission used the survey results to compare the experiences of regulatory workers (around 300 in regulatory roles in central government agencies and 160 in local government or district health board regulatory roles) with non-regulatory workers (VUW IRC & PSA, 2014).

A short survey was undertaken of 23 chief executives of New Zealand regulatory agencies. The survey focused on their perceptions of regulatory regimes (NZPC, 2014a).

- **Information request**: An information request went to 33 regulatory agencies seeking detailed information about their institutional features and regulatory practices. Twenty-six agencies responded.

- **Case studies**: Three case studies were carried out that drilled deep into understanding a particular sector, regulatory domain or regulator. Case studies investigated the regulatory frameworks for financial markets and the aged care sector and the Environmental Protection Agency (EPA).

- **International experts**: The Commission had the benefit of meeting with or attending presentations by leading international experts in the field of regulation.

Together, these have provided a rich picture of New Zealand’s regulatory landscape, institutions, regulatory practices and regulatory impacts on business and productivity.

### 1.6 Guide to this report

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<td><strong>Chapter 4</strong> outlines the impacts and causes of unclear regulator roles, and proposes actions to improve role clarity.</td>
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<td><strong>Chapter 5</strong> discusses the importance of independent regulators and how this relates to their institutional form.</td>
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<td><strong>Chapter 6</strong> considers appropriate governance and decision-making arrangements, including the role of administrative discretion.</td>
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<td><strong>Chapter 15</strong> reviews the approach to managing the large stock of legislation and regulation in New Zealand, and recommends improvements.</td>
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<td><strong>Chapter 16</strong> provides suggestions about how the report’s recommendations could be embedded in New Zealand’s regulatory management system by strengthening existing institutions and creating an environment in which the recommendations will have most effect.</td>
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</table>
2 Features of New Zealand regulation

Key points

- Regulation is the product of an interaction between a number of actors within and outside of government, and can best be thought of as a system. To develop proposals for improving regulation, it is important to understand the factors that affect the regulatory system. These factors can include constitutional arrangements, history, cultural practices and expectations, geography, levels of national wealth and economic structures.

- Five main features have a significant impact on how regulation is made and implemented in New Zealand:
  - a centralised and statute-driven system, with comparatively few checks and balances;
  - resource constraints, driven by New Zealand’s small population, distance and relatively low incomes;
  - a weak review and evaluation culture;
  - the acknowledgement of Māori interests in regulation; and
  - the increasing role of international regulatory standards.

- New Zealand is notable for having regulatory regimes that score highly on numerous international measures of quality, while also being the subject of criticism for instability and inconsistency.

- These features lead to some systemic themes in the development and implementation of regulation in New Zealand:
  - A number of important regulatory regimes in New Zealand are young and are still settling down. Electricity and telecommunications are the most prominent examples. This has created perceptions of risk and instability.
  - Regulatory regimes in New Zealand can easily become rigid and obsolete. This reflects the strongly statute-driven system, scarce parliamentary time, and the weakness of review and evaluation systems. As a result, New Zealand regulation can struggle to keep up with changes in technology or public expectations.
  - New Zealand has applied different regulatory models across similar issues, rather than applying a coherent and consistent approach. This increases compliance costs on firms operating across multiple regimes, and limits the ability of regulators to learn from each other’s experiences.
  - Although official recognition of Māori interests in regulation has increased since the 1980s, questions remain over how best to recognise Māori interests and acknowledge Treaty of Waitangi principles. Also, mechanisms for ensuring Māori can participate effectively in the implementation of regulatory systems are still developing.

2.1 Introduction

Regulatory institutions and practices vary between countries. Differences in regulatory approaches are the result of a range of factors, including constitutional arrangements, history, cultural practices and expectations, geography, levels of national wealth and economic structures. To identify recommendations on how to improve the design and operation of regulatory regimes in New Zealand, it is important to understand the context within which regimes are set, and the factors that affect their implementation. This
Chapter 2 | Features of New Zealand regulation

This chapter explores the New Zealand regulatory system, identifies key factors that affect regulatory design and implementation, and highlights some systemic themes in New Zealand regulation. In particular:

- Section 2.2 provides a brief overview of the regulatory system in New Zealand;
- Section 2.3 outlines features that have a significant impact on how regulation is made and implemented in New Zealand;
- Section 2.4 considers the strongly divergent views about the quality of New Zealand regulation; and
- Section 2.5 identifies some systemic themes in the design and implementation of New Zealand regulation.

A note on terminology

There are many ways of defining the different sources of regulation. For the purposes of this inquiry, the Commission distinguishes between two main types (Table 2.1).

### Table 2.1 Sources of legislation

<table>
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<tr>
<th>Type of source</th>
<th>Definition</th>
<th>General features</th>
</tr>
</thead>
</table>
| “Statutes” or “primary legislation” | Statutes or primary legislation are mostly (apart from local and private Acts) of general application and deal with general matters of public policy. Local and private Acts are confined to a geographical locality or to benefiting a limited class of persons. | ● Most are drafted by the Parliamentary Counsel Office (PCO).  
● Referred to a Select Committee for examination and report after the first reading in Parliament.  
● Passed by Parliament (after three readings and debate), Royal Assent given by the Governor-General. |
| “Secondary legislation” or “delegated legislation” | Secondary legislation is legal rules promulgated by a delegate of Parliament (an individual or body) entrusted with specific powers of legislation. There are several different types of secondary legislation:  
- Government regulations: these are drafted by the PCO; approved by the Cabinet; promulgated by the Governor General in Council; notified in the Gazette; and published in the Statutory Regulations.  
- Deemed regulations: these are usually drafted by the organisation making them and are not normally subject to Cabinet approval or submitted to the Governor General in Council. Deemed regulations take a variety of forms, including rules, codes, instructions, and standards. They are often made by ministers or officials.  
- Local authority bylaws: made under the Local Government Act 2002. | ● Government and deemed regulations are examined by the Regulations Review Committee (a parliamentary Select Committee).  
● Parliament has powers to disallow any government or deemed regulations. |

**Notes:**

1. These definitions differ from the categories used in the Legislation Act 2012.
2.2 A system with many players

Regulation in New Zealand is designed and implemented by a number of actors within and outside of government. It is also subject to a number of checks and balances. The roles of the different actors, and the relative strength of the checks and balances, are examined in more detail elsewhere in this report. But at a high level, the process of designing and implementing regulation can be thought of as a system (Figure 2.1).1

In many New Zealand regulatory regimes:

- A central government department identifies the policy problem and recommends regulatory action;
- Cabinet takes the decision to introduce new regulation;
- Parliament (for primary legislation) or the Executive Council (for secondary legislation, such as Orders in Council) approves the new regulation;
- A Crown entity administers the new regulation, monitors compliance and takes enforcement action, where required;
- The courts interpret the law, resolve disputes and carry out judicial review; and
- The central government department evaluates the impact of the new regulation and assesses the performance of the regulator.

However, some functions may be carried out by different sets of people or organisations. In some regimes, the regulator may identify a problem, take the decision to introduce a new rule, approve the new rule, and administer and enforce the rule. For example, the Electricity Authority (EA), an independent Crown entity, is empowered to make certain amendments to the Electricity Industry Participation Code (the rules which

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1 As discussed in Chapter 1, this inquiry does not deal with the "problem identification" or "decision to act", and focuses on the other elements of the regulatory system.
govern the New Zealand electricity market) and to administer and enforce the amended Code. In other regimes, organisations outside of central government implement regulation. For gas regulation, a private company (the Gas Industry Company) has a role in identifying policy problems, recommending new regulations, administering regulations and monitoring compliance. Local authorities play significant administrative, monitoring and enforcement roles in a number of regulatory regimes (NZPC, 2013a).

There are a number of constraints on regulatory power in New Zealand. Regulators may only exercise the powers that have been given to them by statute or through other methods approved by Parliament. Some primary legislation allows ministers, the Governor-General or regulators themselves to make secondary legislation (government or deemed regulations). This secondary legislation may be disallowed (cancelled) by Parliament. Regulators’ operating processes may be prescribed in law. The courts can review regulators’ actions to ensure they are reasonable and lawful. And the ability of regulators to successfully implement their regimes can depend on the willingness and capability of regulated parties (such as businesses or professionals) to comply. Regulators may lack the information, capability and capacity, resources or powers to ensure compliance.

Regulatory systems like that outlined in Figure 2.1 exist in many countries. However, their processes and outcomes vary significantly between countries, based on such factors as constitutional settings, resource levels and cultural expectations. Section 2.3 describes the main features that affect the regulatory system in New Zealand.

### 2.3 Significant features of New Zealand’s regulatory system

Five main features have a significant impact on how regulation is made and implemented in New Zealand:

- a centralised and statute-driven constitutional system, with comparatively few checks and balances;
- resource constraints, driven by New Zealand’s smallness, distance and relatively low incomes;
- a weak review and evaluation culture;
- the growing recognition of Māori interests in regulation; and
- the increasing role of international regulatory standards.

#### A centralised and statute-driven constitutional system

New Zealand’s constitutional system is highly centralised and relatively lacking in checks and balances, compared to other countries. Palmer (2007) notes that New Zealand inherited the doctrine of parliamentary sovereignty from Westminster. Yet, as a unitary state with no supreme law, no federalism, no written constitution and no membership of a supra-national body that binds domestic laws as does the EU, New Zealand now manifests this doctrine in an even purer form than the United Kingdom. (p. 582)

Other factors contributing to a powerful central government include parliamentary procedures (such as urgency, and Part-by-Part review of legislation during the Committee of the Whole House) which can permit the passing of legislation with limited scrutiny, and the lack of strong industry bodies (Gill, 2013).

These features have a number of implications for the design and implementation of New Zealand regulatory regimes. First, Cabinet plays a very strong role in developing regulatory policy, including technical matters and lower-level rules in some cases (Gill, 2011). Palmer (2006) commented it is “notable in New Zealand that Cabinet decisions get down to a level of detail and specificity that is not found even in Australia” and observed that Cabinet has a much more central role in government in New Zealand than is the case in the United Kingdom (p. 21).

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2 Chapter 10 discusses the role of the courts in the regulatory system.

3 Chapter 11 explores issues with compliance and enforcement strategies.
Second, New Zealand’s public service is vertically integrated and lacks strong traditions of horizontal coordination (Gill, 2013). This makes individual ministers central and often active “customers” in many New Zealand regulatory systems. Conway (2011) noted “a very ‘hands on’ approach from some government ministers, who are often in regulatory decisions and enforcement at a very detailed level” (p. 22).

Third, the Commission heard from a number of inquiry participants that New Zealand makes more use of primary legislation in its regulatory systems than other jurisdictions (see, for example, Frankel & Yeabsley, 2013). The lack of data and the differences in constitutional systems between countries make this statement difficult to test objectively. There is not a consistent and internationally-shared definition of “primary” or “secondary” legislation. It is also difficult to find the right point of comparison with foreign jurisdictions. For example, many other countries have federal systems (for example, Australia) or are members of organisations that make laws on their behalf (for example, the European Union). As a result, primary legislation in other countries is often made at more than one level of government, while in New Zealand all primary legislation is made by Parliament.

**Benefits and costs of legislation**

The heavy use of primary legislation to underpin regulatory regimes has benefits and disadvantages. On the positive side of the ledger, all legislation (except bills under urgency) must be referred to a Select Committee for consideration under Parliament’s rules of procedure (Standing Orders). Select committees often seek submissions from the public on the bills before them. As a result, the public can have a significant ability to influence the design of regulatory systems in New Zealand. David McGee, the former Clerk of the House of Representatives, noted that, through Select Committees, “the public is enlisted into the legislative process in a way that does not occur with overseas legislatures. Select committee consideration of a bill and the public’s ability to participate in it are regarded as akin to democratic rights” (McGee, 2007, p. 424). George Tanner, former Chief Parliamentary Counsel, said of the Select Committee process, “At its best, it works well and is probably a more effective scrutiny process than many upper Houses around the world” (Frankel & Yeabsley, 2013, p. 13).

However, this reliance on primary legislation has costs. Parliamentary time is a scarce resource, which is one key reason why it can be hard to amend legislation and keep regulatory systems up to date. This can put pressure on regulators working with outdated statutes. As Maritime New Zealand commented:

> There is so much legislation on the NZ statute book that even if changes were identified due to perception of risk, the ability to make fundamental shifts is often hampered by more urgent matters on the political and social landscape. This tends to lead to crisis driven law-making (i.e. policy initiatives that are only made in response to a significant event or crisis) at the expense of clearly programmed initiatives that ensure maintenance of regulatory stock. As a result regulators are often left to perform their functions within old, outdated regimes with seemingly increasing public and political expectations they will “adjust” to the changes within those outdated regimes. For entities that are creatures of statute, this presents particular challenges because they are limited to perform the functions given to them by law. (sub. 15, p. 3)

Almost two-thirds of public sector chief executives who participated in a Commission survey on regulatory regimes either strongly agreed or agreed with the proposition that agencies with regulatory functions “often have to work with legislation that is outdated or not fit-for-purpose” (Figure 2.2).

In addition, while New Zealand makes considerable use of Select Committees to review proposed legislation, there is much less use of other engagement mechanisms. Gill (2011) noted that there is more consultation on early policy design stages in Australian federal or state government than in New Zealand, with significant use of “exposure drafts” and less frequent consideration by Select Committees. As ministers or officials may be less inclined to make substantial changes to legislation once it is before Parliament, the reliance on Select Committees for regulatory scrutiny in New Zealand may mean that other opportunities to seek contributions on and improve draft regulation are missed.
Impacts of MMP

A number of commentators have argued that the move to the Mixed-Member Proportional (MMP) electoral system in 1996 has acted as a constraint on the Executive’s ability to pass legislation, especially in comparison with the previous First Past the Post (FPP) electoral system. Palmer and Palmer (2004) concluded that MMP had “slowed down the system of government, made it less friendly to executive power, increased the distinction between the Executive and Parliament and revitalised Parliament”. Malone (2009) agreed, noting that under MMP, governments “no longer have automatic majorities on the select committees”, the number of government bills passed each year has fallen since 1996 and government bills take longer to pass through all their stages than was the case under FPP. According to Malone (2008), this slower pace and lower output reflects the fact that the Executive under MMP has to devote greater time and energy to building and maintaining parliamentary support for legislation and cannot resort to urgency as easily.

However, while MMP has slowed the pace of government and forced policy changes in some areas, the Executive continues to have significant scope to implement policy. Malone (2008) commented:

'It is relatively uncommon for governments to find themselves in a position where they are unable to legislate on account of a lack of a parliamentary majority. It is true that changes may need to be made to proposals to take into account a policy position of a non-government party, but the main thrust of a policy will invariably survive intact and be passed into law. Scores of major government bills have been passed by MMP parliaments. (p. 234)

To the extent that MMP has acted as a constraint on government legislation, it may have strengthened incentives on the Executive to use secondary legislation to advance government policy:

The power to make regulations assumes greater importance under MMP. Where there are governments with minority support in Parliament or a coalition with some uncertainties within it, a Cabinet may not always want to run the gauntlet of Parliament to get its policies adopted. It may instead use its power to the full to make regulations from statutes already passed. (Palmer & Palmer, 2004, pp. 207-208)

Palmer and Palmer (2004) found that the average annual number of government regulations made in New Zealand rose in the six years following the introduction of MMP. Although most government regulations are subject to ex post parliamentary oversight and possible disallowance, parliamentary and public scrutiny of secondary legislation before its introduction is more limited than is the case for primary legislation.

Size, distance and resource constraints

As a distant country with a small population and per-capita incomes below the Organisation for Economic Co-operation and Development (OECD) average, New Zealand faces a number of tensions and trade-offs that affect how its regulatory regimes are designed and run.
Limited resources mean that New Zealand has to be selective in the regulatory issues it tackles or approaches it adopts. As the Reserve Bank of New Zealand commented:

Our smaller market size means that it is not always practical or in our best interest to mirror every single regulatory initiative or institution that significantly bigger economies have. Those bigger economies are usually in a position to dedicate more resources to regulatory affairs and to set up specialised regulatory institutions. (sub. 9, p. 1)

Vector argued that limited fiscal resources have led to an excessive focus in New Zealand on reducing costs in the design of regulatory systems:

[T]here has been a general reluctance on the part of officials and Ministers to establish regulatory bodies across all of New Zealand’s regulatory regimes and/or set up formal arrangements for oversight and review… A reluctance to consider proper separation of regulatory roles in order to manage costs, which has been a barrier to regulatory reform in New Zealand in the past, is arguably misplaced. (sub. 29, pp. 25, 27)

In some areas, resource constraints have led New Zealand regulators to take more flexible and proportionate approaches. The Institution of Professional Engineers New Zealand (IPENZ) cited the example of regulators allowing chartered professional engineers to certify operator protective structures on mobile plant (for example, bulldozers and excavators), rather than requiring “destructive laboratory testing, as is generally the case overseas”. IPENZ described this approach as “alternative means of attaining satisfactory public-good outcomes that are more readily available in larger economies” (sub. 21, p. 5).

Expertise the greatest constraint

Arguably the most significant resource constraint New Zealand faces is expertise. A number of regulatory systems rely on specialised technical expertise, yet New Zealand’s size provides fewer opportunities to specialise than are available in larger-scale economies. Searancke et al noted:

New Zealand has relatively limited competition in many markets and lack of depth or capability amongst expert professions and advisors. This increases the risks for us that regulatory systems which rely for their effectiveness on vigorous competitive disciplines, well-developed markets for information and readily available expertise, may not be effective, or as effective, in New Zealand. (Searancke et al, 2013, pp. 1-2)

Mighty River Power echoed this conclusion, and added that it can therefore be difficult in New Zealand to “strike an appropriate balance of industry, consumer and regulatory representation” (sub. 30, p. 10).

Expertise constraints affect how well regulatory regimes are designed. In the Commission’s engagements with senior government and industry officials, it was noted that designing a regulatory system in New Zealand was often a “once in a career” experience in the public service, and that lessons learned were not well retained or shared with others.

Expertise constraints are an inevitable result of a drive towards regulatory complexity. The shift to longer, more complicated, principle-based or risk-based frameworks has created a demand for higher technical skills among regulatory staff and imposed growing compliance burdens on those subject to regulation. New Zealand is not alone in facing growing regulatory complexity. Haldane and Madouros (2012) describe the growth of financial regulation in Britain:

In the UK, regulatory reporting was introduced in 1974. Returns could have around 150 entries … Today, UK banks are required to fill in more than 7,500 separate cells of data – a fifty-fold rise. Forthcoming European legislation will cause a further multiplication. Banks across Europe could in future be required to fill in 30-50,000 data cells spread across 60 different regulatory forms. There will be less risk of regulators missing the wood from the tress, but only because most will have needed to be chopped down. (pp.11-12)

Haldane and Madouros go on to question whether the drive to complexity is leading to more effective regulation, using the metaphor of catching a frisbee:

Despite this complexity, efforts to catch the crisis frisbee have continued to escalate. Casual empiricism reveals an ever-growing number of regulators, some with a Doctorate in physics. Ever-larger
litters have not, however, obviously improved watchdogs’ Frisbee-catching abilities. No regulator had the foresight to predict the financial crisis...

So what is the secret of the watchdogs’ failure? The answer is simple. Or rather, it is complexity…the type of complex regulation developed over recent decades might not just be costly and cumbersome but sub-optimal for crisis control. In financial regulation, less may be more. (p.1)

New Zealand is probably less able than larger countries to sustain further increases in complexity. However, current regulatory management processes do not measure capability levels or gaps or compliance burdens. Ministers and officials therefore do not have a sense of where the expertise constraints lie or whether the existing level of complexity has already outstripped the ability of regulatory staff to deliver and regulated parties to comply.

Scale and competition trade-offs

New Zealand often has to strike a different balance between the goals of competition and efficiency in its economic regulation than would be the case in other countries. As Berry (2013) notes, there exists a basic tension between productive efficiency and competitive conditions. In many markets in New Zealand demand means that only a few firms can operate at productively efficient levels of manufacture. New entry may often create diseconomies of scale, unless domestic firms are also able to export their output. (p. 6)

The limited number of participants in some domestic markets and the physical distance from other countries potentially make the social and economic costs of overly restrictive regulation higher in New Zealand. Higher levels of industry concentration may be required in New Zealand to produce goods and services at similar levels of efficiency as other countries. Regulation also needs to allow cooperative arrangements between rivals that promote dynamic efficiency, such as allowing the spreading of cost or sharing of investment risk when introducing new technologies. Such an “efficiency defence” has been explicitly recognised in New Zealand’s main competition regulatory framework, the Commerce Act 1986 (Scott, 2013).

A weak review and evaluation culture

New Zealand does not have strong processes for reviewing regulatory regimes. A 2013 review of New Zealand’s regulatory systems found “general weaknesses across agencies in undertaking and utilising review processes” and concluded that “[w]e tend to have a ‘set and forget’ mind set to regulation” (Office of the Ministers of Finance & Regulatory Reform, 2013a; 2013b). The Ministry of Business, Innovation and Employment observed that 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 a regulatory intervention, and also in determining whether regulatory regimes are, or continue to perform, effectively. (sub. 52, p. 3)

Gill and Frankel (2013) cited George Tanner, who observed that [t]he lack of any systematic process for post-enactment scrutiny means that routine maintenance of some very major pieces of legislation rarely happens. We paint our houses and service our cars, but we don’t look after our laws in the same way. (p. 13)

Aviation New Zealand noted that “if there is a major event, money is applied to fixing perceived problems however very little funding is there to proactively address issues before they occur” (sub. 36, p. 3). The Board of Airline Representatives New Zealand Inc. said that too often “regulations and regulatory requirements are developed and left to lie, with no on-going review of whether they are functioning effectively and whether they are producing the desired outcomes” (sub. 16, p. 1). IAG characterised the New Zealand approach as “largely piecemeal and ad hoc. Specific regulatory regimes are often developed and implemented in response to short-term political pressures or specific (dramatic) instances of perceived regulatory failure” (sub. 10, p. 12).
A lack of embedded review processes?
In part, the weak review and evaluation culture may reflect the lack of embedded review processes in the New Zealand administrative system. Unlike most Australian states and territories (and the Australian federal government), New Zealand does not make use of sunset clauses and, according to a survey conducted for Gill and Frankel (2013), very few New Zealand statutes or regulations have review provisions. Several submitters also noted that there are few formal processes for the periodic review of regulatory regimes or regulators (Vector, sub.29, pp. 29-30; Electricity Networks Association, sub. 27, p. 12).

Insufficient pressure from existing accountability provisions?
Another possible cause of the weak evaluation and review culture is insufficient pressure from existing accountability provisions. These include the Parliamentary Regulations Review Committee, performance reviews by the Office of the Auditor-General and monitoring of Crown entity regulators by departments and ministers. Submitters identified weaknesses with all three:

In principle, Electricity Authority rules and other similar tertiary legislation is subject to review by the Parliamentary Regulations Review Committee and any rule can, potentially, be struck down or referred back to the rule-making body should it be found to be ultra vires or to have been incorrectly made. However, in practice, due to limited resources and time, the Committee can only review a relatively small number of regulations, rules or orders. (Powerco, sub. 14, p. 3)

Although the Controller and Auditor-General undertakes a number of performance audits annually, a lack of resources, among other factors, limits the extent to which regulators come under effective scrutiny. (Mortlock Consultants Ltd, sub. 31, p. 8)

Existing monitoring mechanisms under the Crown Entities Act are underutilised, possibly because they are viewed as weak accountability tools and/or because there are limited consequences for poor performance. (Vector, sub. 29, pp. 28-29)

The Minister does not appear to use existing powers to input into and/or amend the SOI or review operations and performance. (Genesis, sub. 48, pp. 5-6)

Not an issue specific to regulation…
Poor review and evaluation practices appear to be an issue across central government, and not just focused on regulatory regimes. A 2003 State Services Commission and Treasury report concluded that the evaluative resource is currently poorly targeted, with repeated interventions in areas where there is a high degree of certainty and a lack of consideration of agency priorities across the whole spectrum of business or wider government priorities. Use of evaluative findings to inform policy, service delivery or broad government strategy and budget decision-making decisions is patchy. (SSC & New Zealand Treasury, 2003)

A 2011 review of expenditure on policy advice similarly found that the “New Zealand policy advisory system’s use of evaluation is limited in contrast with some governments”, the “scope, methods and relevance of evaluation need reconsideration” and more “evaluation needs to be undertaken as part of the general process of improving the quality of policy analysis and advice” (Review of Expenditure on Policy Advice, 2011).

…nor to central government
In its recent inquiry into local government regulation, the Commission identified in local authorities:

- weak “whole-of-system” mind sets;
- performance reporting and post-implementation reviews that provided few feedback loops to help councils improve how they deliver their regulatory functions; and

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4 There are a few exceptions, however: For example, s.157AA of the Telecommunications Act 2001 requires the Minister to “commence a review of the policy framework for regulating telecommunications services in New Zealand, taking account of the market structure and technology developments and competitive conditions in the telecommunications industry at the time of the review, including the impact of fibre, copper, wireless, and other telecommunications network investment” before 30 September 2016.
a common view that regulatory performance assessment was a compliance task, rather than an important means of improving performance (NZPC, 2013a).

**Steps being put in place to improve review and evaluation**

The current government has put greater focus on review and evaluation through its *Initial Expectations for Regulatory Stewardship*, which spells out how departments should design, implement and maintain regulatory regimes (Box 2.1).

**Box 2.1  Cabinet’s Initial Expectations for Regulatory Stewardship**

In March 2013, the Cabinet agreed to the *Initial Expectations for Regulatory Stewardship* (see below). These expectations replace those outlined in the 2009 *Government Statement on Regulation: Better Regulation, Less Regulation*.

Cabinet expects that departments, in exercising their stewardship role over government regulation, will:

- monitor, and thoroughly assess, at appropriate intervals, the performance and condition of their regulatory regimes to ensure they are, and will remain, fit for purpose;
- be able to clearly articulate what those regimes are trying to achieve, what types of costs and other impacts they may impose, and what factors pose the greatest risks to good regulatory performance;
- have processes to use this information to identify and evaluate, and where appropriate report or act on, problems, vulnerabilities and opportunities for improvement in the design and operation of those regimes;
- for the above purposes, maintain an up-to-date database of the legislative instruments for which they have policy responsibility, with oversight roles clearly assigned within the department;
- not propose regulatory change without:
  - clearly identifying the policy or operational problem it needs to address, and undertaking impact analysis to provide assurance that the case for the proposed change is robust, and
  - careful implementation planning, including ensuring that implementation needs inform policy, and providing for appropriate review arrangements;
  - maintain a transparent, risk-based compliance and enforcement strategy, including providing accessible, timely information and support to help regulated entities understand and meet their regulatory requirements; and
  - ensure that where regulatory functions are undertaken outside departments, appropriate monitoring and accountability arrangements are maintained, which reflect the above expectations.

(Source: Offices of the Ministers of Finance and Regulatory Reform, 2013b.)

**The acknowledgement of Māori interests in regulation**

Another distinctive feature of New Zealand’s regulatory system is the acknowledgement of Māori interests. This is reflected both in the overall regulatory management system and in a number of specific regulatory systems.

**Māori in New Zealand’s regulatory management system**

Under the Cabinet Manual, all proposals to introduce a new bill to Parliament must clearly specify whether the proposed bill would comply with the principles of the Treaty of Waitangi, and identify any variances...
Disclosure Statements for government legislation must outline the steps that have been taken to determine whether the policy to be given effect by the bill is consistent with the principles of the Treaty of Waitangi (New Zealand Treasury, 2013a). There is a general presumption that Parliament will legislate in accordance with the principles of the Treaty and will appropriately apply the principles on issues of relevance to Māori (Legislation Advisory Committee, 2012). There is also an expectation that Māori will be consulted appropriately where legislation affects the rights and interests protected by Article 2.

Although the requirements and practices outlined above provide protection for Māori interests and Treaty principles, this protection is not absolute. Parliament remains sovereign, and retains the power to pass legislation that conflicts with Treaty principles or that impairs or extinguishes customary rights.

Māori involvement in regulatory implementation

A number of individual regulatory regimes reference the Treaty or Treaty principles or otherwise acknowledge Māori interests in regulation. The involvement of iwi and Māori in regulatory implementation is arguably the most advanced in environmental regulation. Prominent areas of Māori involvement in environmental regulation include customary fisheries, joint management agreements, and iwi management plans.

- **Customary fisheries**: Guardians (tangata tiaki or tangata kaitiaki) can be appointed by the Minister of Fisheries to authorise customary fishing within specified areas, and to play a role in wider fisheries management. Tangata tiaki/tangata kaitiaki or tangata whenua may also apply to the Minister for the establishment of mātaitai reserves, under which the guardians can make bylaws to restrict or ban fishing in the area.

- **Joint management agreements**: These agreements permit joint Māori and government (local or central) management of natural features. The first agreement was between the Taupō District Council and Ngāti Tūwharetoa, which allows publicly notified resource consents and plan changes applying to multiply-owned Māori land to be decided upon by a panel chosen equally by Council and the iwi. Another example is the Waikato River Authority, a statutory body charged with restoring and maintaining the health of the Waikato River. Members of the Authority’s Board are appointed by the river iwi and ministers of the Crown.

- **Iwi management plans**: Local authorities must take into account iwi authority planning documents when preparing district and regional plans.

Other areas of regulation also provide for the protection of Māori interests in specific sectors. For example, under section 17(1)(c) of the Trade Marks Act 2002, the Commissioner of Trade Marks “must not register as a trade mark or part of a trade mark any matter ... the use or registration of which would, in the opinion of the Commissioner, be likely to offend a significant section of the community, including Māori”. The Commissioner is also obliged under sections 177 and 178 to appoint a committee to advise “whether the proposed use or registration of a trade mark that is, or appears to be, derivative of a Māori sign, including text and imagery, is, or is likely to be, offensive to Māori”.

The comparatively high level state of Māori involvement in environmental regulation most likely reflects ownership links, Treaty obligations and legislative recognition.

- **Strong cultural and ownership links to natural resources**: Iwi and hapū have strong relationships with the land, local geographical features (for example, rivers, mountains, wahi tapu) and sea, often involving kaitiaki obligations. Hancock (2011) argued that Ngāti Tūwharetoa was able to obtain a joint management agreement with the Taupō District Council because the iwi was the dominant landowner in the region and these landholdings had been “relatively unchanged by colonialist land takes”.

(Cabinet Office, 2008). Similar requirements also apply to proposed new Orders in Council (Cabinet Office, n.d.).
• **Clear Treaty obligations:** Article Two “confirms and guarantees to the Chiefs and Tribes of New Zealand and to the respective families and individuals thereof the full exclusive and undisturbed possession of their Lands and Estates Forests Fisheries.”

• **Explicit legislative recognition of Māori interests:** Key pieces of environmental legislation – including the Resource Management Act 1991, Hazardous Substances and New Organisms Act 1996, Environmental Protection Authority Act 2011, the Conservation Act 1987 and the Fisheries Act 1996 – require officials or local authority to take account of the principles of the Treaty, establish requirements to consult with Māori, or provide opportunities for Māori to become involved in decision-making and regulatory implementation.

Although official acknowledgement of Māori interests in regulation has grown since the 1980s, questions remain over how best to recognise these interests. Official guidance on how to apply Treaty principles or consult with iwi and hapū is of variable quality, as is the practice of consulting and applying the principles.

The Waitangi Tribunal’s *Ko Aotearoa Tēnei* report explored a number of regimes where concerns have been raised about the adequacy of engagement with Māori and the protection afforded to taonga (see Box 2.2). There has been a rising interest in other taonga – language, education, health etc. – as well as land, water, wahi tapu and other valued flora and fauna. The initial proposal for a joint trans-Tasman therapeutic products regulator failed in part because of concerns from Māori that the new regime could restrict the use of traditional medicines or affect claims to intellectual property rights in traditional medicines (von Tigerstrom, 2007).

**Box 2.2  “Ko Aotearoa Tēnei”: The Waitangi Tribunal’s findings on Māori and regulation**

“Ko Aotearoa Tēnei” is the Waitangi Tribunal’s report on the Wai 262 claim, which dealt with the place of Māori culture, identity and traditional knowledge in New Zealand law and government policy. The report made a number of findings and recommendations relating to regulation.

- **Intellectual property (IP):** The Tribunal concluded that New Zealand’s IP regulations did not sufficiently protect “the Māori Treaty interest in matauranga Māori, taonga works and taonga-derived works”. “Taonga works” are artistic or cultural works that are significant to an iwi or hapū, because there is a body of inherited knowledge associated with them or they invoke ancestors. “Taonga-derived works” are not significant to the identity of a particular iwi or hapū, but have a recognisably Māori element to them.

The Tribunal found that external parties could acquire IP rights over taonga works and related knowledge with “little or no consideration for kaitiaki interests”. Others could use and control taonga works in offensive ways, without informing or seeking the consent of the relevant iwi. The Tribunal noted that this did not mean that kaitiaki should have veto rights, and there needed to be a balance between the interests of iwi and hapū, artists and businesspeople whose works or trademarks are based on taonga works, and of the wider community. The Tribunal recommended that rights to object to derogatory or offensive uses of taonga works or taonga-derived works be strengthened, and that a commission be established to consider these objections, provide guidance on the use of such works and maintain a register of specific cultural works.

- **Genetic and biological resources:** The Tribunal found that current IP laws did not recognise the relationship that iwi and hapū have with taonga species, or the traditional knowledge associated with them. “Taonga species” are flora and fauna that are significant to the culture or identity of an iwi or hapū (for example, through a whakapapa relationship, a body of inherited knowledge, or an iwi or hapū’s obligation to act as their kaitiaki). The Tribunal recommended that the Hazardous Substances and New Organisms Act be amended to give greater weight to kaitiaki interests in decisions about genetically-modified organisms. They also recommended changes to laws and

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5 Official English translation.
processes related to patent and plant variety rights, including giving the Commissioner of Patents the power to refuse patents that unduly disrupted kaitiaki relationships with taonga species.

- **Resource management**: The Tribunal found that while the Resource Management Act (RMA) provided a means for balancing competing interests in the environment, its implementation only rarely supported kaitiaki control over taonga. They recommended changes to the RMA to make it easier to delegate decision-making powers to, and establish partnerships with, iwi.

- **International instruments (such as treaties)**: The Tribunal concluded that while the Crown had the right to represent New Zealand internationally and develop foreign policies, in doing so it had a Treaty obligation to actively protect Māori interests in taonga. Where treaties covered matters of core importance to Māori, the Crown should go beyond consultation with iwi and seek consensus or negotiated agreement. The Tribunal made a number of recommendations to improve Crown engagement with Māori over international instruments and the ability of Māori to participate.

The Government has not yet formally responded to “Ko Aotearoa Tēnei”.


There is often a mismatch between the requirements of the regulatory system and the ability of Māori participants to meet them. This was one of the findings of the Commission’s recent inquiry into local government regulation. The Commission recommended that local authorities work to improve the quality of regulatory decision making by establishing appropriate “secondary rules” about who decides on what, when and how; supporting Māori decision makers with appropriate provisions for tikanga Māori in rules and plans; and providing appropriate legal backstops and safeguards (NZPC, 2013a).

### A regulatory system increasingly shaped by international standards

New Zealand’s domestic regulation is increasingly being shaped by international laws and standards, as a result both of deliberate choices of New Zealand governments and global developments.

Kenneth Keith stated in 2004 that “New Zealand surveys of the Statute Book have concluded that about 200 of the approximately 600 public statutes appear to raise issues concerning New Zealand’s international rights and obligations” (Keith, 2004). The Legislation Advisory Committee’s guidelines note:

New Zealand is party to around 900 multilateral and 1,400 bilateral treaties. It has about 700 Acts in force, of which 92 expressly refer to treaties, either specifically or generally. Fifty-one of these Acts refer to specified treaties, of which all but 4 are multilateral. These 51 Acts implement 99 different treaties, in whole or in part (20 deal with more than 1 treaty and several deal with an aspect of the same treaty). Fifty-three of these treaties are set out in schedules to their respective Acts and 2 are set out in schedules to their respective regulations. … These numbers seem small relative to the number of treaties that apply to New Zealand. However, the 92 Acts contain 32 general references to all treaties to which New Zealand is a party and 30 general references to all treaties on a particular subject to which New Zealand is a party. These Acts also do not include those Acts that implement treaties without referring to them in any way. (Legislation Advisory Committee, 2012)

Treaties are not the only vehicle through which international standards affect New Zealand regulation. As noted in the inquiry Issues Paper, other means include unilateral adoption, unilateral recognition, mutual recognition, harmonisation and joint regulation (NZPC, 2013b, pp. 13-14).

### Drivers of regulatory globalisation

Three main factors are driving the globalisation of New Zealand regulation. The first is New Zealand’s long-standing commitment to be a good international citizen, and to ensure that New Zealand laws reflect global norms. The expectations of what “good international citizens” should do have increased over time and cover an increasingly wide range of fields and activities. This rise in expectations reflects increasing global interdependence and a growing awareness that some risks are trans-national (for example, infectious diseases, climate change, financial market shocks, and terrorism) and require international collaboration and coordination (Kingsbury, Krisch & Stewart, 2005). In addition, technological developments (such as digital
and internet-based trading) are increasingly integrating markets, leading governments to cooperate over issues such as standards and tax regimes.

The second factor is New Zealand’s small population. In many industries, the centres of expertise and technical capability lie offshore. In these cases, it can be more efficient to adopt or share international standards and rules. Capability constraints in New Zealand, particularly in terms of attracting and retaining specialised skills, were a key motivation behind the proposal to establish a joint Australia and New Zealand therapeutic goods regulator (von Tigerstrom, 2007).

The third is a concerted effort by successive administrations to use regulatory harmonisation to improve New Zealand’s access to foreign markets and exposure to competition from international trade. Key milestones in this effort are noted below.

- The Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) came into force on 1 January 1983. Subsequent protocols have deepened and expanded economic integration between the two countries, and, in several cases, New Zealand has deliberately modelled its own regulatory regimes on Australian models. For example, the Commerce Act 1986 and Fair Trading Act 1986 were based on Australia’s Trade Practices Act 1974. The aim was to have laws that were comparable to those of New Zealand’s major trading partners so as to reduce unnecessary barriers to trade and competition (Ministry of Consumer Affairs, 2010; Ahdar, 1991).

- New Zealand’s active participation in the Uruguay Round of international trade negotiations (1986-94) concluded with revisions to the General Agreement on Tariffs and Trade, agreement to a General Agreement on Trade in Services and the establishment of the World Trade Organization (WTO). As a result of this active participation, New Zealanders continue to play a prominent role in WTO panels and dispute resolution mechanisms, and other international organisations of importance to New Zealand’s wellbeing (for example, the World Organisation for Animal Health).

- A number of bilateral and multilateral trade agreements have been successfully completed over the first decade of the 21st century, and negotiations are continuing on a number of others.

How international standards affect domestic regulation

International agreements and foreign rules and standards are reflected in New Zealand regulation in a number of ways. In some cases, the agreements may limit the scope of domestic regulation or oblige New Zealand to carry out specific activities. For example, WTO agreements require that New Zealand governments give citizens of other member countries the same treatment as New Zealanders (“national treatment”) and do not discriminate between trading partners (“Most Favoured Nation”). The Free Trade Agreement with China constrains the ability of the New Zealand and Chinese governments to expropriate the property of each other’s citizens, and creates a right for aggrieved investors to be compensated for losses or seek redress through an international tribunal.

Other international arrangements create obligations for New Zealand’s domestic regulatory regimes. As a signatory to the 1944 Convention on International Aviation, New Zealand is obliged to comply with the International Civil Aviation Organization’s (ICAO) standards and recommended practices on global aviation, unless it is impracticable to do so. Where New Zealand’s domestic rules vary from ICAO’s standards and practices, New Zealand must report this to ICAO.

Overseas standards can be reflected in New Zealand regulation, either as the equivalent of New Zealand standards or as the basis for New Zealand standards. Following a deal agreed in 2005, New Zealand recognises test reports and product certification of electrical and electronic products carried out in Taiwan (and vice versa). Similar arrangements are in place with China and the European Union. Mutual recognition systems play an important part in ensuring that New Zealand exporters in other sectors (for example in the agricultural sector) can access foreign markets.

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6 General Agreement on Tariffs and Trade, General Agreement on Trade in Services, Agreement on Technical Barriers to Trade, Agreement on Sanitary and Phytosanitary Measures, Agreement on Trade-Related Aspects of Intellectual Property Rights.
Although adopting international regulatory standards imposes duties on New Zealand authorities, they also provide benefits to New Zealand citizens and firms. The WTO agreements have reduced barriers to New Zealand selling its products overseas, and provide protection against arbitrary or discriminatory barriers being re-imposed in the future. They also provide mechanisms of redress for countries who have been subjected to discriminatory treatment. Such protections and mechanisms are critically important for small trading countries like New Zealand. In addition, while international travel regulatory systems (like those operated by ICAO or the International Maritime Organisations) impose obligations on New Zealand agencies, compliance with these systems allows New Zealanders to easily travel and to trade, and enables foreigners to visit New Zealand.

**Challenges**

The use of international regulatory systems or standards provides significant benefits for New Zealanders, but it can also create challenges.

The benefits of adopting overseas standards may be concentrated in a small number of firms (for example, exporters, or businesses that have premises in more than one jurisdiction), with costs spread across the wider community (Quigley, 2003). New Zealand may lack the capability required to effectively run a system designed for a larger market. Introducing foreign systems into New Zealand without suitable modifications could either leave activities not appropriately controlled or impose undue costs on the community.

The Council of Trade Unions expressed concerns that some forms of global regulation could constrain New Zealand’s “freedom to regulate and to change regulatory approaches as we learn from experience” and cited investor-state dispute mechanisms in international trade agreements as tools that could act as a barrier to regulatory change (sub. 25, pp. 9-10). Physicians and Scientists for Global Responsibility shared these concerns, stating that the “potential for trade agreements or other agreements aimed to enable trade, or build ‘harmonisation’ is a serious risk to New Zealand being able to regulate effectively for its own national local-level interests” (sub. 3, p. 5).

The key challenge for governments is to assess whether and when the benefits of harmonisation (for example, higher productivity arising from greater competition, lower trade barriers, higher investment or the expansion of more efficient firms) outweigh the costs of constrained sovereignty.

**New Zealand is not simply a “taker” of foreign regulation**

Due to the country’s small population, New Zealand is often thought of as a “policy taker” when it comes to international regulatory systems. It is true that New Zealand does not have the resources to participate in all international fora that develop regulatory systems and standards. And even where resources are available, New Zealand is generally only one voice among many. However, a number of regulators (for example, the Civil Aviation Authority, Ministry for Primary Industries) and other New Zealand agencies (especially the Ministry of Foreign Affairs and Trade) are active in international organisations and seek to shape the design of international standards where inappropriate approaches could create significant costs for New Zealand. In some cases, active involvement in international fora has helped to reduce unnecessary barriers and costs for New Zealand firms (see, for example, Meat Industry Association, sub. 40, pp. 5-6).

**2.4 Both internationally respected and unstable?**

New Zealand is notable for having regulatory regimes that score highly on numerous international measures of quality, while also being the subject of criticism for instability and inconsistency.

**Bouquets…..**

New Zealand generally scores very highly in international comparisons of business environments, such as those run by the World Economic Forum, World Bank, Grant Thornton, Transparency International and the World Justice Project. These surveys generally find that New Zealand provides a high degree of protection and certainty for business and investors (see Box 2.3).
On the other hand, New Zealand’s regulatory system has been described as having a “significant degree of inconsistency in the extent to which policy settings are supportive of competition” and according to Conway (2011), this inconsistency “has been escalating in New Zealand”:
Although policy inconsistency typically increases at the beginning of reform programmes, this should subsequently reverse as reforms become entrenched and applied more uniformly across the board. In contrast to a number of comparator countries, this period of regulatory consolidation has yet to occur in New Zealand, indicating an unfinished reform agenda. (p. 16)

During the course of this inquiry, there was considerable discussion in the media about the stability of New Zealand regulatory regimes, especially following the Commerce Commission’s decisions on the pricing of broadband on Chorus’ copper network and credit rating decisions for several regulated utilities. Affected firms cited assessments by organisations such as Standard and Poor’s that New Zealand’s regulatory regime “is less stable than other regimes internationally and they see it as a higher risk” (Vector, 2013).

Similar themes emerged from submissions. Vector quoted statements from credit ratings agencies that “regulatory uncertainty and subjectivity remains endemic” in New Zealand and that “uncertainties surrounding the regulatory framework” were offsetting the company’s strengths (sub. 36, p. 24). Chorus similarly quoted comments from equity analysts, questioning whether New Zealand was now “the land of the long regulatory cloud” and asking if it was “time for international investors to abandon New Zealand?” (sub. 51, p. 2). The New Zealand Council for Infrastructure Development expressed concerns “that the risks involved in building and operating network infrastructure, principally electricity, gas, fibre, copper and mobile infrastructure, are unnecessarily high and having a detrimental effect on the delivery of world class infrastructure for New Zealanders” (sub. 34, p. 2).

### Regulatory uncertainty

Underpinning these comments is the concept of regulatory uncertainty – that is, the idea that unexpected changes in regulatory settings, implementation or enforcement can discourage investment. This can be the case particularly in sectors where assets are expensive, have long lives and are specific to the industry (that is, because they are of little use to other firms, they cannot be easily sold to recover capital). Without some confidence over the security of their revenue (which can be affected by regulatory decisions over prices), firms may see investing in replacement or new assets as too risky. Academic work on regulatory uncertainty therefore often focuses on mechanisms to constrain the scope for unexpected changes and provide “regulatory commitment” (see, for example, Levy & Spiller, 1994).

Empirical studies provide mixed messages about the impact of uncertainty on investment incentives. On one hand, Bittlingmayer (2001) found that aggressive competition policy enforcement, and the resulting policy uncertainty, contributed to low investment in affected industries over the 1950s and 1960s. Kelly, Sullivan and Reich (2013) posited that increased uncertainty in US energy markets, arising from new and unclear enforcement powers being given to a federal regulator, had led to firms leaving the market.

However, a statistical analysis by Cox (2012) of stock prices following the announcement of new financial market regulations found “insufficient evidence to support claims of significant economic consequences from regulatory uncertainty”. The analysis by Hoffman, Trautmann and Hamprecht (2009) of German power company investment responses to the European emissions trading scheme concluded that “regulatory uncertainty does not necessarily lead to postponement of investment decisions and can, in fact, even accelerate investment decisions”.

The Commission has not attempted to conduct a detailed study of the relative state of regulatory uncertainty in New Zealand. Data constraints, among other factors, preclude such a study. However, in the course of the inquiry, the Commission sought comment and evidence about the nature and extent of uncertainty in New Zealand, including from credit ratings agencies. A few indicative conclusions can be drawn from this process.

### New Zealand institutions are not perceived as being fundamentally weak

Standard and Poor’s commented in its assessment of New Zealand’s banking industry that the policy environment is

stable and predictable, supported by deep and mature policy-making institutions and an effective judiciary and independent media. The New Zealand civil service has a long and strong record of effective policy development and implementation. The system has also demonstrated resilience and adaptability in the face of strong pressures. (Standard and Poor’s, 2012)
Transparency International also assessed New Zealand’s political and legal institutions favourably, although it noted that political pressure on the independence of the public service had increased (Transparency International New Zealand, 2013).

**Uncertainty appears to be concentrated in specific sectors**

Discussions with ratings agencies indicated that the perceived risk of New Zealand industries varied considerably. For example, banking was seen as a generally lower risk, insurance as a slightly higher risk, and utilities higher again. Standard and Poor’s assessment of the banking sector noted “strong … banking regulation and supervision” and “regulations [that] are more conservative than the international standards” (Standard and Poor’s, 2012). In comparison, New Zealand regulated utilities were assessed by Standard and Poor’s as having higher risk than equivalent sectors overseas.

**There are examples of uncertainty caused by political decisions, but they are not common**

There have been cases where ministerial decisions have created uncertainty over the longevity or direction of New Zealand regulatory regimes. One example is the 2008 introduction of government regulations tightening the screening criteria for overseas investment applications, and the subsequent rejection by ministers of an Overseas Investment Office recommendation to approve a Canadian pension fund purchasing shares in Auckland International Airport. This decision was the subject of considerable debate (for example, Chapman Tripp, 2009, Simpson Grierson, 2008a and 2008b), with Parliament’s Regulations Review Committee concluding that the Regulations were “an unusual and unexpected use of the regulation-making power” (Regulations Review Committee, 2008). Such cases are unusual however, and their prominence in public debate perhaps reflects this.

**Repeated change in underlying regulatory settings is a major cause of uncertainty**

Frequent changes in underlying legislation are a significant driver of uncertainty. This point was made to the Commission in its engagements with ratings agencies; although New Zealand economic regulatory regimes are generally sound, many are also relatively new (see, for example, Standard and Poor’s, 2013). In electricity and telecommunications in particular, regulatory regimes have been subject to repeated and significant change. Minter Ellison Rudd Watts commented that the “electricity sector has had various self-regulatory arrangements, followed by the Electricity Commission and then the Electricity Authority. This pattern of change to institutional form in the electricity sector looks likely to continue” (sub. 28, p. 29). Scott and de Joux (2013) described government involvement in the telecommunications sector as an “unplanned evolution”:

> It features a strong wave of liberalisation and privatisation, with minimal regulation becoming more and more stringent as dysfunctions appear. It shows a deregulated market, controlled first by the courts, then by an industry-specific regulator and, within the past decade, a growing government input. Finally, it goes full circle to once again having the government in control to a large extent of the telecommunications infrastructure. (pp. 1-2)

Mladenovic (2011) noted the “constant reviews of and changes to regulatory regimes [governing electricity and telecommunications] that have been carried out during the last quarter century” (p. 364).

One key criterion that rating agencies use to assess risk is “consistency in the regulatory framework over time”, particularly with regards to decisions over the pricing of regulated firms. In other countries, regulated utilities have been through several cycles of re-setting prices, allowing investors and rating agencies to gain confidence about the consistent application of regulation over time. By comparison, New Zealand is still in the process of bedding in its first set of regulated prices and information disclosure requirements for lines companies, gas pipeline firms and airports. Repeated changes to underlying frameworks in New Zealand have therefore contributed to relatively poor risk ratings for some New Zealand industries.

**Not all regulatory uncertainty is bad; what matters is its source**

Some degree of uncertainty in regulatory systems is inevitable and can be desirable. As Willis (2012) comments:

> It is worth emphasising that regulatory uncertainty is, to an extent, a necessary and desirable feature of all principled regulatory processes and regulatory regimes. It is excessive or unnecessary uncertainty...
that represents a genuine policy issue and which ought to be mitigated. Regulatory uncertainty is the result of regulatory discretion and, within certain limits, regulatory discretion is desirable. Regulatory discretion promotes flexible regulation responsive to the dynamic commercial and political context in which regulation is required to function. (p. 232)

In some circumstances, regulators need room to apply their regimes to new cases and circumstances; otherwise they may fail to achieve their objectives and reduce public harms.\(^7\)

Unforeseen changes to underlying regulatory frameworks by ministers or Parliament are a more problematic source of uncertainty. While the exercise of regulator discretion is generally subject to oversight and, where necessary, correction (for example, through the courts), Parliament is supreme in the New Zealand constitutional system. As a result, sudden or dramatic changes in legislative direction can undermine investor confidence in the stability of regulation and the security of their returns. Mighty River Power cited former Australian Minister for Resources and Energy, the Hon Martin Ferguson, on the benefits of consistent and measured change:

> The focus of reform should be on a process of continuous learning rather than throwing the rule book out at the first sign of trouble. The pace of reform may frustrate commentators but they should appreciate that the legitimacy and quality of policy outcomes ultimately depend on proper process being observed. (sub. 30, p. 8)

Tensions between regulatory regimes and political imperatives are common worldwide. The challenge is to design regulatory systems that allow political pressure to be released, without needing to fundamentally overhaul the entire system. This matter is considered in more detail later in the report.

### 2.5 Systemic themes in New Zealand regulation

New Zealand does not have a unique approach to regulation. But the features outlined above mean that there are some systemic themes in New Zealand regulation.

- A number of important regulatory regimes in New Zealand are young and are still settling down. Electricity and telecommunications are the most prominent examples. This has created perceptions of risk and contributed to perceptions of wider instability.

- Regulatory regimes in New Zealand can easily become rigid and obsolete. Heavy reliance on statutes, scarce parliamentary time and the weakness of many checks and balances and agency evaluation cultures mean that it can be difficult to change or update regulatory systems in the absence of a crisis. This puts pressure on agencies working with obsolete laws, and limits the ability of New Zealand regulation to keep up with changes in technology or public expectations.

- New Zealand has introduced different regulatory models across similar issues, rather than applying a coherent and consistent approach. For example, as Vodafone noted, “the approach to regulating prices in the telecommunications sectors differs substantially from the approach to regulating prices in the electricity or airports sectors, and again from that which applies to the dairy industry” (sub. 46, pp. 3-4). The absence of a common framework limits the ability of New Zealand regulators to learn from experience in related sectors and to build up a “jurisprudence” of principles, rules and decisions that can be applied to similar circumstances across different regimes. It may also increase compliance costs for firms, especially those that operate across multiple regulatory regimes.

- Official acknowledgement of Māori interests in regulation has increased since the 1980s. Even so, questions remain about how best to recognise Māori interests and about mechanisms for ensuring Māori can participate effectively in regulatory implementation. Appropriate application of Treaty principles to regulatory systems are still developing.

The recommendations in this report aim to address these themes, and other barriers to the effective design and implementation of regulation in New Zealand.

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\(^7\) The issue of when to give regulators discretion, and how much discretion to confer, is considered in Chapter 6.
3 Understanding the regulatory system

Key points

- Maps and groupings are valuable as a way to understand regulatory regimes and agencies, but mainly as a first step in a more detailed analysis. For most regimes, further disaggregation is likely to be needed to gain a full understanding of their dynamics, relationships and differences.

- No single set of categories will support all avenues of analysis into how regulatory regimes perform. A range of frameworks can be applied that answer different questions and lead to different combinations of agencies and regimes.

- In responding to the inquiry Terms of Reference, the Commission has sought to improve the ability of policy advisers to:
  - construct maps and groupings that suit their particular lines of research and analysis into regulatory performance; and
  - design new regulatory regimes, by classifying and grouping regulatory institutions and practices.

- The lack of regular and detailed reporting on the state of New Zealand regulators and regulation is a key gap in the current regulatory management system.

- More comprehensive and comparable information on New Zealand regulators should be collected to help offset barriers to identifying and making systemic improvements to regulatory practice. In particular, such information could:
  - help designers of regulation compare and contrast regulatory approaches and features;
  - help regulators identify better practice among their peers that they might adopt in their operations; and
  - be used to identify trends or patterns in implementing regulation or the performance of regulators, regimes that need review, or agencies where closer oversight is required.

- Standardised reporting on regulatory activity and impacts should be embedded into existing accountability processes, such as agency annual reports. The Treasury and the State Services Commission, as the central agencies responsible for the public sector accountability framework, should be responsible for developing standardised reporting requirements for annual reports.

- Standardised reporting requirements should be designed to allow analysis of the structure, efficiency, effectiveness, responsiveness, scope of activity, burden of activity on regulated parties, and transparency and accountability of New Zealand regulators.

- Information from standardised reporting could be formally integrated into the Treasury’s regulatory management and evaluation systems. In particular, it could be used to find any parts of the regulatory system that need improving, and underpin policies to make those improvements.

3.1 Introduction

As part of the Terms of Reference for this inquiry, the Commission was tasked with developing:

- “a high-level map of regulatory regimes and regulators across central government, including their organisational form”; and
This chapter discusses:

- submitter feedback on the indicative maps that the Commission publishes in its Issues Paper;
- the benefits and limitations of regulatory groupings and maps;
- the need for better information to categorise and compare regulators; and
- options for collecting and using better information on regulatory activities and impacts.

### 3.2 Feedback on the indicative maps in the Issues Paper

The Commission outlined two indicative groupings of regulators in its Issues Paper. The first group was based on the type of organisation carrying out regulatory functions (such as public service departments, Crown agents, Independent and Autonomous Crown Entities), and the other group was based on the broad subject area (such as economic, environmental, or social) that the regulatory regime covered (NZPC, 2013b, pp. 16-17).

Some submitters saw merit in the indicative groupings. Vector welcomed the approach taken in the Issues Paper, but added extra categories to provide more granularity. In the subject matter groupings, Vector proposed four high-level subjects (economic regulation of markets, social regulation, environmental regulation, and international trade and tariffs regulation) and a series of subheadings under the subjects (sub. 29, pp. 7-17). The Vector categories are reproduced below (see Figure 3.1).

Other submitters also recommended modifying the Commission’s frameworks by adding categories. The Reserve Bank of New Zealand proposed adding a “health and financial” grouping to avoid “too rigid” demarcations (sub. 9, p. 2). Internet New Zealand considered “that critical infrastructure services are substantially different to other commercial businesses and regulation of those infrastructure services requires particular care and attention” (sub. 45, p. 6).

Another group of submitters proposed different frameworks for classifying regulatory agencies and regimes.

- Molly Melhuish proposed a graphical typology based on “democratic influence in design, ranging from democratic to autocratic” and “regulatory complexity, scaled to the size (perhaps measured as GDP) of the sector” (sub. 42, pp. 3-4, 6-8).
- Aviation New Zealand said that regulatory regimes could be grouped according to the “risks being treated e.g. all safety regulatory risks could be grouped as their objective is treatment of harm and hazards to individuals” (sub. 36, p. 5).
- The Civil Aviation Authority noted that regulatory authorities could be categorised by organisational status; “Activity (service delivery; regulatory compliance; trading; or a mix of two or more of those activities); Sectoral span (e.g. aviation or marine, or aviation and marine); or Regulatory objective (e.g. safety, or security, or economic, or social, or a mix of two or more of those)” (sub. 6, p. 11).
- The Compliance Common Capability Programme noted that:

  it may be helpful to categorise regulatory regimes according to the domestic, bilateral or multilateral/international nature of the drivers of regulation. This would be helpful as in areas such as maritime law, where NZ is “signed up” to the IMO decision making process, having a situation where a full policy process is required to turn internationally agreed mandatory requirements into NZ law is inefficient and costly. Categorisation in this way might highlight opportunities for efficiencies across a category of regulators. (sub. 12, p. 8)

- ANZ Bank Ltd argued that it “is more important to focus on the function of different regulatory regimes, rather than their subject matter...For example, prudential and market conduct regulation of financial...
markets have the same subject matter (financial markets) but promote quite different regulatory objectives” (sub. 24, p. 10).

3.3 Benefits and limitations of regulatory groups and maps

The variety of submitter responses to the Commission’s indicative maps highlights the benefits and limitations of such exercises. In brief, maps can help to break down system-level complexity, but on their own they may oversimplify regulatory regimes and agencies. In doing so, they may not give a complete picture (and so understanding) of the benefits and limitations.

Benefits

The ability to understand the scale and impact of regulatory activity, and to compare, contrast and assess regulatory regimes has been constrained by the:

- growing volume of regulation and regulatory activity; and
- diversity of approaches taken to the design and implementation of regulatory regimes.

Grouping regimes or agencies into categories can help break down this volume and diversity into more manageable units of analysis. This can let advisers and policymakers reveal activities with a common purpose, identify patterns and relationships, compare and contrast regimes and approaches, reveal gaps between regimes, and help to identify benchmarks.

In other jurisdictions, thematic or sectoral groupings of regulatory agencies and regimes have helped governments to identify and reduce duplicated burdens on regulated firms by rationalising regulators. For example, businessman Philip Hampton led a review of British inspection and enforcement practices that proposed consolidating 31 agencies down into 7 organisations. Those organisations were to be based around the themes of consumer protection and trading standards, health and safety, food standards, environmental protection, rural and countryside issues, agricultural inspection, and animal health (Hampton 2005, p. 64). By grouping agencies around these themes, the review aimed to reduce the number of required interfaces between business and regulator, promote better risk assessment, eliminate multiple inspections, internalise conflicts and reduce duplication (Hampton, pp. 63-64).8

Similarly, the Victorian State Services Authority recommended rationalising 32 State regulators down to 8, based on the thematic or sectoral categories of education, the built environment, health, workplace safety, wildlife and fisheries, consumer protection and essential services, food and biosecurity, and integrity.9 (VSSA 2009)

Limitations

High-level maps can involve significant degrees of aggregation or simplification, to the point where important nuances can be lost, reducing the explanatory power and so the classification’s usefulness. Thematic groupings may not effectively categorise regulatory regimes with purposes that cross themes. Maritime New Zealand questioned the value of the thematic groupings outlined in the Commission’s Issues Paper, commenting that it “might provide a helpful basis to distinguish regulatory regimes, but as many sit across the proposed subject area it is unclear what purpose such a grouping would serve” (sub. 15, p. 4). In addition, the Civil Aviation Authority argued that thematic groupings may create a misleading picture of uniformity:

The transport sector (e.g. rail, land, air, maritime) regulations are not homogenous to the extent that might be imagined. Civil aviation and maritime have broad similarities (e.g. similar international regulatory frameworks, broadly similar domestic regulatory frameworks, etc) but have quite different characteristics in a technical sense (aviation and maritime engineering, navigation etc, whilst conceptually similar in some ways, are very different). In reality, the transport sector is a set of systems

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8 Many, but not all, of the mergers proposed by Hampton took place.
9 “Integrity” covered liquor, gambling, prostitution and racing regulation.
that have elements/degrees of overlap and congruence – it is not all that obvious that categorization by theme (e.g. transport) would add much in the way of value or insight. (sub. 6, p. 11)

Other submitters highlighted the pitfalls inherent in trying to categorise regulators or regimes. Tasman District Council commented that there “will inevitably be differences in the nature and scope, structure and focus of regulations between and within the areas identified that would mean that it is going to be difficult to come up with a typology for which uniform design and operation principles could be established” (sub. 1, p. 2).

The Council of Trade Unions noted “the great variety of regulators and the very different contexts in which they work” and concluded that it “is likely to be futile to attempt to categorise them too tightly, let alone try to do so in a legal or institutional sense which is likely in fact to be counterproductive and damaging” (sub. 25, pp. 10-11). And Minter Ellison Rudd Watts commented that regulatory institutions “and their practices are often considered at arms’ length and at a high level. However, the best lessons are sometimes learned from a ‘deep dive’ into particular regulatory structures” (sub. 28, p. 3).

One response to the problems of oversimplification is to develop more detailed classifications, to reflect the nuances and differences between regimes. For example, Hood, Rothstein and Baldwin (2001) developed a tiered framework based around:

- the types of risk being managed;
- public preferences and attitudes around the need for regulation;
- whether organised interests are present in the regulated industry;
- the size of the regulatory regime;
- the structure of the regulatory regime; and
- the regulatory style applied.

Lawrence, Simmons and Vass (2002) developed a framework for the British regulatory system that explored the institutional responsibilities and relationships (such as the form of oversight, level of independence from ministers, and review and audit processes) of the different types of agencies.

### 3.4 A way forward

The issues identified with maps and groupings in submissions and literature (as noted above) point to two conclusions:

- Maps and groupings are valuable as a way to understand regulatory regimes and agencies, but mainly as a first step in a more detailed analysis. For most regimes, further disaggregation is likely to be needed to gain a full understanding of their dynamics, relationships and differences. As Hood et al comment:

  > How we use the idea of regime anatomy as a method of comparing types of regulation depends on what we are applying it to and what we are using it for. The more similar the systems being compared, the further down the scale of disaggregation the comparison will need to go if their distinctive fingerprints are to be identified… How far we need to disaggregate regimes to greater levels of complexity also depends on how many ‘degrees of freedom’ there are in regulatory regimes – that is, how far variation in one element of a regime is linked to variation in another, or how far we can predict what one dimension of a regulatory regime will be like from knowledge about another dimension. If there are infinite degrees of freedom in regulatory regimes, we need very complex ways of describing and comparing them; if there are only a few degrees of freedom, a parsimonious characterization will suffice. (Hood, Rothstein & Baldwin 2001, p. 35)

- No single set of categories will support all avenues of analysis into how regulatory regimes perform. As the submission responses to the indicative maps in the Issues Paper indicate, a range of frameworks can be applied that answer different questions and lead to different combinations of agencies and regimes.
Maps and groupings are perhaps best thought of as initial hypotheses for research and analysis. As noted above, clustering regimes or agencies together is one way to explore patterns or relationships in behaviour. Clusters of regimes or agencies could be designed to test whether particular patterns or relationships exist and, if so, how strong they are. For example, in considering the relative efficiency of regulators (for example, the unit costs of common activities such as the issuing of licences), agencies could be grouped by their size (for example, by total FTEs or total expenditure on regulatory activities). Then the economies of scale in New Zealand regulators (if any) could be assessed. Alternatively, agencies could be grouped by the number of regimes they implement, to assess whether economies of scope exist. To properly test the hypothesis in either option, the analysis would need to proceed below the level of regime or agency.

From these conclusions, the Commission has not continued to develop the indicative maps from the Issues Paper. Instead, the Commission has focused on two actions.

- Creating the conditions to let advisers or policymakers build maps and groupings that suit their lines of regulatory research and analysis. The main barrier to achieving this is better and more comparable information on regulatory activity and impacts. The Commission’s recommendations on how to gather better information are set out in Section 3.5 and Section 3.6.

- Developing groups of regulatory institutions and practices, to help system-wide analysis and the design of new regulatory regimes.

Maps and groupings are valuable as a way to understand regulatory regimes and agencies, but mainly as a first step in a more detailed analysis. For most regimes, further disaggregation is likely to be needed to gain a full understanding of their dynamics, relationships and differences.

No single set of categories will support all avenues of analysis into how regulatory regimes perform. A range of frameworks can be applied that answer different questions and lead to different combinations of agencies and regimes.

**Categorising regulatory institutions and practices**

The Commission focused on unpacking and classifying the key institutional arrangements and practices that have a bearing on the incentives on regulators and regulatory efficiency and effectiveness. More “fine-grained” groupings at this level can help officials and policymakers understand when specific approaches (such as those focused on enforcement, or on engaging with regulated parties) would be most suitable. During its inquiry, the Commission has developed a number of such groupings.

- Chapter 4 outlines a typology of regulatory standards
- Chapter 7 provides typologies for analysing organisational cultures.
- Chapter 8 groups (by type of engagement mechanism used) the various statutory requirements to consult that regulators face.
- Chapter 9 explains that some regulators have Treaty clauses in their statutes, and that the phrasing of these creates different obligations.
- Chapter 10 categorises the different forms of review and appeals mechanisms available in New Zealand’s regulatory regimes.
- Chapter 11 outlines the different types of compliance and enforcement strategies used by regulators
Figure 3.1  Grouping of regulatory regimes proposed by Vector

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<thead>
<tr>
<th>Economic markets regulation</th>
<th>Social regulation</th>
<th>Environmental regulation</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Electricity Authority (Electricity Industry Act 2010)</td>
<td>• Ministry of Transport (Land Transport Management Act 2003)</td>
<td>• Ministry for Primary Industries (Fisheries Act 1996)</td>
</tr>
<tr>
<td>• Takeovers Panel (Takeovers Act 1993)</td>
<td>• Ministry of Civil Defence and Emergency Management (Civil Defence Emergency Management Act 2002)</td>
<td>• Local and regional authorities (Resource Management Act 1991)</td>
</tr>
<tr>
<td></td>
<td>• Health and Disability Commissioner (Health and Disability Commissioner Act 1994)</td>
<td>• Ministry for Primary Industries (Biosecurity Act 1993)</td>
</tr>
<tr>
<td></td>
<td>• Ministry of Business, innovation and Employment (Building Act 2004)</td>
<td></td>
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<td></td>
<td>• Civil Aviation Authority (Civil Aviation Act 1990)</td>
<td></td>
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<td></td>
<td>• Ministry for Primary Industries (Food Act 1981)</td>
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<td></td>
<td>• Local authorities (Building Act 2004)</td>
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<td></td>
<td>• Ministry of Health (Medicines Act 1981)</td>
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<td></td>
<td>• Employment Relations Authority (Employment Relations Act 2001)</td>
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<td></td>
<td>• New Zealand Teachers' Council, Tertiary Education Commission (Education Act 1989)</td>
<td></td>
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<td>• Reserve Bank of New Zealand (Insurance (Prudential Supervision) Act 2010)</td>
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<td>• Gambling Commission (Gambling Act 2003)</td>
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<td></td>
<td>• Department of Internal Affairs (Gambling Act 2003, Films, Videos, and Publications Classification Act 1993)</td>
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<td>• Maritime New Zealand (Maritime Transport Act 1994)</td>
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<tr>
<td>Economic regulation of infrastructure</td>
<td>Health and safety</td>
<td>Resources</td>
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<tr>
<td>Other economic</td>
<td>Occupational</td>
<td>Hazards</td>
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<td>Conservation</td>
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<tr>
<td></td>
<td></td>
<td>Other environments</td>
</tr>
</tbody>
</table>

10 Note: the CAA has some competition functions, but its predominant focus is the safety of New Zealand’s aviation system.
3.5 Better information to drive system-wide improvements

Groupings and maps of regulatory agencies and regimes require good information. New Zealand’s current regulatory management system lacks comprehensive and detailed reporting on the state of New Zealand regulators and regulation. The lack of data on regulatory activity compares poorly with fiscal management processes, which (among other things):

- provide policymakers and the community with a full picture of the government’s revenue and expenses, for “informed and focused debate about fiscal policy” (New Zealand Treasury, 1996, p.11);
- encourage policymakers to set and implement clear strategies, and enables Parliament and the community to assess their performance in carrying out those strategies; and
- allow policymakers, Parliament and others to compare and contrast different areas of expenditure.

It is not surprising that New Zealand lacks equivalent reporting on regulation. Budgeting and spending use a common measure (such as dollars and cents) and are subject to an independent and objective set of standards (Generally-Accepted Accounting Principles). But “an accounting” of regulatory activity and impacts requires a broader array of measures, to reflect the diversity of regulatory regimes and approaches.

Also, compiling a full list of regulators and their activity is challenging. An attempt to prepare a list of British regulators in 2003 led the Better Regulation Taskforce to question “whether even Ministers could be certain that they know of all the independent regulators that surround their Departments” (BRTF 2003). Similarly, Julia Black (2012) observed:

> Successive attempts have been made by organisations such as the Better Regulation Taskforce, or indeed by Parliamentary Select Committees, to ‘map’ the organisational landscape of regulation but the task can exhaust even the most dedicated cartographers. (p. 7)

Even so, scope exists to significantly improve the quality and comparability of regulatory performance information. The Australian Productivity Commission (APC) and the Victorian Competition and Efficiency Commission (VCEC) have demonstrated such scope (see Box 3.1).

**Box 3.1 Australian studies of regulators**

**Australian Productivity Commission**
The APC has carried out a number of inquiries or research projects on specific practices of Australian regulators. Recent examples include the 2013 report on regulator engagement with small business; the 2012 performance benchmarking report into local government regulators; the 2011 performance benchmarking report on planning, zoning and development assessment; the 2010 report on occupational health and safety regulation; and the 2009 report into food safety regulation. In each report, the APC collected evidence about regulator practices, compared and contrasted these practices, and (where possible) assessed them against best practice criteria.

**Victorian Competition and Efficiency Commission**
VCEC has produced regular reports on State regulation and regulators since the Commission was founded in 2004. “The Victorian Regulatory System” report describes in detail each regulator in Victoria, including:

- the regulatory objectives that each regulator must seek to achieve;
- the number of Acts, regulations and other legislative or guidance instruments that each regulator enforces;
- the volume and type of enforcement activities of each regulator in the last year;
- its revenue, expenditure, staff numbers and numbers of licensed parties;
The Commission sees specific benefits from collecting and publishing more comprehensive and comparable data on the arrangements and practices of regulators. The information could enable policymakers to:

- better understand and assess the scale of regulatory activity in New Zealand;
- compare and contrast regulatory approaches and features;
- identify trends in implementing regulation or performance of regulators, or identify areas for improvement;
- help regulators identify better practice among their peers that might be adopted in their own operations; and
- provide more informed debate on regulatory matters.

Most benefits from such information are likely to result from revealing to designers, implementers and users of regulation how regimes are being implemented in New Zealand. For example, designers of new regulation would be able to look at how regulators with a similar focus approach issues of engagement or enforcement and develop suitable benchmarks. Regulators (and regulated parties) could use the data to assess how their performance on various aspects (such as the time taken to process a licence) compares with other agencies. Both uses should create incentives for improvement.

At a high level, collecting and publishing more comprehensive information on the New Zealand regulatory system would allow a more strategic approach to regulatory management. In particular it would provide a better empirical basis that ministers and central agencies could use to hold regulators to account and identify regimes where reviews were needed, offsetting weaknesses in the current regulatory management system.11

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11 Regulator accountability and regime review are discussed in Chapters 14 and 15, respectively.
The lack of regular and detailed reporting on the state of New Zealand regulators and regulation is a key gap in the current regulatory management system. The lack of data on regulatory activity compares poorly with fiscal management processes. Those processes promote informed and focused public debate on fiscal policy, encourage governments to focus their actions, and enable comparisons between different areas of the public sector.

More comprehensive and comparable information should be collected on the activities and impacts of New Zealand regulators. Such information could help offset barriers to identifying and making systemic improvements to regulatory practice. In particular, it could:

- help designers of regulation compare and contrast regulatory approaches and features;
- help regulators identify better practice among their peers that might be adopted in their own operations; and
- be used to identify trends or patterns in implementing regulation or the performance of regulators.

Offsetting weaknesses in the regulatory management system

New Zealand’s current regulatory management system is highly devolved. Departments have the primary “ongoing, practical responsibility for oversight of regulation” (Offices of the Ministers of Finance and Regulatory Reform 2013b), including responsibility to:

- conduct “independent quality assurance” on regulatory impacts statements (RIS) that departmental staff produce (New Zealand Treasury, 2013b, p. 1.10);
- monitor, and assess “at appropriate intervals, the performance and condition of their regulatory regimes to ensure they are, and will remain, fit for purpose” (Offices of the Ministers of Finance and Regulatory Reform 2013b);
- have processes in place to “identify and evaluate, and where appropriate report or act on, problems, vulnerabilities and opportunities for improvement in the design and operation of those regimes” (Ibid);
- maintain a database of all legislative instruments for which they have policy responsibility; and
- ensure that the regulatory functions of other organisations are subject to “appropriate monitoring and accountability arrangements” (Ibid).

The Treasury acts as the guardian of the regulatory system, advising ministers on regulatory management rules, monitoring overall performance, reviewing specific processes (e.g. assessing the rigour of departmental RIS quality assurance and of significant regulatory proposals), and collecting information on upcoming regulatory proposals.

This devolved model fits with the public management approach taken since the late 1980s, which promotes performance and accountability to ministers. But it may not sufficiently encourage systemic improvements in regulatory performance.

- The devolved and “vertically-aligned” type of model means that incentives for agencies to coordinate, learn from each other and exchange information on regulatory practice are weak (see Chapter 11 for more discussion).
- The devolved model also implies relatively weak central leadership over regulatory management. The relevant department is responsible for identifying, improving or correcting regulatory institutions and...
practices. This limits the ability to identify and improve on common issues across departments or portfolios.

- The focus on departments also means that less central and consistent scrutiny is placed on the practices of non-departmental regulatory agencies. Such agencies are monitored by the relevant departments, and these departments are subject to oversight by Parliament and central agencies. But those with oversight or that monitor have few incentives to reveal information in a comparable format.

Underpinning these constraints on systemic improvements is the absence of consistent, comparable and comprehensive information about the practices of implementing and enforcing regulatory regimes. For example, the lack of readily-accessible comprehensive information means that those agencies that do wish to compare the regimes they are responsible for against others can struggle to find useful benchmarks.

Over 2013, the Treasury collected information from departments for a Regulatory System Report on regulatory management. That Report focused on such topics as how policy oversight is allocated, how policy is developed and implemented, how outcomes are monitored, and include aspects of evaluation and review (see Box 3.2). This information was used to inform decisions about Treasury’s future regulatory work programme. At this stage, there is no intention to publish the findings of the Regulatory System Report, which means that it cannot be used to promote wider discussion of regulatory performance.

Box 3.2 The Regulatory System Report

Over 2013, the Treasury collected the following information from departments about their regulatory management systems:

Allocating policy oversight

1. Does your department use the regulatory scanning database set up by the Treasury and hosted in CFISnet for keeping track of the legislation that it administers?

2. Does your department maintain a comprehensive database for keeping track of the legislation it administers, other than the database hosted in CFISnet? If so, please provide a copy or sample from that database.

3. Has your department clearly assigned policy oversight roles and responsibilities for each of the regulatory regimes it administers? (Clear assignment means an individual or team is fully aware of their responsibility for the regulatory regime). In answering this question, for each regulatory regime please provide details on:
   a) Is the oversight assignment visible within the organisation (e.g. to senior management, or reception/telephonist staff) and outside the organisation?
   b) Has the department clearly described the nature of, or set out minimum expectations for, this policy oversight role? If so, how?

4. Does the policy oversight role drive cross-agency collaboration or encourage feedback loops between departments? If so, how?

Policy development

5. Does your department’s regulatory impact analysis (RIA) quality assurance (QA) process involve:
   a) an independent QA panel;
   d) a designated independent person or persons; or
   e) other (please explain)?

6. Does your department’s quality assurance review cover:
a) final assessment of preliminary impact and risk assessments (PIRAs) and regulatory impact statements (RISs) only;

b) comments on drafts, and final assessment, of PIRAs and RISs;

c) comments on drafts, and final assessment, of PIRAs, RISs, and discussion documents; or

d) other (please explain)?

Implementation

7. For each of the regulatory regimes administered by your department that impose obligations on members of the public or businesses, does your department, or any other agency with responsibilities under that regime, have a documented compliance strategy?

If so, please provide a copy or sample from each documented compliance strategy.

8. For each of the regulatory regimes administered by your department but implemented (in full or part) by another entity, does your department maintain any specific systems for monitoring the approach taken to implementation, monitoring, and enforcement by that entity? If so, what are those systems?

Monitoring outcomes

9. Does your department have any systems or processes for encouraging feedback from the regulated community on the impact of regulation?

10. Does your department maintain any systems for collecting and recording information on:

   a) difficulties or problems in implementing legislation administered by the department (whether they are problems for the implementing agency or the regulated community), and

   b) errors or potential problems identified during implementation in the way legislation administered by the department has been drafted.

11. For each of the regulatory regimes administered by your department, does your department maintain any systems or processes for collecting and recording information on its regulatory impacts (positive and negative, intended or otherwise)? If so, what are those systems or processes?

12. For each of the regulatory regimes administered by your department that impose obligations on members of the public or businesses, does your department maintain any systems or processes for collecting and recording information on:

   a) levels of compliance by the regulated community;

   b) the drivers or determinants of compliance levels; and

   c) the costs incurred by the implementing/administering agency to encourage or ensure compliance, including information provision and enforcement activity?

If so, please provide information about those systems or processes.

13. Do those responsible for policy oversight have ready access to the information provided by the systems and processes discussed in questions 10 to 12 above? How is this access facilitated?

Evaluation and review

14. What, if any, requirements does your department have for periodically formally reviewing and reporting on the performance of each of the regulatory regimes it administers?

Please provide information on both external and internal requirements (e.g. what are those...
The information that the Commission is proposing should be collected would provide more granular data on how the regulator performs, and so give more depth to the Regulatory System Report. It would also be of value to monitors and implementers of regulation.  

What sort of information should be collected?

Feedback is sought on the types of information that regulators should be required to report on. At a high level the Commission considers that information should be collected that would allow an analysis of various institutional and practice aspects of regulators. Examples of the sort of information that could be collected are set out in Table 3.1.

Table 3.1 Possible scope of comparable information that could be collected from regulators

<table>
<thead>
<tr>
<th>Regulator structure</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Organisational form (e.g. department, Crown Entity, Crown agent, other body)</td>
<td>• Size of governing body (if appropriate)</td>
</tr>
<tr>
<td>• Method of appointment for governing body (if appropriate)</td>
<td>• Composition of governing body.</td>
</tr>
<tr>
<td></td>
<td>• Who has decision-making responsibility</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Efficiency</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Total expenditure and revenue</td>
<td>• Total or proportion of revenue recovered by fees, levies or other charges</td>
</tr>
<tr>
<td>• Total staff</td>
<td>• Unit costs of key regulatory processes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Effectiveness</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Number of licences/approvals issued</td>
<td>• Number of complaints received about regulated parties</td>
</tr>
<tr>
<td>• Number of investigations undertaken</td>
<td>• Number/type of enforcement actions taken</td>
</tr>
<tr>
<td>• Number of regulatory actions reviewed or appealed</td>
<td>• Outcome of reviews and appeals</td>
</tr>
<tr>
<td>• Type of enforcement strategy (e.g. risk-based)</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Responsiveness</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Whether licences/approvals can be applied for (and/or renewed) online</td>
<td>• Whether the regulator has statutory obligations to consult, and, if so, with whom</td>
</tr>
<tr>
<td>• Average time taken to process a licence/approval or other regulatory activity</td>
<td>• Whether the regulator publishes online guidance on how to comply</td>
</tr>
<tr>
<td>• Whether the regulator’s enforcement strategy is published</td>
<td></td>
</tr>
</tbody>
</table>

Source: New Zealand Treasury, 2013c, pp. 8-10.
The information collected from regulators should allow analysis of the structure, efficiency, effectiveness, responsiveness, scope of activity, burden of activity on regulated parties, and transparency and accountability of New Zealand regulators.

Options for collecting comparable data

The two main ways that comparable data on regulator activity could be collected are:

- a stand-alone, publicly-available survey of regulators, like the survey run by VCEC in Victoria (see Box 3.1); or
- setting standardised reporting requirements in existing accountability processes, especially the annual reports of the regulatory agency.

The choice between the two options largely comes down to a trade-off between efficiency and accessibility. A stand-alone survey, with all information presented in one place, could let regulators, advisers and members of the community easily compare agency practices and identify examples of good practice. But a stand-alone survey would also impose extra reporting requirements on regulators, increasing their costs. In comparison, using existing accountability processes to report on regulatory practices could involve lower costs for agencies. But doing so would require interested parties to collate information from a large number of different locations to compare and contrast regulator performance – a potentially onerous task.

In practice, the cost and accessibility differences between the two options may not be large. Most of the costs from a stand-alone survey or standardised reporting requirements in annual reports would be in the set-up phases (setting standard definitions, establishing new data reporting templates, and so on). And while standardised reporting would provide less access to data than a stand-alone survey, this problem
could be offset by a central agency analysing the data from regulator annual reports and publishing an annual summary.

On balance, the Commission prefers that standardised reporting requirements in agency annual reports be used to collect data on regulator activity. Doing so fits better with the long-standing expectation that public agencies are responsible for accounting for their performance to ministers, Parliament and the community.

The Treasury and the State Services Commission (SSC), as the central agencies responsible for the public sector accountability framework, should be responsible for developing these standardised reporting requirements.

R3.1 Standardised reporting requirements for agency annual reports should be used to collect data on regulator activity. The Treasury and the State Services Commission, as the central agencies responsible for the public sector accountability framework, should be responsible for developing these standardised requirements.

The Commission also recommends that, at the end of each financial year, the Treasury – as the agency responsible for regulatory quality management – collect and analyse performance data from regulator annual reports, and produce a public report outlining key features and trends.

This activity would serve two purposes.

- As noted above, a public report would help offset barriers to accessing the information on regulator practice.
- A public report would provide a stronger empirical basis to Treasury and SSC advice on regulatory management issues.

R3.2 At the end of each financial year, the Treasury should collect and analyse performance data from the annual reports of regulators, and produce a public report outlining key features and trends.

Using the data to identify system-wide issues

As noted earlier, the process of revealing comparable information on regulatory activity alone is likely to create incentives for improving design and performance. But producing comparable data would also permit the Treasury to better identify system-wide performance issues. For example, data from annual reports could be used to assess whether specific parts of the regulatory system can be improved (such as processing licences/approvals more quickly, and being able to apply online for licences/approvals). This data would also be a useful input to annual assessments of how well departmental chief executives have fulfilled their regulatory stewardship obligations (see Chapter 14). Where relevant, policies could be developed to resolve these issues. Then the next round of reporting might reveal how much regulatory practice has improved (Figure 3.2).
3.6 Implementing better reporting on regulatory activity

As the recommendations in this chapter involve a transition towards a system with standardised reporting as the norm, upfront adjustment activities and costs are inevitable. The three main steps needed to implement standardised reporting on regulatory activity will be to:

- confirm the agencies that will be covered by the reporting requirements;
- set common definitions of key regulatory processes; and
- issue new guidance on how to prepare annual reports.

Scope of agencies covered

As noted earlier, for the purposes of this inquiry, the Commission has focused on a subset of regulators that are national in focus, target market failures and carry out more than one regulatory function. This led the Commission to exclude agencies that provide the underpinning structures for wider regulation (such as the Courts, Police, and Inland Revenue), regional organisations with regulatory powers (such as District Health Boards, local authorities), and occupational regulators. If standardised reporting is to support better decisions about regulatory design and practice, it must cover a wider range of New Zealand regulators. Officials will need to do a stocktake of existing regulators and their regimes, and develop a framework for assessing which other agencies to include.

To avoid creating an unwieldy task, it would be worth continuing to focus on organisations that:

- are national in focus; and either

- are solely or largely focused on regulatory tasks (such as the exercise of coercive power) rather than on funding and other activities; or
• exercise regulatory functions that have, or can have, a significant impact on specific industries, groups or the wider economy.

**Setting common definitions**

To allow meaningful analysis of regulator activity and comparisons between regulators, common definitions of key regulatory processes or outputs must be agreed. For example, to measure the unit costs of key regulatory processes, definitions of these processes must be developed. Two examples of processes are issuing licences/consents, and carrying out audits/inspections. Given the very different industries and activities that regulators cover, this may be a challenge. But some central frameworks can be applied. For example, for the purposes of this inquiry, the Commission used the following descriptions of regulatory functions (Table 3.2).

**Table 3.2 Types of regulatory functions**

<table>
<thead>
<tr>
<th>Function</th>
<th>Description/examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Make rules or standards (under legislative or delegated authority)</td>
<td>Set standards, guidelines or rules to which regulated entities, individuals or activities must comply, reflecting the regulatory objectives set out in statute.</td>
</tr>
<tr>
<td>Inform and educate</td>
<td>Provide general or targeted information to firms and individuals subject to regulation about compliance.</td>
</tr>
<tr>
<td>Approve/prohibit activities</td>
<td>Provide approval to carry out regulated activities (for example, issue consents, approve mergers, license individuals to practise in a regulated profession), refuse to provide approval, or prohibit activities that are contrary to the objectives of the regulatory regime.</td>
</tr>
<tr>
<td>Promote and monitor compliance</td>
<td>Actively seek information from regulated entities and/or collect market intelligence to assess compliance levels and identify potential risks.</td>
</tr>
<tr>
<td>Handle complaints from the public</td>
<td>Receive and process complaints from the public about the performance of regulated entities and their compliance with regulatory requirements. Where appropriate, require the regulated entity to make amends.</td>
</tr>
<tr>
<td>Enforce compliance where breaches suspected</td>
<td>Investigate cases where entities or individuals are suspected of breaching regulatory requirements, assess whether the breach has occurred and assess the impacts of any breach. Where appropriate, issue penalties against the entity or individual or take enforcement action against them.</td>
</tr>
</tbody>
</table>

**Notes:**

1. This model is adapted from a framework from Victorian State Services Authority 2009.

To ensure that the framework applied captures the breadth of regulatory activity, regulatory agencies should be consulted before finalising the framework and definitions.

A second and related issue is whether reporting should take place at the level of the regulatory agency or regulatory regime. For a number of regulators, the two are synonymous (for example, single-regime regulators such as the Takeovers Panel, Office of the Health and Disability Commissioner, and the Electricity Authority). Other regulators implement a number of different regimes. While regime-level reporting could arguably allow more sophisticated analysis of design and practice features, the compliance costs for larger regulators of disaggregating performance data down to regime level may be significant. The Commission noted that Victoria’s survey on regulatory activity reports at an agency, rather than a regime, level. At this stage, the Commission is not convinced that the benefits of reporting at a regime level would outweigh the compliance costs of disaggregating performance data down to regime level.
Although reporting at the level of individual regulatory regimes might allow more sophisticated analysis of design and practice features, at this stage the Commission is not convinced that these benefits would outweigh the costs to larger departments of disaggregating performance data down to regime level.

Are there factors that would make the benefits of reporting at a regime level, rather than an agency level, outweigh the costs of doing so?

Issuing new guidance on annual reports

Finally, regulatory agencies must receive new guidance on how to use their annual reports to meet standardised reporting requirements. For many regulators, this may simply involve updating Treasury’s technical and process guides for departments and Crown Entities (New Zealand Treasury, 2013d; 2013e). But a number of regulators – especially occupational regulators – have reporting obligations that stem from specific Acts of Parliament, rather than the broad-based Public Finance and Crown Entities Acts. The Treasury and the State Services Commission should work with departments that have responsibility for these regulatory regimes to review the relevant legislation and issue new guidance on preparing annual reports.

The Treasury and the State Services Commission should work with relevant departments to ensure that all regulators not captured by the Public Finance or Crown Entities Acts comply with the new standardised reporting requirements for their annual reports.
4 Role clarity

Key points

- Clear regulatory roles and objectives are critical to regulator accountability and focus, compliance by regulated firms, predictable decisions and enforcement, and the legitimacy of the regime.

- Manifestations of poor role clarity include the expansion of regulatory scope beyond its original mandate; duplicative or contradictory regimes; gaps in regulation, monitoring or enforcement; and inconsistent enforcement. Many firms that the Commission surveyed perceived problems such as contradictory or incompatible regimes and regulators poorly managing duplicated compliance requirements.

- Regulatory regimes may lack clarity because:
  - the standards used do not fit the industry or activity being controlled;
  - policymakers give insufficient guidance about the desired objectives;
  - regulators have functions that create conflicts of interest; or
  - little attention was paid to designing the regime to the role of other regulators or the interaction of different regimes on regulated firms.

- Actions to improve the clarity of regulator roles, functions and objectives include:
  - ensuring that the regulatory standard used (outcome-, principle-, process- or input-based) is appropriate;
  - applying greater discipline in designing regulatory regimes;
  - avoiding perverse incentives when allocating regulatory functions to agencies; and
  - establishing processes to minimise or resolve problems from overlapping regimes.

- Issues to be considered in selecting the right regulatory standard are the level of harm that would arise from non-compliance, capability levels in the regulator and regulated industry, and the levels of trust between the industry and regulator.

- If a range of capability levels exists within a regulated industry, “deemed-to-comply” models can help to provide flexibility for more capable firms and certainty for less capable firms. Deemed-to-comply models allow more capable firms to develop their own compliance strategies, while also providing detailed guidance for other firms on how to comply.

- Legislative frameworks that minimise the number of objectives and conflicts and provide a clear hierarchy of objectives help to support consistent and predictable decision making by regulators.

- To promote better engagement with industry about the definition and interpretation of regulatory objectives, the Commission recommends that:
  - the Cabinet Manual be amended to make publishing exposure drafts the norm, before significant regulatory legislation is introduced; and
  - the next version of the State Services Commission’s machinery of government guidance require that all entities that implement new regulatory regimes have legislative obligations to publish a statement that outlines how they interpret their mandate, consult on that statement,
4.1 Introduction

Studies of the performance of regulatory regimes and agencies often dwell on the issue of mandate – that is, what the agency was authorised or tasked to do by ministers or Parliament (see, for example, Baldwin, McCrudden & Craig, 1987; House of Lords Select Committee on Regulators, 2007; Organisation for Economic Co-operation and Development [OECD], 2013a). The studies emphasise that a clear set of roles, duties and objectives is important if regulatory regimes are to be effective. Regulatory regimes with clear objectives are more likely to enjoy high levels of compliance and credibility, and regulators with clear and well-understood roles can more easily be held to account. But achieving “clarity” is not a simple or straightforward task due to the complex issues regulation often deals with, the multiple stakeholders in any regulatory regime, and the large amount of existing regulation.

This chapter discusses the impacts and causes of poor role clarity, and outlines steps to remedy these problems:

- Section 4.2 discusses why clear roles, objective and functions are important if regulatory regimes are to function efficiently and effectively;
- Section 4.3 describes how poor role clarity is seen in regulatory regimes or the actions of regulators; and
- Section 4.4 outlines the main causes of poor clarity and responses to those causes.

4.2 The importance of a clear mandate

A clear mandate can help promote accountability, compliance, focus, legitimacy, and predictability.

- **Accountability**: with clear objectives and functions, Parliament, industry and the wider public can more easily assess a regulator’s performance.
- **Compliance**: clear objectives and functions better allow regulated firms or individuals to understand what they need to do to meet regulatory standards, and so promote voluntary compliance.
- **Focus**: an agency with a clearly-defined mandate is more likely to be well run and well organised.
- **Legitimacy**: with clear objectives – and agency commitment to those objectives – regulated firms and the public will see the agency as more legitimate.
- **Predictability**: with a clearer mandate, the agency is more likely to apply its powers consistently, and individuals and firms are better able to predict how decisions will be made in the future.

A corollary of these principles is that clarity is defined by more than one party: the regulators and the regulated need to understand the job of regulators and how they should do their job. In addition, the test of clarity is not just in how roles, functions and duties are laid out in statute or policy frameworks, but in how the agency’s actions align – and are perceived to align – with these purposes.
4.3 Examples and effects of poor role clarity

Regulatory creep

One possible outcome of unclear roles and objectives is regulatory creep – the extension of the scope or impact of regulation in a non-transparent manner either deliberately or unintentionally. Regulators may take on functions not considered when the regulation was established, or may increase the range of activities and firms subject to control. The affected firms and the wider community then face an increase in the cost of regulation.

Regulators may have in-built incentives to expand the scope of their activities. Niskanen (1971; 1991) argued that bureaucracies seek to maximise their discretionary budgets (defined as the “difference between the total budget and the minimum cost of producing the output expected by the political authorities”). The discretionary budget can then be “spent in ways that serve the interest of the bureaucrats and the political authorities” (Niskanen, 1991, pp. 18-19). This can happen because of lack of market disciplines on bureaucracies (for example, only one “purchaser”, no competition for the provision of services, and no independently-determined prices). It can also happen because of the low value (relative to cost) that politicians derive from holding bureaucracies to account for their spending and activities. As a result, agencies will have larger budgets than they need to produce their services, and will seek to create the fiscal room to pursue other objectives.

How regulators interact with business can drive regulatory creep. “Cat-and-mouse” games between regulators and some regulated firms – which involve repeated exchanges where firms test the boundaries of regulation, and regulators respond – may convince regulators that they need to expand their jurisdiction in order to effectively deliver on their objectives (Berg, 2008).

Regulators also often face external pressure to respond to new issues or changing public views about acceptable risk levels. The Australian Productivity Commission (APC)’s recent review of regulator engagement with small business described these pressures:

> Growth in regulation is testament to the importance society now places on mitigating risks. As society becomes less tolerant of exposure to risks, regulators are under increasing pressure to justify their activities, and demonstrate how they are efficiently managing risks. …Regulators are frequently faced with calls to ‘do something’ in response to what is publicly perceived as unacceptable. (APC, 2013a, pp. 60-61)

Similarly, the Civil Aviation Authority cited two key challenges to successfully implementing a risk-based enforcement approach: “increasing public expectations of ‘no-risk’ results in high-risk aviation sports/activities”; and that the media “seeks to ‘blame’ regulators (and investigators) for failure to ‘keep people safe’ in high-risk aviation sports/activities” (sub. 6, p. 41). In such circumstances, a regulator can find it hard to resist pressures to expand the scope of its activities.

However, regulatory creep may be a well-intentioned response to gaps in the policy framework:

> High level goal-setting objectives may need further clarification. Goal-setting regulation can leave a vacuum that Government, regulators and industry will seek to fill with guidance. The guidance may stray beyond the original intention and/or it may be applied prescriptively by regulators and those being regulated. (Better Regulation Taskforce, 2004, p. 11)

Regulatory creep is not specific to goal-based regulation. The inherent inflexibility of prescriptive regulation means that regulators need to regularly update and refresh the mandatory standards. Over time, or without sufficient checks and balances, this could see the scope of activities subject to control expand. Similarly, with process-based regulatory standards (such as food safety plans) the definition of what constitutes an “adequate” risk management system or process changes over time. This can lead to regulatory creep.

Julia Black, Martyn Hopper and Christa Bland’s assessment of principle-based regulation in UK financial markets found that “high-level Principles have been used to extend the FSA’s [Financial Services Authority] scrutiny into areas such as ‘product design’, which had not previously been thought to be the subject of regulatory requirements”. The reluctance of the FSA to “identify a bright line between what is acceptable
or unacceptable” also left firms “to work out standards for themselves”, leading to a risk that they would “set them either uncomfortably high or too low” (Black, Hopper & Band, 2007, p/ 198).

Gaps may also arise because the underpinning legislative framework is outdated and no longer meets public expectations. As noted in Chapter 2, regulatory regimes in New Zealand can easily become obsolete, because of the heavy reliance on statutes, high demand on parliamentary time, and the lack of a strong review and evaluation culture. Regulators can feel pressure to move beyond their legal mandate:

For entities that are creatures of statute, this presents particular challenges because they are limited to perform the functions given to them by law. The result can be that entities feel compelled to interpret their law in a strained or unexpected manner to meet expectations causing them to breach the law and/or breach rights which in turn results in a diminished level of public confidence and in some cases can cause social harms. (Maritime New Zealand, sub. 15, p. 2)

Duplicated or contradictory regimes

Regulatory regimes may overlap with each other, lack clear boundaries, duplicate processes and create contradictory obligations on firms. Overlaps are particularly likely to occur when general and industry-specific regulations cover the same issue (VCEC, 2011). These tensions create unnecessary costs for regulated firms and cause confusion about which regulatory obligation or agency has priority:

We have previously sought clarification from the Ministry for the Environment as to the priority afforded the Commerce Act in seeking to give effect to the presumption in the Waste Minimisation Act, that manufacturers demonstrate ‘Extended Producer Responsibility’ (EPR). One interpretation of EPR is that it includes an obligation to discuss with manufacturers of similar products the possible means and arrangements whereby those products can be recovered and recycled. It is conceivable that concerted efforts to give effect to the statutory/regulatory expectation for EPR could be misconstrued as an unintended or deliberate breach of laws intended to prevent cartel or collusive behaviour. (Carter Holt Harvey, sub. 8, p. 9)

Evidence that the Commission collected revealed differing views on the scale and significance of overlaps in New Zealand. On one hand, some submitters argued that overlap “is relatively limited” (Genesis, sub. 48, p. 7; Reserve Bank of New Zealand (RBNZ), sub. 9, p. 3). Others argued that regulators managed overlaps well (New Zealand Food and Grocery Council (NZFGC), sub. 35, p. 5; Aviation New Zealand, sub. 36, p. 11). Thirty-nine per cent of regulator chief executives (9 out of 23 respondents) agreed with the statement that “regulatory regimes often have competing regulatory objectives”, while 34% (8 respondents) disagreed or strongly disagreed. In addition, more than half (56%; 13 out of 23 respondents) of chief executives agreed or strongly agreed that “agencies usually manage competing regulatory objectives effectively”.

Figure 4.1 Chief executives who agree with the statement “Regulatory regimes often have competing regulatory objectives”

On the other hand, 90% of the 1,526 businesses surveyed by the Productivity Commission believed that regulatory requirements in New Zealand were “sometimes”, “mostly” or “always” contradictory or incompatible with each other (Figure 4.3). Businesses that were 3-5 years old were most likely to report that requirements were “always” or “mostly” contradictory (29%), while firms in the information, media and telecommunications and professional, scientific and technical services sectors were most likely to state that they were “rarely” or “never” incompatible (19% and 17%, respectively).

In response to a Productivity Commission request for information, 18 of 25 regulators reported that they implemented at least one regulatory regime that overlapped with those run by other agencies (see Figure 4.4).

Source: Colmar Brunton, 2013.
Source: Information collected by the Productivity Commission.
Roughly half of the businesses that the Commission surveyed believed that regulators “rarely” or “never” work with each other to reduce the paperwork/effort on firms (Figure 4.5).

**Figure 4.5** Businesses that agree with the statement “Regulators work with each other to reduce the paperwork/effort on organisations”

Many firms that the Commission surveyed saw contradictory or incompatible regimes and regulators poorly managing duplicated compliance requirements as issues in New Zealand.

One possible explanation why surveyed businesses perceived a higher degree of incompatibility and contradiction in regulatory regimes and lower regulator effectiveness in managing duplicated compliance requirements is that firms face a much wider range of regimes than regulators appreciate. In addition, 80% of survey respondents were small firms (19 or fewer full-time equivalent staff). Such firms are likely to lack the regulatory management staff of large businesses. This means that smaller firms may feel the burden of regulatory compliance more keenly.

A number of submitters also identified specific regimes where boundaries were not clear, or where firms experienced conflicting requirements (see Box 4.1).

**Box 4.1 Key overlapping regulatory regimes that submitters identified**

The areas of regulatory overlap most commonly identified in submissions were electricity, financial markets, and health and safety.

**Electricity**

A number of submitters highlighted the roles of the Commerce Commission and Electricity Authority in regulating electricity lines businesses (for example, Powerco, sub. 14, pp. 4-5; Wellington Electricity, sub. 17; Electricity Networks Association, sub. 27, pp. 12-15; Minter Ellison Rudd Watts, sub. 28, pp. 17-21; Vector, sub. 29, pp. 14 and 23; Transpower, sub. 32, p. 7). Most of the commentary focused on the potential for problems to arise, but some cited cases where the overlap had created actual issues:

Electricity networks are regulated by both the Commerce Commission under Part 4 of the Commerce Act 1986 and the Electricity Industry Participation Code 2010 (code). Decisions made by either regulator often have direct implications for the functioning and effectiveness of the regime implemented by the other regulator. For example, changes to the Code which result in increased costs and/or risk to distributors that were not known at the time the Commission determined the Default Price-quality Path. (Wellington Electricity, sub. 17, p. 1)

...there have been occasions when the industry regulator has made policy recommendations that are not aligned with the Commission’s regulatory regime. For example:

- The EA released a transmission pricing methodology (TPM) that would have given rise to

---

13 43% of respondents had 1-5 FTEs.
volatility in transmission costs to ENBs [electricity network businesses]. Transmission costs are a pass-through for non-exempt ENBs, and the way the DPP [default price path] is structured for pass-through costs does not allow for volatility. This meant that the proposed TPM would not work with another part of the regulatory regime; and

• The EA proposed using the structure of its levy to create incentives for participants, without understanding that these are a pass-through cost for non-exempt ENBs. This means that ENBs are not directly affected by EA levies.

Such disconnects between the regulatory regimes impose costs and impair overall effectiveness for no apparent advantage. (Electricity Networks Association, sub. 27, p. 15)

Minter Ellison Rudd Watts argued that different approaches taken by the two regulators affected regulatory certainty:

There is no single correct process to address grid upgrades or renewal allocation. However, it does not enhance regulatory certainty if one regulator uses an ex ante approval process for grid upgrades, and the other regulator uses an ex post process for the allocation of the costs of the same upgrades. (sub. 28, p. 17)

Financial markets

Submitters identified two main areas of overlap in financial market regulation. The first was the large number of organisations involved in regulation, unclear boundaries between many of them, and the lack of guidance on how and when the different organisations would work together. In some areas, submitters believed there were conflicting requirements:

An example is the overlap between the NZX [New Zealand Stock Exchange] and the FMA [Financial Markets Authority]. NZX firms are regulated under the NZX Participant Rules. The same firms are also ‘brokers’ for the purposes of the Financial Advisers Act and must comply with the broking requirements in the legislation. Currently, the rule sets (and each regulator’s interpretation) conflict with each other, so that compliance with one set…[of]…rules could potentially be a breach of the other. It is unclear which regulator’s views will prevail in the event of conflicts between the NZX and the FMA. (ANZ, sub. 24, p. 3)

Bell Gully argued that the Memorandum of Understanding (MOU) between the Serious Fraud Office and the Financial Markets Authority allowed for “concurrent investigations in relation to a single set of circumstances”, which could create significant costs and legal complications (sub. 38, p. 2).

The second issue identified was two organisations (the Commerce Commission and Financial Markets Authority) having responsibility for preventing and prosecuting misleading and deceptive conduct in the financial markets (Insurance Council of New Zealand, sub. 5, pp. 3-4; IAG, sub. 10, p. 13; ANZ, sub. 24, p. 10; New Zealand Bankers’ Association, sub. 43, p. 8). In the case of financial advisers, the Insurance Council of New Zealand argued that such conduct could be potentially covered by three different regimes—the Financial Markets Conduct Act 2013, the Financial Advisers Act 2008, and the Consumer Law Reform Bill that was recently passed.

Health and safety

Comments about health and safety focused on the number of agencies involved in regulatory implementation and the weak leadership in some areas (Council of Trade Unions, sub. 25, p. 16; Institution of Professional Engineers New Zealand, sub. 21, p. 6).

Aviation New Zealand said that different standards were applied to safety issues in the aviation industry:

there is only one state of safe and that is people are not hurt or injured, but we have different definitions of ‘safe’. We have different definitions of serious harm. We have different threshold tests. We have very different ways of investigating incidents and accidents – we have different definitions of accident.

To place some semblance of accountability into this complex confusing and conflicting regulatory
Gaps in regulation, monitoring or enforcement

Gaps may appear either within or between regulatory regimes, leaving some activities uncontrolled or ineffectively overseen. Prescriptive or input-based regulatory standards are arguably most prone to this problem, as technological changes outpace the ability of detailed rules to control risks.

The risk of gaps appearing is higher when multiple regulatory agencies operate within an industry without one agency being a clear leader. This has been a particular issue with financial market regulation during the past decade, both here and overseas. The Commerce Select Committee inquiry into finance company failures found that:

The supervisory framework was fragmented and insufficiently rigorous. …The several regulators operated under relatively narrow legislative mandates. Overlapping responsibilities and inadequate funding led to things slipping through the cracks. (House of Representatives Commerce Committee, 2011)

Similarly, financial market regulators in the United Kingdom faced strong criticism from Parliament for failing to: prepare adequately for crises such as the failure of the Northern Rock bank; resolve weaknesses in the legislative framework when they had been identified earlier; or respond quickly enough to Northern Rock’s difficulties. The parliamentary inquiry identified as a key problem the absence of a clear leadership structure within the financial regulators (House of Commons Treasury Committee, 2008).

Inconsistent decisions or enforcement

The last manifestation of poor role clarity is where regulators enforce their regimes inconsistently. This may discourage investment or innovation, as firms are unsure how regulators will treat their activities. Poor role clarity can also be perceived as unfair and undermine the regime’s credibility.

Inconsistent enforcement can occur when regulatory objectives or principles are not adequately defined, where conflicting objectives exist, or where an industry has multiple regulators:

The Resource Management Act creates a mandate for broad interpretation of “sustainable management” of the environment by Regional and District government. Our experience over the last 20 years has been that ‘Sustainable management’ of forestry operations has been interpreted differently by different regulators sufficiently often to justify greater national direction. (Carter Holt Harvey, sub. 8, p. 2)

The New Zealand energy market includes regulation by the Commerce Commission, Electricity Authority, GIC [Gas Industry Company], Energy Efficiency and Conservation Authority and the Energy Safety section of MBIE [Ministry of Business, Innovation and Employment]. There is some overlap between these bodies in particular areas. Additionally, regulated firms can find different regulators taking inconsistent or opposing positions on the same issues. (Vector, sub. 29, p. 23)

Responses to a business survey undertaken for the Commission indicated that inconsistent regulatory decisions are a problem in New Zealand. While 39% of surveyed firms felt that organisation across their industry were “mostly” or “always” treated fairly and consistently, 45% believed this was only “sometimes” the case. A further 16% believed organisations in their industry were “rarely” or “never” treated fairly.
Firms in the professional, scientific and technical industries were most likely to report that organisations in their industry were “always” or “mostly” treated fairly (52%), while businesses in the construction industry were most likely to report that organisations in their industry were “rarely” or “never” treated fairly (22%).

Compliance and enforcement practices are discussed in more detail in Chapter 10.

4.4 Causes of poor role clarity, and responses to it

A regulator or regulatory regime may lack clarity for a number of reasons, including that:

- the regulatory standards used do not fit the industry or activity being controlled;
- policy makers provide insufficient guidance about the desired objectives of regulation;
- regulators have been given functions that conflict with their regulatory obligations; and
- insufficient attention was paid (when designing the regime) to the role of other regulators, or to the impact of different regimes on regulated firms.

Each of these reasons, and possible responses, is discussed in turn. Steps can be taken at all points on the regulatory “value chain” to improve role clarity, including decision review and appeal processes, accountability and performance assessment mechanisms, and engagement systems. This section focuses on actions related to a regulator’s mandate, in particular its founding legislation and functions.

Regulatory standards

Regulatory regimes need to fit the industries or activities being controlled, and have the appropriate capability available to interpret and enforce them. At a high level, there are four main regulatory standards: principle-based; performance/outcome based; input-based/prescriptive; and process or system-based.

Table 4.1 Types of regulatory standard

<table>
<thead>
<tr>
<th>Regulatory standard</th>
<th>Definition</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Principle-based regulation</td>
<td>Sets high-level qualitative principles or rules that entities must follow in their conduct (such as “reasonable care”)</td>
<td>Occupational health &amp; safety</td>
</tr>
<tr>
<td>Performance/outcome-based regulation</td>
<td>Specifies the outcomes/goals to be met, but not the way to meet them</td>
<td>Pollution emission limits</td>
</tr>
<tr>
<td>Input-based/prescriptive regulation</td>
<td>Specifies the precise inputs that must be used to achieve regulatory compliance</td>
<td>Occupational regulation has traditionally been input-based (such as requiring certain educational qualifications), but it is now moving towards performance-based approaches</td>
</tr>
<tr>
<td>Process or system-based regulation</td>
<td>Requires regulated entities to introduce processes or systems with specified elements</td>
<td>Food safety Hazard Analysis and Critical Control Point requirements</td>
</tr>
</tbody>
</table>
The four standards are not mutually exclusive. For example, the Hazardous Substances and New Organisms Act 1996 (HSNO) is a performance-based regime that aims to “protect the environment, and the health and safety of people and communities, by preventing or managing the adverse effects of hazardous substances and new organisms” (section 4 of HSNO). But it is underpinned by a series of detailed expectations that may require holders of hazardous substances to prepare emergency response plans or ensure that storage and transport facilities have specific characteristics. Similarly, principle-based occupational health and safety regulatory regimes are often supported by system or process requirements (such as risk management plans).

Each regulatory standard has strengths and weaknesses, and each suits a different set of circumstances. The selection of the appropriate regulatory standard depends on:

- the ease in defining and measuring the desired outcome(s) from regulation;
- the degree to which regulators and regulated entities trust each other;
- the degree of change or diversity within the regulated industry or activity;
- the level of capability in the regulators and regulated entities; and
- the extent to which standardisation is desired or required.

Selecting an inappropriate standard may introduce unnecessary costs for regulated firms, lead to poor levels of compliance, or leave important hazards or risks insufficiently controlled. MBIE observed that this had been an issue with some of the regulatory frameworks it (and its predecessor agencies) oversaw:

> 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. (sub. 52, p. 4)

The Meat Industry Association argued that inappropriate regulatory standards had hampered the move to a properly risk-based compliance and enforcement approach:

> In an ideal world the New Zealand regulatory standards and those imposed by importing countries would be the same and they would be based on risk and describe the meat hygiene outcomes that must be achieved to address those risks. However, prescriptive requirements remain.

Review and removal of prescriptive requirements should continue, as should challenging importing countries requirements where there is no scientific justification and/or risk-based outcome that requirement is designed to achieve. The converse of this is to continue work on providing the processing sector with outcome-focused performance targets that allow for flexibility in companies’ ability to innovate and achieve the ends required. (Red Meat Regulatory Strategy, cited in sub. 40, p. 20)

### Selecting the right standard

Table 4.2 below outlines the advantages and disadvantages of the different standards and the circumstances in which each standard works best. Some have argued that governments should prefer the more enabling regulatory standards (outcome-based, principle-based, or process-based regulation), on the grounds that they are better able to deal with changes in technology or business practice, allow for innovation in compliance, and permit firms to find the lowest-cost means of complying (see, for example, Business Council of Australia, 2013; Government of Victoria, 2010; OECD, 2012a; US Department of the Treasury, 2008). However, as seen in Table 4.2, there are circumstances where input-based standards are more suitable.
<table>
<thead>
<tr>
<th>Regulatory standard</th>
<th>Advantages</th>
<th>Disadvantages</th>
<th>Works best where…</th>
</tr>
</thead>
<tbody>
<tr>
<td>Principles-based regulation</td>
<td>Allows firms in dynamic industries to adjust to changing circumstances</td>
<td>May lead to uncertainty as to whether a firm’s compliance actions meet the required standards. This may unnecessarily increase costs for that firm. Uncertainty may also discourage innovation.</td>
<td>Outcome/goal of regulation can’t be easily and objectively measured</td>
</tr>
<tr>
<td></td>
<td>Can enable firms to find least-cost means of complying</td>
<td>Can require high levels of guidance from regulators</td>
<td>Other parties (such as consumers, workers) have the capability to monitor compliance</td>
</tr>
<tr>
<td></td>
<td>Can provide a basis for open dialogue between the regulator and those regulated, supportive of substantive (rather than “tick box”) compliance</td>
<td>Diversity of compliance approaches may create a higher risk for a firm to not comply or regulators to undertake inconsistent enforcement</td>
<td>A high degree of trust and good communication exists between the regulator and regulated entities</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Can require high levels of capability within a firm to achieve compliance</td>
<td>The regulator is well-resourced and capable</td>
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<td></td>
<td>The industry/regulated activity is diverse, and acceptable practice is likely to change over time</td>
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<td></td>
<td></td>
<td></td>
<td>Competition/innovation is likely to drive more efficient compliance</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>Greater innovation in meeting regulatory objectives is desired</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Non-compliance by firms or mistakes by regulators do not create high levels of public harm</td>
</tr>
<tr>
<td>Performance/outcome-based regulation</td>
<td>Allows firms in dynamic industries to adjust to changing circumstances</td>
<td>Few cases where outcome/goal can be tightly defined and easily measured</td>
<td>Outcome/goal can be tightly defined, and targeted output can be easily and objectively measured (for example, quantitatively)</td>
</tr>
<tr>
<td></td>
<td>Can enable firms to find least-cost means of complying</td>
<td>If outcome/goal is not clearly defined or easily measured, may lead to uncertainty as to whether a firm is actually complying or requires high levels of guidance</td>
<td>Targeted output (such as emissions) has a strong link to the desired regulatory outcome (such as cleaner air)</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>Firms are better placed than regulators to choose the best way to comply (for example, due to dynamic industry/technical complexity), and have the necessary capability</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Competition/innovation are likely to drive more efficient compliance</td>
</tr>
<tr>
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<td></td>
<td>Greater innovation in meeting regulatory objectives is desired</td>
</tr>
<tr>
<td>Regulatory standard</td>
<td>Advantages</td>
<td>Disadvantages</td>
<td>Works best where...</td>
</tr>
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</tr>
<tr>
<td>Input-based/prescriptive regulation</td>
<td>Can provide a high degree of consistency and certainty for regulated firms</td>
<td>Can have high administration and compliance costs</td>
<td>Little trust exists between regulators and regulated entities</td>
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<tr>
<td></td>
<td>Objective criteria can inform decisions to prosecute/enforce</td>
<td>Leaves a firm little room to comply in other, more efficient ways</td>
<td>Standardisation is very important</td>
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<td></td>
<td></td>
<td>Does not keep up well with rapid changes in technology – may become obsolete or</td>
<td>Regulated entities have neither the ability nor need to be innovative in complying</td>
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<tr>
<td></td>
<td></td>
<td>require frequent adjustments (which increase the cost and complexity of compliance)</td>
<td>Stable risks exists that need a high degree of certainty</td>
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<tr>
<td></td>
<td></td>
<td>Because of its “one-size-fits-all” approach, can be under-inclusive (missing some</td>
<td>The level of harm from non-compliance is unacceptable, and a high level of certainty is desirable</td>
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<tr>
<td></td>
<td></td>
<td>hazards or risks) or over-inclusive (unnecessary in some situations)</td>
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<td></td>
<td></td>
<td>Can be used to create barriers to entry or unnecessary costs</td>
<td></td>
</tr>
<tr>
<td>Process or system-based regulation</td>
<td>Can promote innovation in risk mitigation/management practice</td>
<td>Can be costly to administer</td>
<td>A number of substantial risks must be managed simultaneously</td>
</tr>
<tr>
<td></td>
<td>Can promote firms to own and be accountable for risk mitigation</td>
<td>Potential for scope of risks covered or standards of control required to increase</td>
<td>A range of management measures are available</td>
</tr>
<tr>
<td></td>
<td>Allows firms in dynamic industries to adjust to changing circumstances</td>
<td>over time (so raising compliance costs to firms)</td>
<td>Regulated firms have the capability to effectively assess risk and develop solutions to manage those risks under their control</td>
</tr>
<tr>
<td></td>
<td></td>
<td>In some circumstances, may create overlaps with other regulatory regimes (such as</td>
<td>Regulators have the capability to assess the adequacy of processes or systems</td>
</tr>
<tr>
<td></td>
<td></td>
<td>occupational health and safety and environmental regulation)</td>
<td></td>
</tr>
</tbody>
</table>

Implementing regulatory standards to fit the industry

Enabling standards (that is, outcome-based, principles-based, or process-based) work best where the regulated firms have the capability to interpret the regulatory frameworks and develop suitable compliance strategies. This can create a bias towards larger firms:

Large organisations are more likely to have the resources and capacity to prepare for and respond to regulatory interventions and interactions – they may have dedicated regulatory compliance staff whose job it is to understand the regulatory regime, and can spread the costs of regulatory interactions across a broader business base. This may make them more able to comply with regulatory requirements (or, indeed, more able to find ways to avoid or subvert them). In contrast, small organisations are likely to be less knowledgeable about regulatory requirements and to find it more difficult to make capacity to respond to regulatory interactions. (Walshe & Boyd, 2007, p. 19)

For smaller organisations that lack the necessary capability, the breadth of possible compliance strategies can be daunting. They may prefer the certainty of more prescriptive standards. The Environmental Protection Authority noted that in “some circumstances, there may be a better overall outcome (i.e. higher compliance with basic protections) if individuals/small businesses are given clear, simple obligations to keep themselves and others safe, and to protect the environment, despite the trade-off of less flexibility” (sub. 20, p. 2).

Enabling regulatory standards can be designed to provide flexibility for larger, more capable firms and certainty for smaller entities through such models as “deemed-to-comply”. Deemed-to-comply models combine high-level objectives or principles (usually in primary legislation) with voluntary, detailed rules (usually in guidance documents) that spell out how firms can comply with the objectives or principles. Firms are free to develop their own compliance strategy, but if they follow the rules they are “deemed” to comply.

The Building Act 2004 is one example of a regulatory regime that employs deemed-to-comply. All building work in New Zealand must comply with the Building Code (a secondary regulation made under the Building Act). The Building Code (the Code) sets out the minimum structural and safety standards building work must perform to (such as protection from fire, durability and moisture control), but not how the building should meet them. Building practitioners can comply with the Code by using prescriptive guidelines known as “Acceptable Solutions” that MBIE has prepared. Building consent authorities must approve any designs based on the Acceptable Solutions. Alternatively, building practitioners can propose other ways (“Alternative Solutions”) of to meet the requirements of the Code. Where an Alternative Solution is used, the burden is on the practitioner to demonstrate how their solution complies with the Code.

Deemed-to-comply models can help shift regulatory regimes from prescriptive/input-based approaches to more enabling approaches where desired: the existing input-based guidance becomes the detailed rules, but firms are allowed to seek other options. Deemed-to-comply models can also allow regulatory systems to adapt to changes in technology or shocks. Rather than having to change the underlying statute and regulatory framework, the detailed rules can be updated to reflect new developments. Deemed-to-comply models depend, however, on the regulator having the capability to administer more than one system, and multiple systems may confuse some entities and consumers.

Other models that provide a different balance of flexibility and certainty are menu-based or comply-or-disclose models:

- **Menu-based** regulatory models allow regulated firms to choose from a menu of compliance options. This approach is used in the Trans-Tasman Mutual Recognition Agreement.

- **Comply-or-disclose** models lay down rules or standards, but allow firms/individuals to diverge from the standards, provided the firms disclose where and why they have diverged.

A comply-or-disclose model is arguably more permissive than other models, as firms or individuals do not need to find other ways to meet the standards. They may choose to ignore the standards, provided they disclose this. Even so, it is only suitable for some circumstances, particularly where non-compliance (such as
divergence from the rules or standards) does not create high risks and where consumers or other institutional players are able to judge the performance of regulated firms.\footnote{For example, comply-or-disclose forms part of the listing rules of the Australian Stock Exchange, where firms are subject to regular and high degrees of scrutiny by investors and analysts.}

“Deemed-to-comply” systems can let regulatory regimes adapt to changes in technology or shocks. They also permit different firms to find the compliance approach that best suits them. This lets regimes more effectively cover industries where the capability varies.

Enabling regulatory standards must be implemented and enforced with care, if they are to deliver on their potential. As Julia Black has found, regulators may need to strike a number of balances between competing goals, such as clarity and flexibility (see Box 4.2). Black’s paradoxes also highlight the importance of ensuring that the regulatory standard selected is appropriate for the industry (for example see the explanations of various paradoxes below):

- Paradox 7 reinforces the point that principles-based regulation is unlikely to fit an environment where a low level of trust exists between the regulator and firms.
- Paradox 5 highlights the importance of having sufficient capability within industry to implement the regime.

### Box 4.2 The paradoxes of principles-based regulation (PBR)

Julia Black’s work on UK financial markets regulation has shown that some tensions must be managed when introducing principles-based regulation:

- **Paradox 1: the interpretative paradox** – principles can be general yet precise. Regulatory principles are often cast at a general level (for example, “reasonable care”), giving firms flexibility in how they comply. Despite this, the principles can be interpreted narrowly by firms and regulators. As a result, PBR can in practice “be almost indistinguishable in places from a regime characterized by detailed rules”.

- **Paradox 2: the communicative paradox** – principles can facilitate communication but can also hinder it. Too much communication or guidance from regulators can make it harder for firms to figure out exactly what is expected (they struggle to figure out which statement has precedence).

- **Paradox 3: the compliance paradox** – principles provide scope for flexibility in compliance yet can lead to conservative and/or uniform behaviour by regulated firms. Uncertainty about how regulators will interpret principles “can result in firms adopting conservative behaviour, as if they were bound by detailed rules”. The use of consultants to help firms comply may also encourage “convergence on a set of broadly common practices”.

- **Paradox 4: the supervisory and enforcement paradox** – principles need enforcement to give them credibility but over-enforcement can lead to their demise. A heavy reliance by regulators on tough or punitive enforcement may drive out flexibility in complying, as “firms seek the comfort of detailed rules”.

- **Paradox 5: the internal management paradox** – PBR can provide flexibility for internal control systems to develop but can overload them. PBR can empower a firm’s internal control systems, by giving them (rather than external inspectors) a greater role in assessing whether or not the firm is meeting regulatory requirements. But if internal control systems are not robust, this responsibility can weaken rather than strengthen them.

- **Paradox 6: the ethical paradox** – PBR can facilitate a more ethical approach but it could erode
Guidance from policymakers

The underlying legislative or policy frameworks may not guide regulators or regulated entities clearly enough on how the regime should operate. As a result, firms may struggle to understand how to comply, and regulators may expand their activities beyond the scope originally intended by Parliament, or make inconsistent decisions. These issues can arise where:

- the outcome(s) or principles guiding the regulatory framework are imprecise; or
- the regulatory framework has multiple objectives or principles.

Imprecise outcomes or principles

The outcomes or principles guiding regulatory frameworks may be vaguely worded or open to wide interpretation. Black (2012) noted that “the overall outcomes that regulators are meant to achieve are usually expressed in highly general terms: for example, to protect consumers or the environment, to ensure competition, to maintain financial stability or to uphold the rule of law”. (p. 9)

Some submitters believed that the legislative drafting approach in New Zealand contributed to imprecise regulatory objectives:

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…our style of statutory drafting often relies on broadly phrased “purpose statements”, which are intended to guide regulator discretion but in practice are often imprecise or call for the regulator to make difficult trade-offs. (IAG, sub. 10, p. 8)
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In some cases, the primary legislation lacks sufficient specification of the overall objectives or purposes for which powers may be exercised; there is a tendency for the objectives or purposes to be stated at a very generalised level. (Mortlock Consultants Ltd, sub. 31, p. 2)

The NZFGC considered that legislative drafting had improved over time:

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NZFGC finds that the more recent the regulatory regime, the clearer the objectives. …An example is the current Food Act and the prospective Food Bill. The latter has very clear objectives, the former difficult to locate. (sub. 35, p. 4)
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But Aviation New Zealand and Maritime New Zealand said that the clarity of their legislative frameworks had been eroded by recent amendments:

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In aviation we had a very clear objective of safety at reasonable cost. All participants in the aviation community could apply a cost benefit test to regulatory changes. We had a common mantra and a common way of addressing issues. On November 30 2004 the Act was amended by amending the objective of the Minister to now be “to undertake the Minister’s functions in a way that contributes to the aim of achieving an integrated, safe, responsive and sustainable transport system”. Nobody understood what the change meant or how it impacted on the functions of the Authority. However one thing did become clear: that the quite precise tests which we previously applied to decisions became diluted at least at the regulatory level. (Aviation New Zealand, sub. 36, p. 5)
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The clarity around the objectives for MNZ has over time been eroded by amendments to the law. When the Maritime Transport Act was first made the objective of safe, secure and effective marine pollution prevention was premised only “at a reasonable cost”. This was replaced in 2004 by the current objective which has reduced the singular clarity that existed before. Words like “sustainable” are not defined and increase the risk of reduced clarity around the regulatory objectives although in practice this has not presented material challenges. (Maritime New Zealand, sub. 15, p. 6)
Multiple objectives

Multiple objectives or principles can undermine clarity where regulators lack guidance from policymakers or lawmakers on how they should prioritise objectives, or which processes they should use to reach decisions. In these circumstances, regulators may fail to decide consistently or may place more weight on one objective than another. Business New Zealand cited the now-disestablished Electricity Commission as a case where multiple regulatory objectives can cause problems:

the Electricity Commission had multiple and confused objectives which was complicated by the fact that it had no clear ex ante or transparent definition for making the trade-offs between them. In fact, they were so diverse and complex in the context of the electricity market that there was no obvious way in which the trade-offs could be made. …Ultimately, the Electricity Commission used its judgement to make the trade-offs in a non-transparent manner. This resulted in a regulatory outcome akin to a lottery, and as a result, the industry adjusted upwards its risk adjusted rate of return and investment slowed to the point that the then government was required to procure stand-by plant (it purchased Whirinaki thermal plan in the Hawkes Bay) to ensure sufficient security of supply. (sub. 19, pp. 23-24)

More disciplined design is needed

Greater discipline at the design and drafting stage is an important way of avoiding unnecessary conflicts and creating regimes that are manageable for regulators and the regulated.

Multiple or conflicting objectives are not necessarily poor practice. Parliament may have valid reasons to establish a regulatory regime with conflicting goals. Lawmakers may decide that they lack the time, information or expertise to take optimal decisions or make consistent decisions, especially where regulation deals with technical issues or dynamic industries. In delegating some of these difficult decisions to other parties, lawmakers may be trying to constrain problematic incentives in the political system. For example, the electoral cycle

may induce Congress to prefer trade-offs that achieve short-run benefits at the expense of incurring costs in the distant future and to avoid short-run costs even if it means passing up future benefits. Congress may reduce this bias in policy making by assigning conflicting policies to a long-lived regulatory agency that does not place as high a discount on future costs and benefits. (Wall & Eisenbeis, 1999, p. 140)

Policymakers may also introduce more than one objective into a regime to ensure that regulators take a balanced approach. The RBNZ observed that this can be the case with its two financial stability objectives: “where there is a potential trade off, the efficiency objective can also work as a useful check on the soundness objective” (sub. 9, p. 3).

Even so, delegating decisions to regulators is not without risk. Delegation can create principal–agent problems, where regulators fail to act in line with the intent of Parliament. This is particularly likely where the decisions involve trade-offs between competing values. Before deciding to give decision-making powers to regulators, policymakers should be certain that the issues in question would best be considered by officials rather than elected representatives. As the APC noted in its recent report on major projects, some decisions are more appropriately taken by ministers, rather than regulators:

When approval decisions can be made by applying objective, measurable rules, experts in those rules are well placed to make decisions. …However, primary approval decisions about whether and how major projects should proceed often involve tradeoffs between competing environmental, social and economic values that a technical body is not equipped to assess. (APC, 2013b, p. 207)

The issue of how to allocate decision-making powers is discussed in more detail in Chapter 6.

Where policymakers decide that there would be a net benefit in regulators having decision-making powers in regulatory regimes with multiple or competing objectives, principal–agent issues and other related risks can be reduced by:

• keeping the number of objectives or conflicts in the regulatory regime to the lowest-possible number;
• providing clear signals about the relative priority of regulatory objectives;
• establishing more robust process for clarifying the meaning and interpretation of regulatory objectives.
Minimise the number of regulatory objectives and conflicts
Several submitters argued that problems had arisen where policymakers had not confronted difficult policy trade-offs or attempted to achieve too many goals through one vehicle:

Where policy makers fail to make difficult policy choices about priorities and areas of focus for regulatory outcomes, they create risks to achieving regulatory outcomes. This is because the policy failure results in a lack of clarity or purpose for the regulator. …This results in operational regulatory bodies grappling with the issue and seeking to achieve potentially conflicting outcomes in whatever way they think is expedient. (Maritime New Zealand, sub. 15, p. 2)

The regulatory regimes set up as a result of electricity and gas industry inquiries in the early 2000s contained “kitchen sink” objectives. As a consequence, the regulatory objectives provided little practical guidance on the trade-offs which needed to be made in the regulatory process. (Minter Ellison Rudd Watts, sub. 28, p. 8)

With a growing tendency to specify principles in primary legislation, there is a danger that Parliament will provide a smorgasbord of outcomes that are to be achieved. The Resource Management Act is a very good example, but there is little guidance given as to how decision makers should decide between potentially conflicting outcomes. (Tasman District Council, sub. 1, p. 2)

Participants are more likely to understand and regulators more effectively manage a legislative framework with the least possible number of objectives and conflicts. As the Auckland Energy Consumer Trust noted, to be able to adequately monitor the balancing of objectives it is always easier when there are fewer objectives to be taken into account. Indeed, two is a good number. Aside from the obvious ease of understanding, one reason for this is that with two objectives there is only one trade-off [a v b]. With three, there are three pairwise matches [a v b, b v c, a v c]. And such trade-offs are complex social judgements, in which the elements typically change at different rates. They frequently involve hard-to-establish data and values, and are unlikely to be social constraints; so they may have different values depending on scale and incidence. (sub. 22, p. 4)

Provide a clear hierarchy, where multiple objectives are being pursued
Although delegating the management of difficult trade-offs to regulatory authorities can be legitimate strategy, policymakers should provide guidance about which goals have priority when there is a conflict (OECD, 2013a). Vodafone cited the UK Communications Act 2003 as an example:

It is not the case that a regulator can never be charged with promoting multiple objectives. This can be done successfully, provided that there is a clear hierarchy of objectives and a primary objective should exist to provide a ‘guiding principle’ as to how the regulator should proceed where there is conflict between objectives. This model exists in the UK Communications Act 2003, which established the independent communications regulator Ofcom. The Communications Act assigns an extremely broad range of duties to the regulator. However, it makes clear that Ofcom has two principle duties in carrying out its functions, which all other objectives are subject to. …In general, this framework works well with little debate as to how Ofcom ranks and promotes different objectives. (sub. 46, p. 7)

A clear hierarchy in legislation helps ensure that the trade-offs will be made in a consistent and predictable manner over time. Establishing a hierarchy in legislation also ensures that decisions about the relative importance of one goal or value over another are taken by those who are best placed and accountable for such choices.

F4.3 Legislative frameworks that keep the number of objectives and conflicts to the lowest possible number and provide a clear hierarchy of objectives help to support regulators in making consistent and predictable decisions.

More formal engagement, before and after legislation is passed
Uncertainty about the meaning of objectives undermines the credibility and effectiveness of regulatory regimes. Some submitters believed that there was too much vagueness in key regulatory concepts:

In the absence of clear definitions of subjective terms such as ‘public good’ and ‘fairness’ there is little or no benchmark against which the worth of regulation can be assessed. The absence of a clear and agreed definition of these outcomes makes it difficult to examine the claims of those promoting
regulation that their proposals are indeed worthwhile and cost effective. (Carter Holt Harvey, sub. 8, p. 3)

Guidelines could help to ‘flesh out’ and aid the interpretation of the regulatory objectives in legislation such as the Commerce Act 1986. The legislated objectives are necessarily broad and consequently open to multiple interpretations, which can create uncertainty for regulated entities. (PowerCo, sub. 14, p. 2)

However, it is notable that in several cases submitters had opposing views on whether a specific statute had clear objectives (see Box 4.3).

**Box 4.3 Is clarity in the eye of the beholder?**

**The Civil Aviation Act 1990**

The Civil Aviation Authority and Maritime New Zealand (sub. 15, p. 6) cited the Civil Aviation Act as a regime with a clear objective:

> There is a real need for a regulatory body to have a clear purpose (e.g. safety) which can be discharged in a way that is mindful of (or supports) other Government policy goals: In the CAA’s case, maintaining a safe civil aviation system is the primary goal, and this can be achieved whilst being mindful of other Government policy imperatives. (CAA, sub. 6, p. 5)

Even so, as noted above, Aviation New Zealand said that 2004 amendments, which “nobody understood” had eroded the clarity of the Act (sub. 36, p. 5).

**Reserve Bank Act 1989**

The RBNZ said that its legislative mandates (the Reserve Bank Act 1989, Reserve Bank Amendment Act 2008, Insurance Prudential Supervision Act 2010)

> are sufficiently clear as regards the Reserve Bank’s regulatory objectives while providing flexibility for interpreting the mandate in accordance with contemporary circumstances. The Reserve Bank’s mandate as regards prudential regulation of banks, for instance, is to promote the soundness and efficiency of the financial system. Although there are at times trade offs between soundness and efficiency and the interpretation of efficiency can in certain circumstances be ambiguous, the comparatively narrow role of the Reserve Bank’s mandate supports the clarity of its role. (sub. 9, p. 2)

However, Mortlock Consultants Ltd argued that the Act had internal tensions:

> the Reserve Bank of New Zealand Act 1989 … sets out the purposes for which banking supervision may be exercised (see section 68 of the Act). One aspect of these purposes is to promote ‘the maintenance of a sound and efficient financial system’. The Act provides no guidance as to whether, in the event that there may be a conflict or inconsistency between these purposes in relation to a particular matter (eg the exercise of a particular power), the Reserve Bank should primacy on soundness over efficiency, or vice versa. (sub. 31, p. 3)

**Commerce Act 1986**

Transpower identified Part 4 of the Commerce Act as having “plain English clear objectives” (sub. 32, p. 6). The Auckland Energy Consumer Trust and New Zealand Airports Association disagreed:

Simplicity and clarity of objectives should be included in the design of regulation and applied as a test of the quality of regulation. The Commerce Act Part 4 does not rate well on this test requiring four complicated purposes to be balanced. (Auckland Energy Consumer Trust, sub. 22, p. 6)

Regulated suppliers have consistently argued that the policy and legislative history of Part 4 supports a preference for promoting incentives to invest and innovate whenever the objectives may potentially be in conflict. In general, airlines and the Commerce Commission have disagreed. All parties have pointed to policy materials and Parliamentary debates to support their respective positions. However the trade-offs are managed, the divergence in opinion demonstrates there is limited guidance and a lack of clear and transparent frameworks in place for how the Commerce Commission is required to balance its competing objectives. (New Zealand Airports Association, sub. 33, p. 13)
Disagreement over whether or not a regime’s objectives are clear may reflect the different perspectives that various players bring to regulatory enforcement. Black (2008) noted that “regulators and lawyers have a different interpretative schema, even though both are interpreting legal norms … regulatory practices, understandings and reasoning can be very different from those of the legal interpretive community, even though the rules in question have legal status” (p. 447). Similarly, Kalderimis, Nixon and Smith (2013) observed that lawyers and economists often apply different frameworks to the issues of regulatory certainty and discretion:

On a classical legal account of rule of law values, the tendency has been to place certainty and discretion as diametric opposites. Economic literature, in contrast, has not been so dogmatic. (p. 2)

Tanner (2010) argued that the “clarity” and “accessibility” of a law is context-dependent:

To whom must legislation be clear: a specialist in the field? A highly intelligent person? Someone of average intelligence? Is ‘clear’ directed at the drafting or the policy, or both? Legislation has multiple audiences: law makers, users, scholars, judges and administrators. It can be difficult to lay down hard-and-fast rules in this regard. Much depends on the subject matter. (p. 23)

Given the number of groups affected by the regulation and the diversity of perspectives, one way to improve the clarity of regulatory regimes is to make more use of formal consultation processes before and after regulatory regimes are confirmed, to test whether:

- the regulatory objectives are clear and understandable; and
- their interpretation by regulators is appropriate.

The Commission considers that two processes in particular should be used more frequently and consistently. The first process is consultation on exposure drafts of bills before their introduction to Parliament. Although New Zealand’s Select Committee processes provide broad scope for industry and the public to review draft legislation, earlier consultation with affected parties can help identify and resolve problems, especially where the proposed regimes are complex or technical.15

The current Cabinet Manual guidance on consulting on draft legislation place significant weight on confidentiality:

…in some circumstances releasing an exposure draft of the legislation may be helpful. In considering consultation with organisations outside the public sector, Ministers should consider the confidentiality constraints. …At every stage of its development, draft legislation is confidential and must not be disclosed to individuals or organisations outside government, except in accordance with the Official Information Act 1982 or Cabinet-approved consultation procedures. Any such release or disclosure must first have the approval of the Minister concerned. Unauthorised or premature disclosure of the contents of a draft bill could embarrass the Minister, and imply that the role of Parliament is being usurped. Cabinet, government caucus(es), and Parliament must always retain the freedom to amend, delay, or reject a bill. (Cabinet Office, 2008)

While in some circumstances it clearly would not be appropriate to circulate draft legislation for comment,16 the current rules appear unduly restrictive. Public consultation on draft bills need not limit the ability of Cabinet or Parliament to change, defer or decline the proposed legislation. Subject to such caveats as necessary to protect Cabinet flexibility and the public interest, the burden in the Cabinet Manual could be reversed to make exposure drafts a standard step in consulting on significant changes to regulatory regimes.

R4.1 The Cabinet Manual should be amended to set a general expectation that exposure drafts will be published and consulted on before introducing into Parliament legislation that creates new regulatory regimes or significantly amends existing regimes.

15 The Commission notes that the government has used exposure drafts when developing the new workplace safety regime.
16 For example, it may not be appropriate to release exposure drafts, where this could enable individuals or firms to arrange their affairs in a way that evades the new regulatory regime.
The second process is consultation by regulators on how they interpret and intend to carry out their legislative mandate, including how they will make trade-offs. One example was the initiative of Electricity Authority in late 2010 to publish and seek feedback on a draft interpretation of its statutory mandate. The aim of this consultation process was to “assist the Authority Board to make consistent decisions, and … assist staff and advisory groups to develop Code amendment and market facilitation proposals for the Authority Board’s consideration” (Electricity Authority, 2011, p. 1). The Electricity Authority also noted in its submission that the interpretation helps promote a high-performance culture amongst its staff (sub. 50). As Mortlock Consultants Ltd noted, some regulators are required by statute to publish statements of their approach to regulation...however, this requirement is not consistently applied across regulators; many are under no parallel obligation. Partly as a result of this, there is a lack of transparency in the policy framework applied by some regulators in interpreting their responsibilities and in exercising their powers. This impedes the accountability of regulators and makes it more difficult for regulated entities to interpret the actions of their regulators. (sub. 31, p. 6)

Requiring regulators to publish and consult on their interpretation of their mandate will not resolve all issues, as commentary about the Electricity Authority’s interpretation shows (see, for example, IAG, sub. 10, p. 13; Mighty River Power, sub. 30, pp. 3-4; Molly Melhuish, sub. 42, p. 12; Genesis Energy, sub. 48, p. 5; Willis, 2012). In particular, it is no substitute for Parliament making judgements about competing values and expressing these in legislation. Even so, the Commission considers that applying formal obligations more consistently on regulators – preferably in legislation – to publicly outline how they intend to implement their statutory roles and make trade-offs will help promote greater understanding of regulators’ roles and approaches. It should also encourage greater regulator accountability.

R4.2 The next version of the State Services Commission’s guidance on machinery of government issues should set an expectation that, where a new regulatory regime is established, the entity responsible for implementing the regime should have a legislative obligation to publish a statement that explains its interpretation of its mandate, to consult on that statement, and keep it up to date.

Another way to promote greater role clarity used or considered in other countries is ministerial statements or directions on how regulators should conduct themselves, or the specific objectives that they should prioritise.

The UK Government recently consulted the public on its proposal to introduce a “growth duty” for non-economic regulators. The aim of the growth duty would be to “make it clear that regulators can and should be mindful of the economic consequences of their actions, thereby stimulating improvements in business experience of regulation and creating a regulatory environment conducive to growth” (Department for Business, Innovation and Skills, 2013). MBIE recommended that the Commission explore 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. (sub. 52, p. 6)

Such mechanisms can be useful, especially for promoting accountability and general obligations. There is scope to use existing ministerial powers under the Crown Entities Act 2004 and Public Finance Act 1989 to give greater guidance about the respective roles of different organisations within a regulatory regime.

Even so, these tools have limitations. Ministerial directions may not be appropriate for regulatory regimes where a high degree of regulator independence is important. For this reason, the Crown Entities Act constrains the ability of ministers to direct independent Crown entities. It also constrains the performance of statutorily independent functions. As a top-down mechanism for clarifying regulatory roles, ministerial directions would not encourage engagement with regulated parties in the same way that interpreting mandate process would. And because Crown entities must act in line with their legislation, statements of
intent may have only limited effect in making regulatory systems coherent, where conflicts exist in the underpinning laws.

Functions of regulators

Giving some functions to regulators or placing regulators within some types of agencies can affect how effectively regulatory regimes are enforced and reviewed. Functions identified as potentially conflicting with regulatory management and enforcement include policy development, industry promotion and revenue collection.

- **Policy development**: Organisations with policy development and regulatory functions may be more subject to lobbying by regulated firms, may have incentives to use the policy process to expand the scope of their regulatory roles, may be drawn into political processes and be seen as less able to make impartial decisions. The close proximity of regulators to industry may lead to a narrower perspective being applied to policy than a public service department might apply (VSSA, 2009). Involving regulators in developing policy may also encourage an excessive reduction of risk (VCEC, 2005b, p.305).

- **Industry promotion**: Organisations that are tasked with regulating an industry and promoting its development may be less inclined to rigorously enforce compliance or may view the interests of regulated firms and the public as synonymous.

- **Revenue collection**: An agency responsible for regulating and collecting revenue from an industry could have incentives to take a weak enforcement approach. For example, the US National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling (2011) found that the combination of regulatory and royalty collection functions in one agency “led inevitably to internal tensions and a confusion of goals that weakened the agency’s effectiveness and made it more susceptible to outside pressures” (p. 255).

The Victorian State Services Authority has concluded that non-regulatory functions such as service delivery should be separated from significant regulatory functions, to avoid confusion about agency responsibilities (VSSA, 2009).

Aligning incentives in organisational design

Regulators find it hard to carry out some activities. For example, having an agency regulate an industry’s conduct and collect revenues from that industry for the government is likely to create real conflicts or perceptions of conflict that will undermine the agency’s legitimacy. Ideally, regulatory and revenue collection functions should be separate. If they are carried out by the same agency, then there should be clear and strong distinctions between the teams carrying out the functions and their reporting lines (OECD, 2013a).

Giving a regulator industry promotion functions can create similar tensions to those that arise with revenue collection, although the extent and severity of the tension depends on the nature of the industry and regulatory system. The key issue with giving regulators industry promotion functions is whether the industry’s growth is compatible with the objectives of the regulatory regime.

The NZFGC argued that the dual role of the Ministry for Primary Industries as market access negotiator and safety regulator did not present obvious conflicts, and safety was generally a condition of access:

> MPI [the Ministry for Primary Industries] is responsible for market access of food products and for their regulation as was the New Zealand Food Safety Authority. The nexus worked excellently in terms of focussing the regulations on the bottom line for population safety and identifying those aspects that are not safety related and are worthy of negotiation. (sub. 35, p. 4)

Aviation New Zealand commented that the Civil Aviation Authority’s role in promoting New Zealand offshore reinforced its safety and security objectives, as the ability of New Zealand aviation firms to grow depends on the robustness of our regulatory regime (sub. 36, pp. 6, 8-9).
The importance of agency mission and culture
The principle of compatibility should also be applied before decisions are taken on agency mergers or new regulatory functions are allocated to an existing agency. In particular, the mission and culture of the existing or new agency must be compatible with the objectives of the new regulatory regime. The Council of Trade Unions (CTU) and MBIE highlighted this point in their submissions:

A much more important matter than whether policy and implementation should be split is the objective of the organisation carrying out the policy and/or implementation role. The Objective (such as being ‘business-facing’) can threaten the independence, or perception of independence, of either role. (CTU, sub. 25, p. 15)

From our experience indicators that a regulatory system is not meeting its objectives or may be at risk of systemic regulatory failure include … organisational norms and values which are not fully aligned with regulatory systems’ objectives. (MBIE, sub. 52, p. 4)

By way of example, the CTU cited Australian research that found that “the location of an OHS [Occupational Health and Safety] inspectorate in a government agency whose primary responsibility is the economic success and productivity of the very industry it purports to regulate is a prescription for disaster” (CTU sub. 25, pp. 12-13). Regulator culture is discussed in more detail in Chapter 7.

One example where policy advisers did explicitly analyse which agency should be given responsibility for a regime is the Psychoactive Substances Act 2013, where the Ministry of Health assessed six possible agencies against the criterion of “suitability” – that is, “there needs to be an appropriate ‘fit’ between the new regulator and the agency where it sits” (Ministry of Health, 2012, pp. 13-15).

In giving a new regulatory function to an existing agency, care should also be taken to ensure that the new obligations will get sufficient resource and attention. As a Victorian government policy statement on the governance of regulators noted:

Given that regulatory agencies have limited staff and financial resources there will always be competition between various functions for priority. It is important for regulators to ensure their obligations to promote regulatory compliance are given sufficient focus. (Government of Victoria, 2010)

This was one of the issues that the Pike River Royal Commission identified in the Department of Labour’s occupational health and safety role:

Health and safety in New Zealand was not led by a body for which improving health and safety was its sole, or even major, objective. Health and safety was just one of the responsibilities of a department with many responsibilities. This diluted the attention paid to health and safety and contributed to an unwieldy structure in which senior officers had limited opportunities to develop health and safety expertise. (Royal Commission into the Pike River Coal Mine Tragedy, 2012, p. 291)

Regulators and the provision of policy advice
Most regulators need policy functions so they can interpret and implement their legislative obligations. As the Victorian Competition and Efficiency Commission observed,

While elected governments, not regulators, should determine policy objectives … these objectives are typically identified only in general terms (for example, achieving ‘safety’ and ‘amenity’) and may evolve over time as circumstances change. Many decisions (sometimes by the regulator rather than the government) influence how and to what extent policy objectives are pursued, and the development of new policies. (VCEC, 2005b, p. 303)

Much debate about regulator involvement focuses on strategic policy – that is, developing legislation and subordinate legislation, advising government on how to deliver government programmes, and reviewing legislation or government programmes (see Box 4.4 below).
Box 4.4  Submitters’ views on regulators having policy responsibilities

For

Civil Aviation Authority

In order to achieve the CAA’s policy obligations, our operational delivery and policy-making needed to be appropriately ‘engaged’, one with the other and with the Ministry of Transport. Regardless of form, an agency such as the CAA needs some policy capability in order to be able to engage with policy agencies – otherwise it is rather like two different language speakers trying to communicate without a translator. The CAA also needs an internal policy capability to develop the systems interventions and internal policy and procedures for its own operations. From the CAA’s perspective, for a regulatory agency not to have some policy capability would reduce agency’s ability to properly engage in government processes in three ways:

- When it wishes to advocate for a change in policy settings, which might not result in rule (regulatory) changes;
- When being asked by Government to provide advice on policy issues; and
- When engaging in the international arena and seeking to influence international standards beyond simply ‘technical requirements’. (sub. 6, p. 17)

RBNZ

Prudential regulation is a highly-specialised and technical area and in practice there is a lot of interaction between the individual teams. This interaction exists in the policy-making stage as well as when it comes to supervision and enforcement of regulatory requirements. The Reserve Bank believes that having all of these functions unified albeit spread across different, specialised teams is the correct approach to prudential supervision. It allows for synergies and economies of scale to be exploited which leads to more efficient regulation and policy-making than other constellations would. Separating policy-making and compliance functions can lead to duplication of effort and raises the scope for misinterpretation of policy aims. (sub. 9, p. 3)

Council of Trade Unions

The experience of implementing and working day-to-day with policies must inform their development or they will be forever repeating previous mistakes. That is much easier done in one organisation, with ‘Chinese wall’ separation where necessary. In addition, in a country of the size of New Zealand, finding the expertise and experience required for effective policy advice as well as for effective implementation can often be difficult or impossible without thinning both to an unwise level. We believe that the principle of a policy/implementation split should be reviewed. (sub. 25, p. 15)

Against

ANZ Bank Ltd

Our primary concern is to ensure that policy-making and regulation are kept distinct in order to improve regulatory processes and outcomes. …The risks where a regulator has such a role include a number of regulatory shortcomings:

- it affords a regulator discretion as to the objectives it should achieve and how it should achieve those objectives, which can promote unpredictable and inconsistent regulation;
- it limits the role of external accountability mechanisms as regulatory objectives have not been set by an external party to which the regulator is directly responsible; and
- it can frustrate parties that engage in regulatory processes as consultation on policy decisions may not be as open and transparent as for regulatory decisions where the primary concern is implementation to a particular factual context. (sub. 24, p. 8)

Mortlock Consultants Ltd

There is a fundamental conflict between promoting legislation (and preparing cabinet requests for approval and drafting instructions) and administering the same legislation. This arrangement
Involving regulators, as the implementers of regimes, in developing strategic policy is critical for good quality outcomes. As Scott (2001) stated:

for strategic policy to have such influence it must be integrated with, and have its foundation in, the regular flow of detailed policy and organisational operations. Otherwise, the grounding of strategy in the practicalities of the daily work of government is lost. Vital information and advice lies with customers and the people who deal with them, in addition to the information from more formal processes of analysis and consideration at the top levels of management. With processes of this kind, the strategic policy is not only more likely to be robust, but also more likely to be implemented, because the operational managers understand it and have the opportunity to make inputs. (p. 335)

The question is how that involvement should take place, and where the limits are. Ideally, strategic policy development should be structured in way that taps the expertise and experience of regulators while also providing a dispassionate and balanced assessment of the issue. Regulators providing strategic policy advice as part of a contestable process may also be beneficial.

Problems can arise where regulators have the sole or main responsibility to review underpinning legislative or policy frameworks. Regulators – as the people involved on a daily basis in managing a regime – may be less able than others to step back and coolly assess whether the regime is still required and fit for purpose. As the New Zealand Airports Association observed, regulators may also be less inclined than external parties to identify any problems that their approach to implementation had created (sub. 33, p. 14).

### F4.5

Regulator involvement in providing strategic policy advice is important for effective regulatory outcomes. Strategic policy should be developed so that it taps the experience of regulators and provides a dispassionate assessment of the issue. To ensure this balanced assessment, regulators should not have the sole or main responsibility for reviewing underpinning frameworks.

### Separating rule-making from rule-enforcement

A related issue is whether a regulator should have the twin functions of making rules and enforcing them.

A number of submitters, mainly from firms in the energy sector, argued that these functions should be allocated to separate regulatory organisations (Genesis, sub. 48, p. 3; Mighty River Power, sub. 30, p. 11; Vector, sub. 29, p. 27; Minter Ellison Rudd Watts, sub. 28, pp. 12-13; Electricity Networks Association, sub. 27, p. 9; Powerco, sub. 14, p. 3; and Trust Power, sub. 7, p. 4). Possible benefits that submitters cited for separating the two functions included:

- elimination of potential conflicts of interest and encouragement of “the drafting of clear rules that could be readily interpreted and applied by a disinterested body” (Powerco, sub. 14, p. 3);
- enhanced “policy credibility” and reduced uncertainty (Minter Ellison Rudd Watts, sub. 28, p. 13);
- cost savings, due to less need for expensive appeal and merits review processes (Vector, sub. 29, p. 27).

A number of submitters referred to the Australian Energy Regulator (AER) – which monitors and ensures compliance with the regulatory regime – and the Australian Energy Market Commission (AEMC) – which reduces the accountability of the legislative-making process, weakens the effective scrutiny of the proposed legislation and creates a significant risk of over-regulation and too much power being vested in the regulatory agency. (sub. 31, p. 7)

**Mixed**

**Federated Farmers**

Federated Farmers can see advantages and disadvantages from having a split between policy-making agencies (usually a government department) and regulatory agencies (often a separate Crown entity of some sort). (sub. 11, p. 10)
develops and sets rules for energy markets – as examples of a split between those making the rules and those enforcing them.

The question of whether separating the functions would yield net benefits depends on a number of factors. The APC has considered the question of separation in a number of its inquiries.\(^{17}\) Although it has often preferred separation, the APC noted that the question of which “governance model is best depends on circumstances. Regulatory separation is justified where gains from increased probity, increased transparency, reduced scope for regulatory error and any other gains in better governance are warranted by the loss of economies of scope or timeliness” (APC, 2001a, p. 305).

The nature and scale of gains from separation are likely to vary, depending on issues such as the details of the regime and the capability of governors and staff in both agencies. For example, the Australian energy regime has structural separation and merits review options; whether separation has created savings through less recourse to merits review is unclear. Similarly, an assessment of the Australian energy merits review process found that the “rule changes currently under consideration by the AEMC tend to have the effect of affording the AER greater discretion in its decision making” (Yarrow et al 2012b, p. 52). Greater discretion is not necessarily a bad outcome, but it does bring into question arguments that separation inherently reduces uncertainty for regulated firms.

Structural separation often slows down decision-making processes. While slower processes will be beneficial in some cases, in others it will create net costs. In some instances of New Zealand regulation (in particular transport), separating rule-making and rule-enforcement functions appears to have unnecessarily hampered the ability of regulation to keep pace with technology or community expectations. This aspect is described more fully in Chapter 5. In the case of telecommunications regulation, the APC preferred keeping the functions together, on the grounds that a dynamic industry needed prompt regulatory procedures and other remedies would better manage the risks of regulatory creep and bias (APC 2001a, p. 305-306).

**Structural separation is one approach; there are others**

Transparency, probity and good decisions are clearly critical regulatory outcomes. While they are of general importance, they are especially important in regimes where regulatory errors can significantly impact the public.

As the APC’s recommendation on telecommunications regulation indicates, structural separation is just one way to deliver these outcomes. Other possible options include:

- clear statements of regulatory objectives, with conflicts between objectives eliminated or minimised (as discussed above);
- obligations on regulators to explicitly state how they will interpret their mandate (as recommended above);
- organisational or governance arrangements that give a regulator more independence in decision making (Chapter 5);
- stronger consultation obligations (consultation requirements and regulator engagement more broadly are discussed in more detail in Chapter 8);
- clear review and appeals avenues (Chapter 10);
- obligations on regulators to report on specific aspects of their processes or performance (Chapter 14); and
- systematic reviews of regulatory regimes, to check they are still fit for purpose and performing efficiently and effectively (Chapter 15).

\(^{17}\) Examples include the review of telecommunication competition regulation (APC, 2001a), price control legislation (APC, 2002a), the national access regime (APC, 2002b), the gas access regime (APC, 2004), and electricity network regulation (APC, 2013c).
A combination of these other options may provide equivalent levels of transparency, probity and accuracy with lower costs or less disruption than a structural solution.

Creating separate bodies so that one body is responsible for making rules and the other for enforcing them can have benefits, such as greater transparency, probity and good decisions. Even so, whether structural separation creates net benefits will depend very much on the details of the regulatory regime. Combinations of other regulatory design options (such as clearer regulatory objectives, stronger reporting and consultation obligations) may provide equivalent benefits, with lower costs and less disruption.

Regulatory overlaps and conflicts

Regulatory regimes may not adequately take account of the role of other regulators, or the compliance burden that multiple agencies and regimes place on regulated entities. In part, this reflects the structure of government; regulation that “tends to be developed within individual portfolios or jurisdictions, with those inside a particular “silos” less aware of, or concerned about, outside regulation, or whether information/reporting requirements overlap with those of another portfolio or jurisdiction” (Taskforce on Reducing Regulatory Burdens on Business, 2006). The gradual growth of regulatory roles or functions over time is another source of trouble:

Where legislators or governments incrementally add on roles and functions … there is a blurring of roles and functions which can create a significant barrier to effective regulatory operation due to conflicting mandates. (Maritime New Zealand, sub. 15, p. 3)

Regulatory overlaps and conflicts appear to be more widespread in countries with federal systems, where the different levels of government may find it hard to coordinate. In this respect, New Zealand’s centralised constitutional system may be beneficial, as it offers more scope to control and reduce regulatory overlap.18

Improving underlying frameworks and coordination and management practices can reduce overlaps and conflicts.

Improving underlying frameworks

The best way to reduce regulatory overlaps is to review the relevant legislative frameworks, as these are the direct cause of conflict. New Zealand regulatory systems can struggle to keep current and coherent, due to a weak review and evaluation culture and difficulties in gaining access to time at Parliament in the absence of a crisis. A more strategic approach is needed to revisiting regulatory regimes, and the Commission sees a case for periodic, systematic and independent reviews of regulation. This case is outlined in Chapter 15.

These reviews should take into account the full range of legislation that affects firms and individuals in the regulated sectors, to eliminate unnecessary duplication and conflicting obligations. The reviews should also revisit allocating regulatory functions and responsibilities between agencies, to ensure that this provides the best balance of:

- a clear administrative structure that all participants in the regulatory system easily understand;
- effective feedback loops between standard-setting, approval, monitoring and enforcement functions; and
- the allocation of functions to those with the appropriate and relevant expertise and information.

Improving coordination and management practices

Coordination and management practices can also help to manage issues that arise from overlapping regulatory regimes. At the less formal end are practices such as regular meetings of agencies acting in a common sector. One example is the Council of Financial Regulators, which brings together the Treasury,

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18 Even so, the Commission has previously identified coordination problems between central and local government in New Zealand. These problems have impaired the effective operation of regulatory regimes (NZPC, 2013a).
RBNZ, FMA and MBIE on a quarterly basis to share information, consider financial market issues and trends, and coordinate responses as needed. More formal practices include cooperative agreements (such as MOUs) and exemptions.

**Cooperative agreements**

Cooperative agreements can help to reduce the conflicting or duplicated obligations of firms by:

- delineating respective roles and responsibilities;
- establishing processes by which regulators will handle cases where more than one agency has an interest; or
- agreeing to common principles or approaches agencies will apply in enforcing their regimes.

Examples of such agreements include MOUs and shared guidance notes.

New Zealand regulators already use MOUs to manage regulatory overlaps. Of the 18 regulators that the Commission surveyed who identified that their roles overlapped with others, 14 (78%) had formal arrangements such as MOUs in place.

Even so, a formal agreement such as a MOU, even one recently reviewed, does not guarantee the administration of regulation will improve (that is, reduce costs and/or improve effectiveness), and does not necessarily maximise the opportunities for improvement. Rather, the key determinants of an agreement’s benefits are (1) the content of the agreement, (2) the extent to which it adequately addresses areas of shared interest, and reduces overlap and duplication, and (3) the extent to which it is followed in practice. (VCEC, 2009)

To be most effective, cooperative agreements should:

- **be regularly reviewed**, to ensure that they are still fit for purpose and being used effectively;
- **be publicly available** (such as on agency websites), so that the nature of the relationship is clear. Transparency also means that any shortcomings in the agreement “would be more readily recognised”, aiding any subsequent review (VCEC, 2009);
- **provide clear guidance to regulated firms and individuals**: agreements such as MoUs are often expressed in terms of high-level principles that the two agencies will follow. To reduce confusion and improve compliance by regulated firms and individuals, plain English guidance material should also be provided, outlining how the agencies will respond in specific circumstances.
- **be empowered by legislation**: ideally, legislation “should explicitly empower regulators to cooperate with other agencies and bodies in pursuit of the regulator’s objectives. This will allow regulators to simplify their dealings with business and other entities through delegation, information sharing, joint regulation, and co-regulation” (Government of Victoria, 2010).

Cooperative agreements such as MOUs should not be viewed as a permanent substitute for a clear and efficient distribution of functions, but they can help manage issues until the regulatory regime is more substantively reviewed. The more complicated a cooperative arrangement is, the more likely the underlying regimes will need reviewing.

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**F4.7** Cooperative arrangements like Memoranda of Understanding play an important role in managing regulatory overlaps. To be most effective, they should be reviewed regularly, be publicly available, provide clear guidance to regulated firms and individuals, and be empowered by legislation.
Exemptions
Exemptions are another way to manage overlaps. One regulator explicitly permits a firm or individual to not comply with their regime, on the grounds that their compliance with another, similar regulatory system provides sufficient assurance.

A New Zealand example of an exemption power is section 148 of the Financial Advisers Act 2008, which allows the FMA to exempt people or services (or classes of people or service) where it is satisfied that:

(a) the costs of compliance with the relevant obligation—
   (i) would be unreasonable; or
   (ii) would not be justified by the benefit of compliance; or
(b) the relevant person, service, or transaction is subject to the regulations of an overseas jurisdiction and the FMA is satisfied that, in the circumstances, the protection of the New Zealand public is unlikely to be prejudiced. (section 148(2))

Allowing regulators greater room to grant exemptions may also enable broad-based regulatory regimes to adapt to changing business practice and circumstances:

While there should be an appropriate degree of emphasis on tailoring the scope and effectiveness of regulatory regimes, governments will often lack the detailed information necessary to do so efficiently. Even if governments could do so, particular concerns may abate over time. As a result, empowering regulators to grant exemptions from generic, catch-all regulation is likely to be the most efficient and responsive approach to ensuring fit-for-purpose regimes in a number of cases. (ANZ, sub. 24, p. 9)

A version of exemptions commonly used in trade is equivalence arrangements, where a good that has passed similar regulatory tests in approved foreign jurisdictions is considered to have met the necessary tests in the domestic market.

Exemptions often require regulators to exercise discretionary powers. To ensure these powers are used appropriately and consistently, principles or criteria guiding their use (such as requiring some form of cost-benefit test) should be included in legislation, and regulators should publish their reasons for granting exemptions.

4.5 Summing up
Clear regulatory roles, duties and objectives are important for operating regulatory regimes effectively and efficiently. But there are a number of reasons why clarity may be lacking, including poor choices of regulatory standards; insufficient attention by policymakers to the definition of regulatory objectives; placing regulatory responsibilities in agencies that also have functions, missions or cultures that act counter to the objectives of the regime; and inadequate consideration by advisers or policymakers in designing a regime to the roles of existing agencies and regimes. This chapter laid out possible actions to minimise these problems.

While the actions outlined in this chapter will help to reduce the prevalence and impact of poor role clarity, they will not eliminate it. There are at least two structural reasons why clarity is unlikely to ever be fully achieved across all regimes:

- The sheer volume of legislation already on the statute books works against clarity: The US Government Accountability Office commented in 1981 that it is “virtually impossible for the Congress not to enact laws whose goals will not compete with other goals previously enacted into law” (US GAO, 1981, p. 23).
Similar issues are likely to apply in New Zealand, especially given the country’s comparatively heavy reliance on statutes.

- **Different participants in regulatory regimes bring different perspectives:** As noted above, lawyers, regulators and economists can apply “different interpretative schema” to the same principle or concept. Other stakeholders may bring other views. Although greater efforts to work through these perspectives in the design phase—as recommended in this chapter—should increase the likelihood of reaching consensus on regulatory principles and concepts, they do not guarantee agreement.

This is not to say that policymakers should give up the pursuit of clear regulatory roles, duties and objectives. But it is worth viewing this pursuit as an ongoing process—much like the “regulatory cycle” of design, implement and review—rather than a journey with a fixed destination.
5 Regulatory independence and institutional form

Key points

- The institutional form of regulators and the degree of independence with which they are expected to undertake their regulatory functions are key considerations for designers of regulatory regimes.

- There is widespread agreement on the importance of regulation being undertaken by independent regulators. Independence is multi-faceted and is more than a matter of legally designating an agency as “independent”.

- Independence is a key institutional factor that will support regulators adopting effective regulatory strategies. Designers of regulatory regimes need to carefully appraise the arguments for and against regulator independence. Arguments for political control must be weighed carefully against the benefits of providing a credible long-term commitment to an impartial and stable regulatory environment.

- Regulators often have to work with legislation that is outdated or not fit-for-purpose. Their independence could be enhanced by:
  - ensuring greater consistency in allocating legislative material between primary legislation and secondary legislation (government regulations and deemed regulations); and
  - looking for opportunities to delegate more rule making to regulators, particularly in areas that experience rapid technological change, subject to important checks.

- Political imperatives will inevitably diverge sometimes from the objectives of independent regulators. While political interference in independent regulatory regimes is undesirable, providing transparent mechanisms for political intervention is preferable to undertaking more fundamental and ad hoc regulatory reform to solve political problems. Providing such mechanisms can actually enhance the independence of regulators. This also allows ministers to be properly held to account for their actions.

- Any mechanisms to provide for political intervention should be transparent, and operate in a way that does not undermine the regulator or encourage regulated parties to work around the regulator.

- In many areas government is both a funder of services and a regulator – for example, in aged care. Government often uses its contractual levers instead of regulatory powers to manage concerns about the quality of government-funded services. While this may mean any quality concerns are quickly resolved, it can obscure issues about system performance.

- In practice, choices around institutional form are more important because of what they signal about expected independence rather than for the legal constraints and freedoms associated with particular agency forms. As such, careful attention must be paid to establishing clear expectations, norms and cultures in new independent regulators.

- Government has signalled an intention to consider reallocating some functions currently undertaken by Crown entities (which are operationally independent) into a new type of institutional form known as a departmental agency.
  - Such agencies are not operationally independent, so careful attention will need to be paid to the appropriate degree of independence required of individual regulatory powers as they are
transferred.

- The Commission is concerned at the potential for confusion around the respective roles and responsibilities of the chief executives and ministers of departmental agencies and host departments.

- The Minister of State Services and the State Services Commissioner should be involved in reviewing agreements to establish departmental agencies to ensure that accountabilities are clear.

- Regardless of the advantages or disadvantages of particular institutional forms, the disruptive effect of institutional change on the smooth operation of regulatory functions must be acknowledged. During periods of institutional change, leaders need clear strategies for maintaining the effective operation of regulatory functions.

### 5.1 Regulatory independence

Independent regulators are free from the direct control of politicians and regulated parties. Independence prevents a regulator being used for partisan purposes, and promotes public confidence in the decisions of the regulator. Independence is not a binary condition: regulators can be more or less independent in a range of ways.

The Organisation for Economic Co-operation and Development (OECD, 2013a) says that some of the consequences from a more independent regulator are:

- more credible commitments from government to the administration of regulation over the long term;
- more consistent and stable decision making;
- the avoidance of many potential conflicts of interest; and
- the development of expertise in the regulatory field.

Most submitters agreed that independence was an important feature of regulators.

Carter Holt Harvey supports those aspects of the discussion document which highlight the value of regulatory independence, particularly where the determination of compliance with regulation is a matter of subjective judgement. (sub. 8, p. 8)

Regulators should be independent both from political interference and from capture by those being regulated. (Federated Farmers, sub. 11, p. 10)

Independence from political interference is viewed as critical in the economic regulation of infrastructure in particular and Ministers should be limited in their ability to direct the regulator. The appropriate mechanism for policy direction by government is by way of legislation, and refining regulatory design arrangements. (Vector, sub. 29, p. 16)

However, submitters were careful to emphasise that independence needed to be accompanied with commensurate accountability.

The Commission’s survey of New Zealand businesses (Colmar Brunton, 2013) revealed an overwhelming perception that politicians are involved in regulatory decisions and processes, with 87% believing this is always, mostly, or sometimes the case. Opinion on the appropriateness of this involvement is slightly more divided, but almost two-thirds (65%) indicate it is at least sometimes appropriate (Figure 5.1).
Figure 5.1  Businesses’ perceptions of political involvement in regulatory decisions and processes

Politicians become involved in the decisions or processes of regulators in New Zealand

<table>
<thead>
<tr>
<th></th>
<th>Strongly agree</th>
<th>Agree</th>
<th>Neither agree nor disagree</th>
<th>Disagree</th>
<th>Strongly disagree</th>
<th>Don’t know</th>
</tr>
</thead>
<tbody>
<tr>
<td>NZ</td>
<td>5%</td>
<td>26%</td>
<td>56%</td>
<td>11%</td>
<td>11%</td>
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It can be inferred that businesses believe there is more political involvement in regulatory processes than is desirable. Notably, firms in the electricity, gas, water and waste industries were most likely to believe politicians become involved in regulatory decisions and processes, with 55% reporting this is “always” or “mostly” the case.

However, businesses are clearly comfortable with a reasonable level of political involvement in at least some regulatory decisions and processes. This is a surprising finding that stands in contrast to the views expressed in submissions to the Commission.

When is independence needed?

There is a lot of literature about when independent regulators are desirable. Figure 5.2 presents two different views, with the OECD focusing on formal considerations and the Victorian State Services Authority (VSSA) taking a more practical view of the outcomes of independent regulators.

Figure 5.2  Two views on when independent regulators are desirable

**OECD: Best practice principles for the governance of regulators (2013)**

- Independent regulators should be considered when:
  - a regulator needs to be seen to be independent to maintain public confidence
  - government and non-government entities are regulated under the same framework
  - decisions have a significant impact on particular interests, so impartiality must be protected.

**Victorian State Services Authority: Review of the rationalisation and governance of regulators (2009)**

- Independent regulators are established to:
  - provide credible commitments over the long term
  - create a stable and predictable regulatory environment
  - develop focus and expertise
  - manage political risks.

The Commission has developed a framework that draws on a range of sources. It highlights the circumstances that would indicate a need for less or more independent regulation (Figure 5.3).
Public confidence is highlighted by the OECD principles (Figure 5.2), and is also a key factor indicating a need for an independent agency form in the State Services Commission (SSC)'s guidance on machinery of government (2007). As such, public confidence in the impartiality of the regulator has been included in the framework.

This framework also reflects a number of comments and suggestions from submitters on the draft framework presented in the Commission’s issues paper (Box 5.1).

**Figure 5.3  Features indicating a need for less or more regulatory independence**

### Less independence
- Decisions involving clear value judgements (which might be appropriately made by elected officials)
- Where political control is needed to guard against "regulatory capture" by regulated sector
- Decisions with significant fiscal implications or which are integral to a government’s economic strategy
- Decisions involving the significant exercise of coercive state power (for example, policing, taxation)
- Flexibility is needed to take account of political imperatives

### More independence
- Decisions where the costs are long term, and likely to be undervalued due to a focus on electoral cycles (for example, economic policies that risk long-term inflation)
- Decisions weighing a politically powerful private interest against a dispersed public interest
- Decisions requiring a substantial degree of technical expertise, or expert judgement of complex analysis
- Decisions whether the causal relationship between the policy instrument and the desired outcome - the *transmission mechanism* - is complex or uncertain
- Regulatory regimes where a consistent approach over a long period of time is needed to create a stable environment
- Regulation of state power, or government-funded services
- Regulation of government and non-government entities under the same framework
- Where decisions need to be taken urgently
- Where public confidence that the regulator is impartial is important

**Box 5.1  Submitters’ view on when independence is less or more required**

There was general support for the draft framework as a tool for considering when independence should or should not be provided for in the design of regulatory regimes. A number of submitters suggested changes to the framework:

- The Financial Markets Authority (FMA) said: “We support the model, and would perhaps add more independence (but with retrospective review) where a decision must be taken with urgency in the public interest”. (sub. 53, p. 4)

The Commission agrees that where there is a need to act swiftly to mitigate a significant identified risk,
Defining “value judgements” is difficult. The framework indicates that less regulatory independence may be appropriate for decisions involving clear value judgements, while more independence is appropriate for

- Air New Zealand argued there were a number of circumstances where a “NZ Inc.” approach should be taken to shaping regulation. It provided the example of authorising international airline alliances, where it thought Ministerial decision making was appropriate, because a pure competition approach could not take account of the “diplomatic, international legal and market distortion considerations”, particularly given the tendency for state ownership in international airlines. (sub. 47, p. 3)

The Commission is wary of this line of argument. Malyshev (2006) argues that independent regulators “shield market interventions from interference from political and private interests” and are particularly necessary for “marking out the separation of the state’s roles as policy-maker and owner of productive assets”, especially where the state has a significant ownership interest in network industries. While the Commission agrees that decisions with significant fiscal implications or which are integral to a government’s economic strategy should not be taken independently of political control, state ownership of firms alone should not justify less independent regulation.

- The Food and Grocery Council took issue with a number of the features that tended to indicate a need for less independence:

  NZFGC does not believe that the framework for determining regulatory independence can be considered in isolation. We suspect that “Where political control is needed to guard against regulatory capture” should not feature as an indicator of a regulator needing less independence … Neither do we agree that less independence should allow for political imperatives nor that government-funded services necessarily warrant more independence … It is about what works best for a sector and New Zealand rather than hard and fast rules or, in this case, frameworks. (sub. 35, pp. 5-6)

This is an important point: frameworks are a useful guide for the designers of regulatory regimes, but they need to be combined with careful analysis about the particular circumstances, rather than being applied in a rote way.

In response to the Commission’s issues paper, submitters also commented on dangers associated with a lack of independence:

- Internet New Zealand argued that political decision making over whether regulation should be applied to services has been lobbied by firms seeking to avoid regulation, to the detriment of the public interest:

  Under schedule 3 of the Telecommunications Act, the Telecommunications Commissioner has to recommend to the Minister any new regulated service and the Minister/Government has to accept the recommendation for the regulation to be introduced. This lack of independence was initially considered to be a safety net to allay fears about overzealous regulators. There are instances where those proposed to be regulated have used this safety net to game and significantly delay the regulatory process. (sub. 45, p. 9)

- Business New Zealand noted that a lack of regulator independence can encourage regulated firms to lobby at a political level, rather than engaging with the regulator directly, with the effect of weakening the regulator. Discussing the old electricity regulator, they said:

  The Electricity Commission … combined the worst practice of having multiple and confused objectives, a board appointed exclusively by the Government of the day and a requirement to have regard to government policy statements. In other words, the industry had absolutely no long-term certainty. Ironically, this led to the explosion in the growth of the political market, as industry turned away from trying to influence the design of the electricity market, and instead lobbied Government rather than apply its effort at influencing the regulator. (sub. 19, p. 12)
decisions requiring a substantial degree of technical expertise, or expert judgement of complex analysis. Many such technical decisions will also entail value judgements. In these circumstances it is appropriate to have more independence so that the value judgements can be informed by a proper understanding of the technical matters at stake. The OECD notes:

For example, controversial planning decisions involving weighing up policy objectives are typically made by elected councillors or by a Minister. In contrast, decisions with objective decision criteria, even if they require a degree of judgement, may be most appropriately allocated to a public servant. Where technical or legal expertise is needed, and the decision maker is not an expert, it should be provided in the form of advice, and the appropriate institutional mechanisms should be provided to allow for this. (2013a, p. 35)

Taking into account these features, for most regulatory regimes in New Zealand the scales will be weighed towards more independence, although there will be a number of regimes where less independence is warranted. Given the preponderance of features supporting more independence, and the clarity with which the countervailing considerations can be established, there should be a presumption that regulatory regimes should be administered independently of political control. Independent regulation provides a credible long-term commitment to an impartial and stable regulatory environment. This outcome should not be lightly discounted.

**F5.1** Designers of regulatory regimes must carefully assess the arguments for and against regulator independence. Arguments for political control must be weighed against the benefits of providing a credible long-term commitment to an impartial and stable regulatory environment.

**F5.2** For most regulatory regimes, the arguments for providing more independent regulation will be stronger than the arguments for less independent regulation.

**Supporting effective regulatory practice**

Chapter 11 of this report discusses the factors that influence the behaviour of regulators and regulated parties and ultimately the effectiveness of regulation. Drawing on Baldwin and Black (2008), Chapter 11 emphasises the influence of the broader institutional setting the regulator operates within, in shaping the regulator’s actions and decisions. This broader setting comprises:

… the role of the political and legal infrastructure in which the regulator (state or non-state) is situated in shaping actions and decisions: the patterns of formal and informal control over the regulator, of veto points in decision making … (Baldwin and Black, 2008, p. 70)

Baldwin and Black (2008) argue that the institutional arrangements under which the regulator is established and operates has an important bearing on its practices.

Guerin (2003) identifies how political pressures can lead to the adoption of regulatory regimes or approaches that are poorly targeted at managing risks:

Both ministers and officials tend to be held more accountable for failing to regulate than for regulating at excessive cost, as the former is more transparent and can be held up as the reason for any negative outcomes in the activity to be regulated. Excessive regulation, however, is much harder to detect and the costs will be dispersed among those who are regulated, or those to whom the costs can be passed on.

…

Both ministers and officials face strong incentives to “get something done” and weak incentives to “do it well” or take a longer term perspective (eg, develop improved policy capabilities). The popularisation of concepts such as market failure encourage this approach, while the risk of government or regulatory failure is much harder to explain or is seen as an excuse for inaction. (p. 7)
There will always be uncertainty about risks. Regulators can and do make mistakes in assessing risks, with sometimes tragic results. Even so, Chapter 11 argues that, with appropriate institutional settings and by adopting effective regulatory strategies, expert regulators will be better at assessing risks and managing them than the media, politicians or the general public.

Institutional arrangements can support or undermine a regulator’s ability to deploy effective regulatory strategies. Misplaced public and political perceptions of risk, and the ability of the public and politicians to pressure regulators into adopting sub-optimal enforcement strategies, threaten a regulator’s effectiveness.

### How is regulator independence achieved?

Malyshev (2006) identifies the key mechanisms to protect independence. The four mechanisms are governance structure, transparency of procedures and guarantees for due process, the selection and nomination process, and the financing of the agency.

The OECD (2013a) emphasises that legal status is not a guarantee of actual independence, but that appropriate culture, leadership and relationships are essential components of independent regulatory behaviour. It says independence in decision making can be fostered by:

- operational clarity;
- clear articulation of decision-making powers in legislation;
- clarity about requirements to report to the minister;
- definition and clarity around ministers’ power of direction;
- an adequate resource base;
- staffing flexibility (to recruit and retain appropriate staff);
- transparent processes for appointing members of governing bodies and chief executives, and for terminating appointments;
- explicit provisions covering performance criteria and review; and
- limitation on the “post-separation activities” of governors.

VSSA (2009) provided a more concise list, saying that the major requirements for regulatory independence include:

- a statutory foundation for the independence;
- an adequate resource base;
- staffing flexibility;
- operational clarity;
- uncompromised enforcement decision making; and
- transparent methods and terms for appointing governors and senior managers.

Figure 5.4 illustrates the point implicit in the criteria offered by Malyshev, the OECD and VSSA: that independence is multi-faceted and covers significantly more than formal legal designation. A regulator can be independent according to one or more of these dimensions in Figure 5.4, but may have its independence constrained in other dimensions.
Submitters generally thought this framework was helpful in thinking about how New Zealand regulators are independent. The view of Minter Ellison Rudd Watts was typical: “It is not hard to think of examples under each head which would have a serious adverse impact on the ability to deliver a stable and coherent regulatory regime” (sub. 28, p. 24). However, the New Zealand Food and Grocery Council again cautioned against applying the framework too strictly noting: “It is about what works best for a sector rather than hard and fast rules or, in this case, frameworks” (sub. 35, p. 5).

Legal independence does not automatically lead to independence in practice. In particular, an agency’s reputation and capability will influence the degree of independence it is accorded in practice, regardless of legal designation. A regulator that is formally within ministerial control will, in practice, be able to act independently if it is held in high regard. A regulator that is formally independent but held in poor esteem by government or regulated firms will find their independence under threat, even with legal protection.

Institutional independence will be considered in section 5.2 alongside a discussion of the institutional forms that regulators can take. The other dimensions of independence are considered below.
“Regulation independence”

Chapter 2 of this report highlights a tendency for politicians to “set and forget” regulatory regimes, with the only opportunity for revision often occurring in the wake of high-profile regulatory failures (at which point reform may occur too hastily). One regulator told the Commission in an engagement meeting that they had a standing instruction not to bring legislative problems to their minister. Many submitters – particularly, but not exclusively, regulators – noted the desirability of being able to more easily update regulations than is common in many New Zealand regulatory regimes.

In the course of its engagement the Commission was told that one barrier to maintaining regulatory frameworks is the often inconsistent and inefficient allocation of material between primary legislation and the different types of secondary legislation (government regulations and deemed regulations, as outlined in Table 2.1).

For example, the FMA has many regulatory requirements determined through government regulations made by Governor-General in Council, while the Reserve Bank of New Zealand (RBNZ) is able to determine regulatory requirements of a similar significance administratively itself, without any approval from ministers or Cabinet:

- The FMA has powers to determine specific requirements for particular regulated entities, but the main requirements are set out in government regulations made by the Governor-General in Council on the recommendation of the Minister of Commerce. The main responsibility for advising on these regulations rests with the Ministry of Business, Innovation and Employment (MBIE), as the policy agency, rather than the FMA.

- In contrast, in the case of the RBNZ, most of the regulatory requirements imposed on affected entities are exercisable by the RBNZ via conditions of registration. Relatively few requirements on regulated entities supervised by the RBNZ are specified in regulations made by Executive Council. Examples are disclosure requirements for banks and prudential requirements for non-bank deposit takers. Unlike the FMA, where MBIE is the government agency with primary responsibility for advising the Minister of Commerce on regulations administered by the FMA, the RBNZ is the principal adviser to the Minister of Finance in respect of regulations it administers. (Indeed, as discussed in Chapter 4, the RBNZ is also the principal adviser to the Minister of Finance in respect of legislation administered by the RBNZ – which is very unusual in any OECD country.)

While there may be sound reasons in some cases for the variation in approach between regulatory regimes, in other cases there appears to be no obvious reason for the different allocation of powers and different levels of regulation independence between them.

As noted in Chapter 2, almost two-thirds of chief executives of regulatory agencies who participated in a Commission survey either strongly agreed or agreed with the proposition that agencies with regulatory functions “often have to work with legislation that is outdated or not fit-for-purpose” (Figure 2.1). This was also a strong message from the Commission’s engagement meetings and in submissions on the issues paper about the regulatory landscape. The case study of New Zealand’s regulatory regimes in transportation sectors is illustrative (Box 5.2).

Box 5.2  Case study: inflexible regulatory frameworks in the transportation sector

New Zealand transportation regimes are internationally credible and have achieved good safety outcomes. For example, road fatalities have dropped by 47% since 2000. Since the mid-1990s the rate of aviation accidents in the agriculture sector has halved, and aviation accidents in other commercial sectors has declined by almost 90%. The rate of maritime accidents and fatalities has remained relatively steady.

Even so, submissions by the Civil Aviation Authority (CAA), Maritime New Zealand, the Ministry of Transport and Aviation New Zealand all highlighted the prescriptive and inflexible nature of the legislative regimes regulating transportation, emphasising that the regimes were not able to
Regulators often have to work with legislative regimes that are outdated or not fit-for-purpose. For example, regulators in transport sectors have to oversee outdated rules due to an inflexible legislative framework.
The Ministry of Transport notes that a regulatory reform programme, including a project to improve the quality of rules in the transport sector, has been underway since 2010 (sub. 39). However, a review of the rules will not address the underlying causes of the outdated arrangements, and so it is likely that the rules will again in the future fail to provide for improved safety and efficiency measures as technology continues to advance.

The Ministry of Transport is also currently reviewing the Civil Aviation Act 1990 to assess how “fit-for-purpose” the regime is, and has commissioned research to identify where regulations, or their application, may be exacerbating market inefficiencies. The Commission supports this work.

R5.1 The Ministry of Transport should consider in its review of the Civil Aviation Act 1990 how the legislative regime can be flexible enough to take advantage of ongoing technological developments that could provide safety and efficiency gains. Subsequent reviews by the Ministry of Transport should consider how the other legislative regimes in transport can be made more flexible, taking into account the differences between the transport sectors.

Delegating authority to the Minister of Transport to make rules under the transportation sector regulatory regimes has been effective in allowing urgent rule changes to be made swiftly. However, to the extent that deemed regulations are in practice subject to Cabinet processes (Box 5.3), this offers few advantages compared to government regulations made by the Governor-General in Council.

Box 5.3 Cabinet Manual rules on items that should be considered by Cabinet

5.11 As a general rule, Ministers should put before their colleagues the sorts of issues on which they themselves would wish to be consulted. Ministers should keep their colleagues informed about matters of public interest, importance, or controversy. Where there is uncertainty about the level and type of consideration needed, Ministers should seek advice from the Prime Minister or the Secretary of the Cabinet. Similarly, departments should seek advice from the office of the portfolio Minister, or from the Cabinet Office.

5.12 The following matters must be submitted to Cabinet (through the appropriate committee):

   a. significant policy issues;
   b. controversial matters;
   c. proposals that affect the government’s financial position, or important financial commitments;
   d. proposals that affect New Zealand’s constitutional arrangements (see paragraph 5.72);
   e. matters concerning the machinery of government;
   f. discussion and public consultation documents (before release);
   g. reports of a substantive nature relating to government policy or government agencies;
   h. proposals involving new legislation or regulations (see Chapter 7 and the CabGuide);
   i. government responses to select committee recommendations and Law Commission reports (see paragraphs 7.108 - 7.111, and the CabGuide);
   j. matters concerning the portfolio interests of a number of Ministers (particularly where agreement cannot be reached);
   k. significant statutory decisions (see paragraphs 5.31 - 5.35);
   l. all but the most minor public appointments (see the CabGuide);
   m. international treaties and agreements (see paragraphs 5.73 - 5.74);
   n. any proposals to amend the provisions of the Cabinet Manual.

5.13 Matters that should not, as a general rule, be brought to Cabinet include:

   a. matters concerning the day-to-day management of a portfolio that have been
It appears that a conservative approach may be taken to bringing regulation-making decisions to Cabinet, compared to the requirements of the Cabinet Manual. On the other hand, there is a risk that regulation-making powers delegated to ministers might be exercised yet more cautiously where ministers are not able to formally seek the approval of colleagues to proposed changes.

**Operational independence**

Operational independence is the degree to which the regulator can flexibly undertake its powers and functions.

In the course of its engagement, the Commission’s attention was drawn to an example of where a regulator was unable to flexibly undertake its functions, not because of political interference, but because legislation is overly prescriptive about the exercise of those functions (Box 5.4).

**Box 5.4 Legislative requirements about how the Real Estate Agents Authority must manage public complaints**

The Real Estate Agents Act 2008 introduced government regulation of real estate agents following a loss of public confidence in the self-regulatory regime under the old Real Estate Agents Act 1976 and government dissatisfaction at the profession’s proposals to improve self-regulation.

In particular, the Associate Minister of Justice expressed concern at the unsatisfactory handling of complaints by the Real Estate Institute of New Zealand (REINZ), noting that in 2004 the REINZ received 132 complaints but none were referred to the Licensing Board, and in 2005 only seven of the 163 complaints it received were referred to the Board. Other concerns raised by the Minister included long delays in processing complaints, and allegations of poor quality investigations (Cosgrove, 2007).

As a result, the 2008 Act established very detailed and prescriptive requirements for the handling of complaints. Section 74 of the Act requires that every complaint be referred to a Complaints Assessment Committee (CAC), and sections 75-96 describe how the CAC will handle those complaints. Even if a real estate agent acknowledged the merit of a complaint and acceptable restitution was made, it appears that the legislation would still require the complaint to go through this process.

This is an understandable reaction to the deficiencies identified in the old regime. However, the requirement that every complaint be considered by CAC does not appear to be conducive to the swift resolution of complaints in a way that will best protect members of the public, and appears not to support the regulator achieving the desired outcomes of the regime in an effective and efficient way.

**Budgetary independence**

VSSA (2009) citing OECD (2003) says that funding mechanisms can have a significant impact on independence. Where a regulator is dependent on government funds, its independence can be compromised; where dependent on fees and levies, it can be susceptible to lobbying and capture.
The Council of Trade Unions said there was “an argument for longer term funding of regulators. It would give them greater independence, and allow them to take the longer term view that is frequently required” (sub. 25, p. 23).

Submitters did not identify significant concerns around the budgetary independence of New Zealand regulators. Chapter 13 discusses the funding of regulators more generally.

**Improving regulation and operational independence**

The problems of operational independence experienced by the Real Estate Agents Authority and the outdated legislative frameworks that other regulators grapple with due to their lack of regulation independence are both related to the drafting of legislation. A particular issue is the allocation of legislative material between primary legislation and the types of secondary legislation (government regulations made by Governor-General in Council or deemed regulations made by ministers or officials).

The Legislation Advisory Committee (LAC) guidelines (2012) provide useful advice on what material is suited to primary legislation or secondary legislation, including:

- significant policy matters;
- provisions that affect fundamental rights and freedoms;
- rights of appeal;
- provisions that vary the common law;
- the creation of offences and significant penalties;
- the imposition of taxes;
- the creation of new agencies or offices; and
- retrospective changes.

Despite these guidelines, it is clear from the submissions and the Commission’s research that the practice in allocating material between primary legislation and secondary legislation is inconsistent. Burrows (2011) provides two examples:

First, the Transport Rules (“the Rules”), which are of course delegated legislation, contain some of the most important legal rules in our community. We must abide by them every day. The rule that we must drive on the left hand side of the road is part of the Rules. However, the rule that I must tie a load on a trailer securely was enacted by Parliament in s 9 of the Land Transport Act 1998. I have no idea why. Then, in our corrections legislation, the rules about treatment of prisoners are oddly divided between Act and regulations. The rule confining the use of batons by prison wardens is in reg 123 [of] the Corrections Regulations 2005. Yet the rule that a prisoner’s bedding must be laundered regularly is in s 71 of the Corrections Act 2005. I cannot explain that distinction either. (pp. 67-68)

The Regulations Review Committee (RRC) “examines all regulations”, “may consider any matter relating to regulations and report on it to the House” and “investigates complaints about the operation of regulations, in accordance with Standing Order 316, and may report on the complaints to the House” [Standing Order 314]. It looks at all bills being considered by other select committees, and advises those select committees on whether the allocation of material between primary legislation, government regulations and deemed regulations is appropriate and consistent with LAC guidelines. Officials who provide support to the RRC told the Commission that such advice is rarely accepted. This is regrettable. Greater consistency in allocating legislative material between primary legislation and the types of secondary legislation would reduce complexity and promote the efficient and effective administration of legislative regimes. Stronger measures should be considered.
There is inconsistent allocation of legislative provisions between primary legislation and types of secondary legislation in regulatory regimes. There is evidence that existing mechanisms to promote greater consistency are ineffective.

The Minister for Regulatory Reform should coordinate a principle-based review of regulatory legislation to ensure greater consistency in allocation of legislation material between primary legislation and types of secondary legislation.

The Minister for Regulatory Reform should consider stronger mechanisms to ensure greater consistency in the allocating material between primary legislation and types of secondary legislation in government bills, either by elaborating departments’ Disclosure requirements for government legislation, empowering Parliamentary Counsel to provide stronger guidance, or some other mechanism.

The Commission was told by regulators who have worked in New Zealand and foreign jurisdictions that New Zealand uses regulations that can be amended by regulators themselves (deemed regulations) relatively infrequently. Although the Commission has not been able to gather comparative data to verify this claim, it does appear that Australia and the United Kingdom make significantly greater use of regulations that a regulator can set, but which a parliamentary committee can disallow. Gill (2011) notes that Cabinet government is stronger and more active in New Zealand than in Australia at the federal, state or territory level. It appears that where Parliament delegates legislative powers, it mainly creates government regulations made by Governor-General in Council. This requires ministerial leadership to steer changes to regulations through the Cabinet and Executive Council processes.

The six reasons traditionally cited to justify delegated legislation are:

- the pressure of parliamentary time
- the technicality of the subject matter
- any unforeseen contingencies that may arise during the introduction of large and complex schemes of reform
- the need for flexibility
- an opportunity for experiment
- emergency conditions requiring speedy or instant action. (Donoughmore Committee (UK) 1932 report on ministerial powers, quoted in Malone and Miller, 2012, p. 3)

The key countervailing consideration is one of democratic legitimacy. In 1929 Lord Hewart of Bury wrote that, in the UK, secondary legislation had become “a persistent and well-contrived system, intended to produce, and in practice producing, a despotic power which […] places government departments above the sovereignty of Parliament and beyond the jurisdiction of the courts” (Malone & Miller, 2012, p. 5).

One of the clearest examples of broad regulation-making power in New Zealand was the Economic Stabilisation Act 1948. Its purpose was “to promote the economic stability of New Zealand”, and section 11 allowed the Governor-General to make regulations “as appear to him to be necessary or expedient for the general purposes of this Act”. Through section 11 the Executive could, in the words of Sir Robert Muldoon, “do anything provided you can hang your hat on economic stabilisation” including implementing wage, price and rent freezes (Malone and Miller, 2012, p. 4).
Reports by the RRC have identified four principles that should be taken into account when delegating responsibility for making secondary legislation to ministers or officials (deemed regulations), and described the circumstances in which deemed regulations may be justified (Figure 5.5).

**Figure 5.5 Regulations Review Committee guidance on use of deemed regulations**

<table>
<thead>
<tr>
<th>Principles to consider in assessing the case for deemed regulations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The importance of the delegated power</strong></td>
</tr>
<tr>
<td>This requires an assessment of the effect of the delegated legislation on the rights and interests of individuals.</td>
</tr>
<tr>
<td><strong>The subject matter of the power</strong></td>
</tr>
<tr>
<td>Certain subject matter may be more amenable to delegation, including detailed, technical matters not subject to a criminal sanction.</td>
</tr>
<tr>
<td><strong>The application of the power</strong></td>
</tr>
<tr>
<td>Delegated legislation may be more appropriate if the powers will affect a narrowly defined or clearly identifiable group, rather than the public at large.</td>
</tr>
<tr>
<td><strong>The agency to whom the power is delegated</strong></td>
</tr>
<tr>
<td>Whether the delegation is to a Minister, an officer, or an agency, there must be appropriately qualified and competent personnel to draft the delegated legislation, and demonstration that an appropriate process was followed in doing so.</td>
</tr>
</tbody>
</table>

**Circumstances in which deemed regulations may be justified**

- the subject matter is not important enough to warrant consideration by Cabinet
- the subject matter may be highly technical, and thus best dealt with solely by an expert body
- the subject matter may be of interest only to a limited audience
- the subject matter may be the internal rules of an organisation that have minimal effect on members of the public
- the relevant legislation may wish to promote self-regulation in an industry
- there may be strong policy reasons for a particular institution to be able to control the content of rules without intervention by the Government
- the person or body empowered to make rules may have an independent statutory function and not be accountable to Cabinet (for example the Privacy Commissioner)
- it might be desirable in the interests of international uniformity to adopt verbatim rules formulated in another country
- the rules may be of an urgent or temporary character
- the changing nature of the subject matter may be such that a mechanism for rapid amendment and updating is required.

**Source:** Regulations Review Committee, 1999 & 2004.

Given the pressures on parliamentary and ministerial time, there appears to be significant scope for greater use of deemed regulations, subject to a number of controls. Examples include obliging the agency delegated the regulation-making power to consult on proposed changes, ensuring the regulations are gazetted, ensuring they are reviewed by the RRC, and ensuring that the RRC is adequately resourced to manage an increased workload. In its submission the CAA provided advice on this point:

Technical adjustment of rules would be useful – bearing in mind that Rules are essentially tertiary legislation [deemed regulations] and sound processes in which both Government and public can have confidence in are in place. There is also a need to ensure that Rule making processes are not captured (eg by the sector, or by technocrats or policymakers, etc), such that technical adjustments are appropriate, do not create unreasonable burdens, and maximise safety or other benefits. (sub. 6, p. 20)
As noted above, in practice regulators’ independence relies on them maintaining ministerial and public confidence in their capability and expertise. This will also be the case in delegating to them greater authority to make regulations. Regulators will need to understand and articulate the trade-offs between continuity and change in the rules, and benefits and costs to regulated parties and the wider public. Sound processes and consultation requirements can make sure these are taken into account.

There is scope for the greater use of delegating authority to make secondary legislation to regulators, subject to appropriate controls, to ensure regulation can keep pace with technological and other developments. Designers of regulatory regimes need to consider what regulation-making powers can be delegated to the regulator, particularly in areas subject to technological or other changes, in order to future-proof the regime.

The RRC reviews hundreds of draft regulations and numerous bills every year, and may draw the attention of the House to a regulation if it meets one of a number of specified grounds (Box 5.5).

Box 5.5  **Grounds on which the Regulations Review Committee can draw the House’s attention to a regulation**

The grounds are, that the regulation—

(a) is not in accordance with the general objects and intentions of the statute under which it is made:

(b) trespasses unduly on personal rights and liberties:

(c) appears to make some unusual or unexpected use of the powers conferred by the statute under which it is made:

(d) unduly makes the rights and liberties of persons dependent upon administrative decisions which are not subject to review on their merits by a judicial or other independent tribunal:

(e) excludes the jurisdiction of the courts without explicit authorisation in the enabling statute:

(f) contains matter more appropriate for parliamentary enactment:

(g) is retrospective where this is not expressly authorised by the empowering statute:

(h) was not made in compliance with particular notice and consultation procedures prescribed by statute:

(i) for any other reason concerning its form or purport, calls for elucidation.

Source: Standing Order 315.

Members of the RRC can recommend to the House that a regulation be disallowed (overturned) by moving a motion of disallowance. This takes effect after 21 working days, unless the notice of motion is withdrawn, Parliament is dissolved or the House disposes of the motion (for example, votes it down) (Legislation Act 2012, s.43). Alternatively, the House can disallow a regulation by passing a motion (Legislation Act 2012, s.42). To date, the disallowance procedure has only been used once successfully.¹⁹

The RRC works best when it has capable and experienced members and is able to operate in a non-partisan way. If the recommendations in this report are accepted, parliamentary oversight of regulations made by agencies will need to be stronger.

¹⁹ Certain provisions of the Road User Charges (Transitional Matters) Regulations 2012 were disallowed at the close of 27 February 2013, following a notice of motion given in the House by Charles Chauvel MP on 13 November 2012. Mr Chauvel was a member of the Regulations Review Committee at the time.
Chapter 13 of this report discusses the role of the RRC in reviewing fees and levies set by regulators.

Q5.1 How can the role of the Regulations Review Committee be strengthened, if regulators are delegated greater regulation-making powers?

Providing for political intervention

It is difficult to predict in what circumstances “flexibility is needed to take account of political imperatives” (Figure 5.3 above).

The duties of independent regulators and the interests of elected politicians will periodically diverge. It is undesirable for politicians to interfere in the decisions of independent regulators. Political intervention in independent regulators will undermine the authority of the regulator, encourage lobbying and special pleading, and contribute to an uncertain environment that deters foreign investment and harms businesses by increasing the cost of borrowing.

Independent regulators are never truly separate from the political process. They operate under the authority and according to laws which Parliament can change. All branches of government – Parliament, courts and other agencies in the Executive – monitor the activity of the regulator (see Chapter 14). Political intervention in regulatory decisions can be legitimate, and it can be exercised for good or ill.

Absolute constraints on ministers may not lead to a more stable regulatory environment. Ad hoc legislation to substantially reform or override regulatory regimes as a result of temporary political frustration is deleterious to a stable, predictable and effective regulatory environment that encourages investment. There is also a risk that without clarity about how to manage such political imperatives, a regulator will be subject to more informal and insidious political pressures.

Direct powers of intervention

For example, it has been argued that by providing clear ways for government to direct the RBNZ, the Bank’s independence is enhanced rather than undermined.

Notoriously, the Reserve Bank regime doesn’t stop a government changing the bank’s inflation target. But it can’t do so secretly, as happened when the government rather than the bank used to manipulate the country’s money supply. What the act ensures is not low inflation, but transparency. (Caygill, 2010, p. 54)

The Reserve Bank of New Zealand Act 1989 provides the Minister of Finance with considerable powers to direct the Governor of the RBNZ, including to:

- formulate and implement monetary policy for any economic objective, other than the standing objective to achieve price stability (s. 12)
- fix the prices at which the bank may engage in foreign exchange (s. 18)
- have regard for government policy objectives (s. 68B).

In each case the direction must be gazetted. Sections 12 and 18 require an Order in Council; section 68B requires the direction to be tabled in the House of Representatives.

The draft OECD guidance (2013a) on the governance of regulators suggests that where powers of ministerial direction are provided for, they should be constrained and exercised transparently. However, it also states that “in the case of economic regulators, legislation should not permit powers to direct by Ministers”.

Where such powers of intervention are transparently provided for, it can strengthen the hand of regulators to resist informal political pressure. It also means that where politicians do intervene, they can be properly judged by Parliament and the public and held to account.
The hurdles for such intervention should be high. For example, legislation should require ministers to do so in writing, with reasons, and table such documents in the House.

**Parliamentary override**

An alternative to providing ministerial powers of intervention is to rely on the supreme powers of Parliament to intervene, as in the case of the creation of Fonterra Co-operative Group.

By the mid-1990s there were only two major dairy cooperatives: New Zealand Dairy Group and Kiwi Cooperative Dairies. Both sold their milk through the government-appointed New Zealand Dairy Board. Proposals to merge the firms in 1999 were declined clearance by the Commerce Commission, which considered that the merger proposal had moderate to large detriments and small public benefits. The vast majority of the detriments were associated with the loss of productive and dynamic efficiency as a result of the loss of effective competition for the merged entity.

However, there was a bi-partisan political consensus that “trading in domestic competition for international clout through one massive exporter leader would be better for NZ Inc” (Malpass, 2014). Another merger proposal was announced in December 2000. The Dairy Industry Restructuring Bill was passed in September 2001, allowing this merger to avoid Commerce Commission scrutiny and deregulating the dairy industry while creating safeguards against abuse of Fonterra’s position.

Parliamentary override of regulatory decisions has the advantage of ensuring broad political support for the intervention, and allows for significant scrutiny as legislation progresses.

**Designers need a plan for dealing with political imperatives**

Designers of regulatory regimes need to consider how the political imperative to intervene in regulatory regimes will be managed. That may or may not require providing direct powers of intervention. Whatever avenue is provided for such political intervention, it should as far as possible occur in a way that maintains the regulator’s role and authority, and that does not encourage future interventions.

| F5.8 | Political pressures to intervene in the decisions of independent regulators are inevitable from time to time. Providing transparent mechanisms for political intervention in the decisions of independent regulators is preferable to wholesale regulatory reform designed to resolve political frustrations. It can also strengthen a regulator’s ability to withstand informal political pressure. |

| F5.9 | Designers need to plan for how to manage the political imperatives to intervene in regulatory decisions. Whether direct powers of intervention are provided or not, designers should seek to ensure: |
|      | • intervention is infrequent |
|      | • intervention does not set precedents for future intervention |
|      | • the regulator’s authority is not undermined |
|      | • intervention does not encourage regulated parties to work around the regulator |
|      | • there is transparency in the intervention. |

**Regulation of government activity**

In its issues paper, the Commission asked whether some aspects of regulatory independence are more or less important in regulating the exercise of state power or the regulation of government-provided or government-funded services.
The Council of Trade Unions considered that it was desirable for public service providers to influence their regulator, expressing the view that it would lead to higher quality standards (sub. 25).

A systematic review of the regulatory systems of six sectors in the United Kingdom found that regulation by quasi-autonomous agencies was suitable where the regulated organisations were private for-profit or not-for-profit entities. However, where the regulated sector was comprised of public services directly managed or influenced by government (such as schools or prisons) regulators seemed to have less independence from government, and there was some evidence of a conflict of interest between the government’s role as regulator and its role in service provision (Walshe & Boyd, 2007).

While there may be some merit in arguing for greater independence for regulators who also regulate the government (such as health and safety in employment law), it could be argued that increasingly the distinction between matters in which the government may have an interest (and therefore a possible conflict) or not is more and more difficult to make. The public sector reach has expanded so far into the private sector that it may not be helpful to attempt to identify regulatory aspects that are more suited to independence than others. (Maritime New Zealand, sub. 15, pp. 6-7)

Where publicly-funded services are being regulated, the government will have two levers to respond to problems – the regulatory system and the funding contract. In establishing a regulatory regime for public services, it is important to think through the relative roles of the funding and regulatory arrangements.

Funding arrangements may permit faster action. The Commission found in its case study of regulation of the aged care sector that the Ministry of Health was more likely to call on District Health Boards to trigger the Aged-Related Residential Care Services funding contract for enforcement, rather than use its own regulatory powers, in part because action through the contract required fewer legal processes and could therefore be taken more quickly.

Enforcement using the funding lever is also potentially more powerful, in that it can put the viability of a provider at risk. However, funding-based interventions tend to target individual providers and so may be less useful for raising performance across the whole system in the absence of substantial failures, or for revealing information to consumers about relative performance.

**5.2 Institutional form**

**Machinery of government in the New Zealand state sector**

The independence, accountability, efficiency and effectiveness with which regulatory functions are undertaken is strongly influenced by decisions around the institutional form in which to locate those functions. The trade-offs and tensions are neatly described by Schick (2002):

Every democratic government must both connect and separate its political and administrative organs. It must connect them so that managers and other service providers comply with the policies and rules laid down by political leaders. But it must also disconnect administrative matters from direct political involvement so that managers are free to act in a fair and efficient manner, without regard to political considerations. No democracy can abide governing arrangements which free managers to disregard the policies made by duly selected leaders, and no democracy can allow politicians to intrude in administrative matters without regard to the rights of interested parties. The first criterion justifies the placement of operating units within departments headed by ministers or by senior managers appointed by them; the second dictates the operational independence of administrative units. (pp. 10-11)
He argues that resolving those tensions is a delicate act, and one that is never settled for all time:

Striking the right balance between co-ordination and subordination on the one hand and independence and flexibility on the other requires that politicians and managers be both empowered and restrained. Each must have authority and resources to carry out basic responsibilities, and each must be deterred from acting in ways that encroach on the other’s domain. The result is an organisational map that is repeatedly restructured through legislation and practice to promote one or the other vision. (p. 11)

The SSC describes the structure and governance of state institutions as the “machinery of government”:

Machinery is an apt metaphor for the structures and systems of government. A machine is an instrument that exists in order to fulfil a purpose beyond itself. The parts in a machine move and change, and can be replaced or improved. (SSC, 2007, p. 3)

There is a complex range of institutional forms which a government regulator might take (Figure 5.6).

**Figure 5.6 Typology of institutional forms for a government regulator**

<table>
<thead>
<tr>
<th>State sector organisations</th>
<th>Organisations outside of the state sector</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Departmental</strong></td>
<td><strong>Crown entity</strong></td>
</tr>
<tr>
<td>Departments of State (eg, Ministry of Health or MBIE)</td>
<td>Independent Crown entities, where there is a high degree of independence from Ministerial influence (eg, Commerce Commission)</td>
</tr>
<tr>
<td>Departmental Agencies (none yet)</td>
<td>Autonomous Crown entities, which have an intermediate degree of Ministerial oversight and independence in decision-making (eg, New Zealand Teachers Council)</td>
</tr>
<tr>
<td></td>
<td>Crown agents, where there is a high degree of Ministerial oversight (eg, CAA)</td>
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<td></td>
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<td></td>
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</tbody>
</table>

Despite this diversity, in most cases designers of regulatory regimes will need to consider whether to establish the regulatory functions in a department or a Crown entity. If a Crown entity, they will need to decide what type of Crown entity is most appropriate.

**Departments**

Departments are listed on the first schedule of the State Sector Act 1988. They form the core of the State Sector, undertaking a wide range of functions. They are legally part of the Crown.

The SSC guidance on machinery of government notes:

There is a close and hierarchical relationship between Ministers and departments, with the governance arrangements centred on a direct Minister-chief executive relationship. Ministers have extensive powers to direct departments, as long as such directions are consistent with the law (e.g. there are relatively numerous statutory requirements for officials to act independently in some matters – which can be quite significant), (SSC, 2007, p. 13)

The guidance indicates that departments should be the default choice of organisational form for the following functions and powers:
• activities that are in some sense an inherent function of the State such as the conduct of foreign policy, and national defence;

• the exercise of significant coercive powers of the State such as policing, prisons, and tax collection;

• other special powers, such as the substantial powers of the Director-General of the Ministry for Primary Industries (MPI) under the Animal Products Act 1999;

• policy advice;

• the undertaking of multiple functions, particularly where those functions potentially conflict;

• activities that are so complex it is difficult to “contract” for their provision by a Crown entity, such as where the objectives/outputs are inherently difficult to specify, or may need to be changed frequently;

• activities where constitutional conventions indicate a need for close ministerial oversight or direct responsibility such as citizenship; or

• there is a ministerial desire to control the process and outcome of an activity, including frequently reviewing its objectives, as may be indicated by:
  - the significance and importance of the activity to the government;
  - the high public and political expectations associated with the activity, or
  - the nature of the risks posed to the Crown (for example, strategic or financial risks).

The chief executive of a department is employed by the State Services Commissioner for a fixed term.

A new piece of machinery – departmental agencies

The new Departmental Agency model in New Zealand aims to reduce fragmentation in the state sector by providing an organisational vehicle within a department for functions that might otherwise be carried out by Crown entities. Departmental agencies are legally part of, but operationally separate from, “host” departments, with their own chief executive appointed by the State Services Commissioner.

The Better Public Services Cabinet paper on departmental agencies indicates that they offer a potential means to:

• incorporate certain operational and/or regulatory functions presently delivered by separate Crown entities into the legal Crown;

• consolidate currently separate operational and policy departments into a single department, with departmental agencies; and

• deliver new operational and/or regulatory functions that may have otherwise led to the creation of a separate department or Crown entity.

The Cabinet paper on departmental agencies says that “departmental agencies are designed to have a strong service delivery focus and therefore operate with a high degree of autonomy (over day-to-day operations) from both the host department and Minister/s” (Office of the Deputy Prime Minister and Office of the Minister of State Services, 2012, p. 3). The close relationship between the host department and the departmental agency provides for improved efficiency through the sharing of back office or corporate functions.

However, this operational autonomy is not provided for in the amended State Sector Act 1988. The new section 27B reads:

(a) the functions, duties, and powers of a departmental agency may be determined by the appropriate Minister of the departmental agency in conjunction with the appropriate Minister of the host department; and
(b) the working arrangements between a departmental agency and its host department must be agreed by their respective chief executives and approved by their appropriate Ministers.

The departmental agency is legally part of the host department, still required to follow any lawful instruction of ministers, with the chief executive appointed and removed by the State Services Commissioner, and subject to the policy and funding framework of the host department.

In this sense they are similar to existing “branded business units” or semi-autonomous bodies. The key difference is that the chief executive is employed by the State Services Commissioner, and has a direct relationship with the responsible minister independently of the host department.

In considering possible institutional forms for a new workplace health and safety regulator, the regulatory impact statement canvasses a significant debate between departments on the desirable form of a new regulator, concluding:

The choice between a departmental agency and a Crown agent is not clear cut and turns on how the different objectives are weighted and views about what will occur in practice under each of the models. A departmental agency is likely to operate more efficiently as there will be less duplication of government activity. In this way, it better aligns with the government’s objective of better public services. However, while SSC and Treasury consider that a departmental agency provides sufficient independence, MBIE considers there is a risk that a departmental agency will not be seen as sufficiently independent or a significant enough change from the status quo to regain public confidence in New Zealand’s workplace health and safety regulatory system. There is a further risk that its credibility and focus could diminish over time as a result of changing departmental and government priorities. The departmental agency structure is new to New Zealand (while recognising that it is an evolution of existing structures), the legislation enabling it has yet to be enacted, and it is largely untested. MBIE does not share SSC’s and Treasury’s level of confidence that the outcomes under this structure are largely predictable and consider it is therefore difficult to assess the likelihood of these risks materialising. (MBIE, 2013, p. 20)

The Commission was told by SSC that the departmental agency model is based on executive agencies in the United Kingdom (Box 5.6).

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**Box 5.6  Executive agencies in the United Kingdom**

Like departmental agencies, executive agencies are legally part of their host department. The rise of executive agencies in the United Kingdom was accompanied by a drop in the number of executive non-departmental agencies -- the rough equivalent of Crown entities -- from 2,167 in 1979 to 760 in 2009. Despite being described as operating quasi-autonomously or at arm’s length from ministers, there are no particular protections for this autonomy. Former Second Permanent Secretary at the Office of the Minister for the Civil Service, Sir Peter Kemp, said this was by design:

>[Agencies] were left within government partly because it was recognised that there were or could be particular cases when ministers would want to get more involved – hence the word “normally” which qualifies the minister’s usual role of standing back. (Wall & West, p. 212)

Key to the success of departmental agencies in the United Kingdom is a civil service mandarin (known as Fraser figures) trusted by both the minister and chief executive, who liaises and coordinates between them and acts as the main source of advice on agency performance to each.

An evaluation of the executive agency model in 2002 concluded that it had been an overall success, and should continue, with agencies meeting or exceeding over 75% of their performance targets. Other evaluations found that most (but not all) executive agencies reduced their administrative costs. (Mosely et al., 2011)

However, Mosely et al. (2011) identify a number of concerns around the accountability and control of executive agencies in the United Kingdom:

- a lack of clarity around the degree of ministerial responsibility for the operational performance of
In recommending the creation of the departmental agency form, the Better Public Services Advisory Group “considered that a smaller number of Crown entities and separate departments would reduce costs and improve system coherence” (Office of the Deputy Prime Minister and Office of the Minister of State Services, 2012, p. 3). Moving functions from Crown entities to departments will require legislative change, and moving those functions from the host department to the departmental agency requires the agreement of responsible ministers.

Any autonomy a departmental agency is expected to have will be highly dependent on its culture; norms established and agreed between the chief executive of the departmental agency and host department, and between the chief executive of the departmental agency and the responsible minister; and, crucially, the statutory independence specifically associated with any powers which ministers delegate to it.

The expectation that departmental agencies will operate with a high degree of autonomy is dependent on agreements between ministers and between chief executives, rather than any legal protections associated with this institutional form.

As Parliament and government consider moving specific regulatory functions from Crown entities (which are operationally independent) to departmental agencies (which are not), it will need to carefully consider whether the individual functions and powers transferred have sufficient statutory independence associated with them, in an environment that is otherwise subject to high degrees of ministerial control.
Government has indicated a desire to relocate some regulatory functions from Crown entities to departmental agencies. By itself, this would serve to reduce the formal operational independence with which those functions are undertaken. As a result, government will need to review any functions that are transferred to consider whether they should be undertaken in a statutorily independent way.

The OECD (2013a) notes potential risks still exist where statutorily independent decision makers are supported by departmental staff, including:

- risks to perceived and actual independence;
- risks to quality arising from lack of control of the quality and quantity of support services or other resources; and
- risks of inappropriate information exchange between regulatory staff and other staff in the host department.

The Victorian Government (2010) also considers these arrangements to involve a risk that staff will be conflicted between the different interests of the regulator and the Secretary or host department. These risks may be particularly acute in an environment where public servants view ministers as a client to be pleased, rather than served.

In the Commission’s view, the departmental agency form is not fundamentally new to the New Zealand state sector, apart from the innovation that the State Services Commissioner will employ the chief executive. While semi-autonomous bodies have worked well in some cases, there are also recent examples where re-integration has been considered necessary to improve performance:

- the Government’s decision to merge NZ Aid into the Ministry of Foreign Affairs and Trade in 2009;
- the Secretary for the Treasury’s decision to merge the Crown Company Monitoring Authority Unit into Treasury in 2009 as the Crown Ownership Monitoring Unit;
- the New Zealand Food Safety Authority, which was:
  - formed as a semi-autonomous body attached to Ministry of Agriculture and Fisheries (MAF) in 2002 by consolidating food safety functions undertaken by MAF and the Ministry of Health;
  - separated from MAF to become a public service department in 2007;
  - re-integrated back into MAF in 2010.

In its 2012 inquiry into housing affordability the Commission found that the structure of the Social Housing Unit as a semi-autonomous body within the Department of Building and Housing left room for unclear priorities, mixed purposes and misaligned accountabilities, despite clarity about its formal objectives (NZPC, 2012a).

Where these arrangements have succeeded in the New Zealand public sector, they have done so in large part because of effective relationships between the head of the agency and the chief executive of the host department. It is possible that the changed employment relationships of the head of the agency may undermine, rather than support, the effective operation of such agencies. The working arrangements agreement between chief executives of departmental agencies and host departments will therefore be particularly important.

The revised State Sector Act 1988, which provides for the departmental agency model, says at s. 32(2):
the chief executive of a department is not responsible for the performance of functions or duties or the exercise of powers by that part of the department that comprises any departmental agency hosted by the department;

the chief executive of a departmental agency is responsible only for the performance of functions or duties or the exercise of powers by that part of the department that comprises the departmental agency.

The Commission is concerned that this division of responsibilities may be hard to sustain, and that there is potential for confusion and conflict around the respective roles and accountability of ministers (of the host department and departmental agency) and chief executives (of the host department and departmental agency). Clarity around roles, responsibilities and mandate is a necessary precondition for effective regulators (see Chapter 4). Some external review of the agreements between ministers that divide functions between host departments and departmental agencies, and the agreements between chief executives on working arrangements, may reduce the potential for confusion and conflict.

There is the potential for confusion about the accountability arrangements of departmental agencies, and the respective roles and responsibilities of:

- the minister responsible for the departmental agency;
- the minister responsible for the host department;
- the chief executive of the departmental agency; and
- the chief executive of the host department.

The Minister of State Services should review agreements between ministers to establish and allocate functions to departmental agencies to ensure that respective roles, responsibilities and accountabilities are clear.

The State Services Commissioner should approve agreements between the chief executives of host departments and departmental agencies to ensure that respective roles, responsibilities and accountabilities are clear, and that there are appropriate formalities in place to preserve the independent exercise of statutorily independent powers.

Crown entities

Crown entities are stand-alone agencies, governed by a board. They are not legally part of the Crown (see discussion in Chapter 9). The SSC guidance on machinery of government notes:

The legal separation from the Crown establishes an ‘arm’s length’ distance between the Minister and the entity. The channels of Ministerial direction or instruction are considerably more formalised than the interactions between Minister and department. The governance arrangements are centred on the Minister-board relationship. (2007, p. 14)

“Arm’s length” means an organisation is “not subject to the direction on individual regulatory decisions by executive government” (OECD, 2013a). However, there are different degrees of distance from ministers within the three main types of Crown entity that might undertake regulatory functions: Crown agents, autonomous Crown entities and independent Crown entities. They differ in terms of the degree to which they are subject to ministerial direction, and the mechanisms by which their boards are appointed and removed (see Table 5.1 below).
However, these differences are important as ultimate safeguards against abuse by ministers, and because of the signals they send, rather than because of their practical value. In fact there have been only two ministerial directions pursuant to the Crown Entities Act, neither of which relate to a regulatory regime, and only two ministerial directives pursuant to other Acts that clearly relate to regulatory regimes. The Cabinet Manual notes that “these powers of direction are likely to be used infrequently because other tools such as letters of expectation work well to convey Ministers’ expectations”. There has only been one instance in which board members of a regulatory Crown entity have been removed from office before the end of their term.

This is consistent with evidence from Europe which finds politicians generally do not use the formal controls over independent regulatory agencies that are available to them. Thatcher (2005) using a principal-agent framework proposes two possible explanations:

- The first is that “independent” regulators have structured incentives to act in accordance with politician’s preferences, meaning there are no agency losses and no need for sanctions. These incentives may include increased powers and budgets, renomination, or they may result from informal relationships.

- The second is that, although there are agency losses, politicians choose to accept these because they are outweighed by the benefits of independent regulators and the costs of applying the sanctions. Those costs may be political or damage done to the regulatory framework’s credibility.

The experience of Roy Hemmingway, former Chair of the Electricity Commission is illustrative (Box 5.7).

Box 5.7 Electricity Commission and regulatory independence

Roy Hemmingway became inaugural Chair of the Electricity Commission (a Crown agent, predecessor to the Electricity Authority) in 2003. He claims he was promised the Electricity Commission would be independent. However, tensions arose after the Electricity Commission decided not to approve Transpower’s application to upgrade the transmission network between Waikato and Auckland. Hemmingway claims he was under pressure from ministers to negotiate an approval of the upgrade application.

Former Minister of Finance Michael Cullen was reported as saying that the Electricity Commission’s decisions raised concerns about New Zealand and Auckland’s future economic welfare that ministers had a legitimate interest in: “In that situation we reserve a perfect right to say to people that we expect you to come to a sensible conclusion here and encourage them rather strongly to do so”.

In 2006 Ministers declined to reappoint Hemmingway to the Electricity Commission. Minister of Energy David Parker was reported as saying “I make no apology for the fact that when security of supply gets ropy there is political accountability in New Zealand and politicians step in. And I did”. Another former Minister of Finance, David Caygill, was appointed as the new chair. Transpower’s proposed upgrade was approved by the Electricity Commission in July 2007.

In a presentation to the Harvard Electricity Policy Group soon after leaving office, Hemmingway argued that many design features of the Electricity Commission contributed to a lack of independence, and claimed that regulated firms had heavily lobbied politicians, who in turn put pressure on him.

It is clear that despite ministers’ frustration with the Electricity Commission’s decisions, they did not
feel the need to resort to formal mechanisms of control over this Crown agent. When informal pressure was unsuccessful, Hemmingway was simply not reappointed. Clearly ministers and Hemmingway did not have a shared understanding of the respective roles of ministers and the Electricity Commission, or of the degree of independence that was signalled by the Electricity Commission’s form as a Crown agent.


The legal differences between the types of Crown entities – the appointment and removal of board members, and ministerial powers of direction – do not in practice differentiate them, because the removal of board members and the issuing of formal ministerial directions to boards has almost never occurred.

### Independence and agency type

Applying the Commission’s framework for regulatory independence (as outlined in Figure 5.4 above) to the major types of institutional form reveals that these forms are not strongly differentiated (Table 5.1).

#### Table 5.1 Institutional forms and dimensions of independence

<table>
<thead>
<tr>
<th>Dimension of independence</th>
<th>Departmental agency</th>
<th>Crown agent</th>
<th>Autonomous Crown entity</th>
<th>Independent Crown entity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulators(^{23})</td>
<td>None yet</td>
<td>Civil Aviation Authority</td>
<td>Commission for Financial Literacy and Retirement Income</td>
<td>BSA</td>
</tr>
<tr>
<td></td>
<td></td>
<td>EEA</td>
<td>Historic Places Trust</td>
<td>Commerce Commission</td>
</tr>
<tr>
<td></td>
<td></td>
<td>EPA</td>
<td>Lotteries Commission</td>
<td>Drug Free Sport New Zealand</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Fire Service Commission</td>
<td>Electricity Authority</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Maritime New Zealand</td>
<td>Financial Markets Authority</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>NZQA</td>
<td>HDC</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>NZTA</td>
<td>Office of Film and Literature Classification</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Walking Access Commission</td>
<td>Privacy Commissioner</td>
<td></td>
</tr>
</tbody>
</table>
|                           |                     |             | Takeovers Panel         |\(^{23}\) According to the Commission’s criteria for inclusion in its mapping exercise (see Chapter 1 for criteria for inclusion).
Dimension of independence | Departmental agency | Crown agent | Autonomous Crown entity | Independent Crown entity
---|---|---|---|---
Operational independence | Required to follow any lawful ministerial direction | Operationally independent; must give effect to government policy | Operationally independent; must have regard to government policy | No ministerial powers of direction
Regulation independence | Each organisation has whatever powers are provided for by Parliament | | | |
Budgetary independence | Usually parliamentary appropriation, except where Parliament provides otherwise, such as the power to issue levies and charges. | | | |

Notes:
1. Excludes the RBNZ and Gas Industry Company, which have unique institutional forms among regulators.

Coupled with the Commission’s earlier finding that the differences in institutional and operational independence do not (in the way that they are actually used) distinguish between organisational forms, this leads to a number of preliminary conclusions:

- the choice of institutional form is important because of what it signals about the expected independence of the regulator, rather than the legal differences between them;
- the culture that is established within the regulator, and the norms established between the agency and the responsible minister, will in practice be strong influences on the agency’s independence;
- the legislation establishing a regulatory regime is particularly important in establishing its independence, because this establishes whether:
  - the regulator has powers that need to be operated independently;
  - the regulator has the ability to set and adjust rules and regulations to effectively achieve the objectives of the regime;
  - the regulator will have independent sources of revenue.

Such a culture is important in terms of establishing how the regulator thinks about what its task is (to please a minister?; to please regulated firms?) rather than as a protection against active threats to the regulator’s independence. An in-depth discussion on the importance of culture, particularly in new organisations, is in Chapter 7.

F5.15 The choice of institutional form will be important as much in terms of what it signals around expected levels of agency independence, as for the legal protections associated with particular agency forms.

F5.16 Ministers and the founding governors and leaders of new agencies need to pay particular attention to the norms and cultures established around independence, in terms of the relationships between them, and the agency’s operations.

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24 Except for “whole-of-government” directions.
The trend towards agency consolidation

The views of the Better Public Services Advisory Group, and the emergence of the new departmental agency form, continue a trend over the past decade towards greater amalgamation of public service entities in New Zealand, leading to policy and regulatory functions being placed within one agency and the merger of regulators in related industries. New Zealand’s public management approach has shifted from one “which advocated that organisations should have ‘simple and clear purposes’, particularly the separation of policy, delivery and regulation in order to align incentives for officials and reduce ‘opportunistic’ behaviour” to one where “the structural focus is to ‘shift the burden of proof towards amalgamation’” (Norman and Gill, 2011).

The establishment of WorkSafe New Zealand as a Crown agent, discussed above, is a notable exception to the trend.

A similar shift can be seen in how regulator design has been considered overseas. The United Kingdom Hampton Review (2005) and the VSSA’s review of regulatory governance (2009) both recommended the gradual consolidation of existing agencies to improve efficiency and effectiveness. Hampton went further and proposed that:

- “no new regulator should be created where an existing one can do the work”;
- “new tasks should be given to existing regulators unless there is a compelling reason to create a new body”.

Jordana and Levi-Faur (2010) have detected an international “trend towards the creation of multi-sector regulatory agencies”. The Blair Labour government in Britain consolidated a number of its economic regulators, creating the Office of Gas and Electricity Markets (Ofgem) out of its gas supply and electricity agencies in 2000 and the Office of Communications (Ofcom) out of five different regulators covering media and communications sectors in 2003. Ofcom’s scope was expanded in 2011 to also cover postal regulation. The scope of Germany’s network regulator has been progressively expanded from telecommunications to include utilities and infrastructure. The Netherlands has recently merged its consumer, competition and telecommunications regulators to form an Authority for Consumers and Markets (OECD, 2013a).

Box 5.8 Submitters’ views on agency consolidation

A number of submitters argued that New Zealand’s regulatory landscape was too cluttered and that a reduction in the number of agencies and regimes could improve the efficiency and effectiveness of regulatory enforcement:

The size of NZ’s population, the similarity of many regulated activities (e.g. building, farming, roading, etc) and the limited availability of specialist expertise justify greater aggregation of regulatory powers, particularly where regulation involves a greater degree of discretion and expert judgement. (Carter Holt Harvey, sub. 8, p. 11)

…we think the amalgamation of agencies operating in the same part of the market with similar or overlapping responsibilities, is not only more economically efficient but also more likely to generate consistent regulatory outcomes. (FMA, sub. 53, p. 2)

There should be more consideration given to the need for a single market conduct regulator … There would be clear benefit in amalgamating knowledge within one market conduct regulatory body, as in Australia, so that insurance conduct matters could be dealt with consistently and effectively. Having a single market conduct regulator also encourages a better working relationship between government and stakeholders, as market participants are not required to

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25 For example, the merger of the Charities Commission with the Department of Internal Affairs, and the merger of the New Zealand Food Safety Authority into the Ministry for Primary Industries.
26 For example, the creation of the Ministry for Primary Industries out of the Ministry of Agriculture and Forestry, Ministry of Fisheries and New Zealand Food Safety Authority.
27 Ofcom’s scope was expanded in 2011 to also cover postal regulation.
28 The Bundesnetzagentur (Federal Network Agency).
commit resources across a number of different bodies. It would also reduce the risk of inconsistent policy and regulatory practice between the agencies, which is a risk under the current framework. (Insurance Council of New Zealand, sub. 5, p. 4)

Mighty River Power considers there could be merit in the Productivity Commission considering whether there could be efficiencies in concentrating industry specific regulator functions in an umbrella regulator like the Commerce Commission … An alternative approach would be to consider concentrating regulatory functions in the Commerce Commission as an umbrella regulator but with some industry specific technical expertise … The benefits of this approach would be to provide sector specific rule-makers with more resource to focus on industry development rather than regulation, compliance and enforcement. (sub. 30, pp. 5, 11)

…we would recommend that a principle of regulatory design be that a single industry should have a single regulator unless a cost-benefit analysis is able to identify clearly why this should not be the case. (Powerco, sub. 14, p. 5)

Others argued that some regulatory functions should be disaggregated.

- Vector said that some forms of regulation, especially economic regulation of infrastructure, require “a greater level of constructive engagement” to work and so should be managed separately from the more adversarial types of regulation, such as consumer protection or competition policy (sub. 29, pp. 15-17, 21, 28-32).

- The New Zealand Food and Grocery Council argued that combining regulators is not necessarily the best way to improve capabilities. Approaches such as bilateral agency communication and cooperation may be more effective (sub. 35, p. 8).

- The Electricity Authority was concerned that combining regulators to improve capability could compromise an agency’s focus on their statutory objective. Establishing links with other regulators may be a better approach (sub. 50, p. 6).

- The FMA also noted that

  fast and responsive is not necessarily correlated with big, and it is the former that is important in the twenty first century. While there have been opportunities explored by FMA in the past 2-3 years to combine regulatory activities across agencies under one umbrella, none of these have been implemented either due to an absence of provable material economic benefit or diffuse levels of political support. ( sub. 53, p. 7)

A number of submitters argued that rule making and rule-enforcement functions should be allocated to separate regulatory organisations, to provide greater checks and external scrutiny over the development of new rules. This issue is discussed in Chapter 4.

In its report on the rationalisation and governance of state regulators, the VSSA identified the following criteria for when regulatory functions should be consolidated in, or separated from, a department (Table 5.2).

**Table 5.2 VSSA framework for location of regulatory functions**

<table>
<thead>
<tr>
<th>Regulators might be better located within a department where…</th>
<th>Regulators might be better located outside a department where…</th>
</tr>
</thead>
<tbody>
<tr>
<td>the environment being regulated is subject to rapid change and there is a need for the regulator to access technical knowledge of the department</td>
<td>functions are easily described and measured</td>
</tr>
<tr>
<td>political/strategic importance requires ministerial oversight</td>
<td>perception of political independence is necessary</td>
</tr>
<tr>
<td>minor or incidental functions not justifying a stand-alone body</td>
<td></td>
</tr>
</tbody>
</table>

*Source: VSSA, 2009.*
Benefits of consolidation

Consolidating regulatory agencies may offer the following benefits:

- **Greater efficiency, arising from economies of scale and scope:** Larger and broader-based agencies are likely to be most efficient to run. A survey of British regulators as part of the Hampton Review found that smaller agencies were more expensive to run, with higher average per-staff and per-inspection costs (Hampton, 2005). Larger organisations may also be better placed to attract, retain and develop capability, apply more sophisticated risk assessment and compliance approaches, and allocate scarce professional resources more effectively (VSSA, 2009; Jordana & Levi-Faur, 2010). Assertions that larger regulators are more efficient are not universally accepted. A 2007 survey of British regulatory regimes concluded that:

  there is no evidence necessarily that the much larger regulators … are either more efficient or effective, certainly beyond a certain scale. Indeed, it could be argued that the larger regulatory agencies, like OFSTED, often resort to subdividing their activities into separate regulatory divisions dealing with different sectors or activities to deal with the complexity that comes with size. (Walshe & Boyd, 2007, p. 119)

- **Reduced administrative burdens, inconsistency or complexity for regulated entities:** A reduction in the number of regulatory agencies may create opportunities to streamline audit processes and reduce other duplicated processes, so that firms face fewer inspections and forms (Hampton, 2005). Bringing multiple regimes and sectors under one agency also enables sharing of practice across similar regulatory issues and sharing of risk information across regimes. Applying common principles or approaches across similar issues may improve regulatory predictability (Jordana & Levi-Faur, 2010).

- **Independence:** Larger agencies that cover a range of sectors may be less prone to capture by regulated industries (VSSA, 2009; Jordana & Levi-Faur, 2010; OECD, 1999).

- **Greater policy focus and connection with operations:** Maritime New Zealand submitted that where regulatory functions are established in a Crown entity, there can be weak incentives for the policy departments to review and maintain the regulatory regime or even maintain specialist capability in the area of regulation.

Disadvantages of consolidation

- **Loss of focus:** multi-sector or multi-regime agencies may focus less on some industries or regimes than single-sector regulators, and so be less effective. The Electricity Authority made this point in its submission:

  [C]ombining regulators to improve capability risks compromising the focus that regulatory agencies have on their statutory objective. In the Authority’s case … this focus is extremely sharp and is key to the successful performance of its functions and its overall effectiveness. (sub. 50, p. 6)

- **Loss of perspective:** The regulation of certain types of rare but catastrophic risks can be at particular risk of loss of focus within a consolidated agency. The Royal Commission into the Pike River Coal Mine Tragedy (2012) noted that:

  History demonstrates that lessons learnt from past tragedies do not automatically translate into better health and safety practice for the future. Institutional memory dims over time. (p. 264) …

  Health and safety in New Zealand was not led by a body for which improving health and safety was its sole, or even major, objective. Health and safety was just one of the responsibilities of a department with many responsibilities. This diluted the attention paid to health and safety and contributed to an unwieldy structure in which senior officers had limited opportunities to develop health and safety expertise. (p. 291) …

  Interestingly, the highest risk sectors were identified primarily according to personal injury data – the consequences of individual accidents – but high-hazard industries are at risk of catastrophic process safety accidents, which are, by their nature, low frequency high consequence events. As the Pike River mine tragedy demonstrates, a focus on personal injury rates alone is not adequate to identify the ultimate workplace hazards. Until recently, there was no sign that catastrophic risk featured in the department’s strategic thinking. (p. 295)
• **Loss of institutional support**: The Compliance Common Capability Programme (CCCP) submitted that in organisations where regulation is only one of many areas of activity, such as MBIE or DIA, “the regulatory compliance business can sometimes fail to get leadership attention amidst a range of competing priorities” (sub. 12, p. 3).

• **Less accountability**: the narrower an organisation’s set of responsibilities, the less likely it is to get diverted or conflicted, and the easier it will be to hold it to account for its performance. This was one of the rationales underpinning New Zealand’s state sector reforms in the 1980s (Ayto, 2001). Agencies managing multiple regimes may be more prone to conflicting objectives, and have to make trade-offs between which regime(s) they commit resources to. These trade-offs may not be made in a transparent or consistent manner. This may make it difficult to hold the agency to account. Greater discussion on role clarity can be found in Chapter 4.

• **Loss of capability**: contrary to the view that larger agencies are better-placed to attract and retain talent, some have argued that multi-sector organisations are prone to lose sector-specific expertise that is necessary for effective regulation (Jordana & Levi-Faur, 2010).

• **Cost and disruption**: Merging existing agencies can be costly, as Environment Canterbury commented:

> Our experience leads us to the view that amalgamation or mergers involve their own costs and unintended consequences. Collaboration, transfer of functions and delegation of responsibilities will often be preferable. (sub. 4)

These risks are neatly summarised by Julia Black (2012):

> If regulatory functions are simply swallowed up into large departmental behemoths, there is no clear organisational structure for their performance; tasks are fungible, as are the departmental units performing them; opportunities for meaningful stakeholder participation are limited in the absence of dedicated advisory committees; and the scale of Departments combined with the weaknesses of Ministerial responsibility is such that accountability is lessened, not enhanced. For example, in commenting on the coalition government’s Public Bodies Bill, the PAC [Parliamentary Public Administration Committee] argued that ‘bringing functions back into sponsor departments is likely to undermine other channels of accountability, particularly with relevant stakeholder groups, and risk leaving policies fighting numerous other priorities for ministerial attention. This will mean less effective accountability and challenge on a day-to-day basis’. (p. 14)

Existing SSC guidance on machinery of government decisions properly focuses on the formal and legal accountability arrangements that are appropriate for certain types of functions, and the degree of ministerial oversight that is appropriate. However, the guidance could usefully be enhanced by discussing some of the practical benefits and risks of consolidation, such as those outlined above.

<table>
<thead>
<tr>
<th>F5.17</th>
<th>Regulation designed to prevent low-frequency, high-consequence (catastrophic) events is less likely to suffer from loss of focus or institutional support over time if located in stand-alone agencies.</th>
</tr>
</thead>
<tbody>
<tr>
<td>R5.6</td>
<td>Updated State Services Commission guidance on machinery of government choices should discuss the practical benefits, costs and risks associated with allocating functions to a department or stand-alone agency, as well as the accountability and governance considerations.</td>
</tr>
</tbody>
</table>

There is no optimal allocation of functions between organisations, and in some cases organisational structure continues to change over time as priorities and fashions change (see, for example, Table 5.3).
<table>
<thead>
<tr>
<th>Date</th>
<th>Change</th>
<th>Reasons for change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1972</td>
<td>The Fisheries Management and Fisheries Research Divisions of the Marine Department are combined with the Department of Agriculture to form the MAF.</td>
<td></td>
</tr>
<tr>
<td>1987</td>
<td>Amalgamation of 10 functional Divisions of MAF into 4 Business Groups (MAF Technology, MAF Quality Management, MAF Fisheries and MAF Corporate Services).</td>
<td>In response to requirements from Government to become more business-like and generate third party revenue.</td>
</tr>
<tr>
<td>1990</td>
<td>Separation of MAF Policy (Agriculture and Fisheries) from service delivery functions in the other Business Groups.</td>
<td></td>
</tr>
<tr>
<td>1992</td>
<td>Science restructuring - MAF Tech is split among Crown Research Institutes (CRIs). Agriculture New Zealand (farm consultants) is kept, but moved over time to full cost recovery.</td>
<td>Reform of the science system and creation of CRIs.</td>
</tr>
<tr>
<td>1994</td>
<td>Policy restructuring - separation of agricultural and fisheries policy.</td>
<td></td>
</tr>
<tr>
<td>1995</td>
<td>Sale of Agriculture New Zealand to Wrightsons.</td>
<td></td>
</tr>
<tr>
<td>1995</td>
<td>Ministry of Agriculture and Fisheries is split into Ministry of Fisheries and Ministry of Agriculture (the MAF brand is retained, although the F doesn’t stand for anything).</td>
<td>Split is considered necessary to provide focus in overseeing a new fisheries management regime.</td>
</tr>
<tr>
<td>1998</td>
<td>Ministry of Agriculture and the Ministry of Forestry merge to become the Ministry of Agriculture and Forestry.</td>
<td>To create efficiency gains, and allow the tighter coordination of government services to the agriculture, forestry and horticulture sectors, including a more integrated policy and service delivery approach to these sectors.</td>
</tr>
<tr>
<td>1998</td>
<td>Forestry Export Certification is transferred to AgriQuality.</td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>MAF Quality Management is replaced by two state-owned enterprises: Asure New Zealand Ltd and AgriQuality New Zealand. Verification Agency and Quarantine Service stay within MAF. The Animals and Plants Laboratories stay as part of core MAF.</td>
<td>To separate the service delivery arm from the core government tasks of policy advice and regulatory standards, and to improve the efficiency and performance of both businesses to ensure their viability.</td>
</tr>
<tr>
<td>1999</td>
<td>Sale of Forest Health to Forest Research.</td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>Separation of Regulatory Authority into Biosecurity Authority and Food Assurance Authority.</td>
<td>To provide greater focus and coordination of biosecurity risks.</td>
</tr>
<tr>
<td>2002</td>
<td>New Zealand Food Safety Authority (NZFSA) becomes a semi-autonomous body attached to MAF, merging MAF Food Assurance Authority and some parts of the Ministry of Health.</td>
<td>Considered necessary to separate food safety functions from the department’s export promotion role.</td>
</tr>
<tr>
<td>2004</td>
<td>MAF Biosecurity Authority becomes Biosecurity New Zealand, incorporating some functions from Department of Conservation and Ministry of Health.</td>
<td>The agency reflects MAF’s expanded mandate and responsibilities in the biosecurity area. It aims to provide a fresh start to biosecurity in New Zealand, as envisaged by the Biosecurity Strategy.</td>
</tr>
<tr>
<td>2007</td>
<td>NZFSA separates from MAF to become a public</td>
<td>It was considered that the focus of NZFSA on public safety did not sit comfortably with MAF’s focus on</td>
</tr>
</tbody>
</table>
Over the history of MAF/MPI a number of functions have been transferred to separate semi-autonomous bodies or departments, and then transferred back. However, the key relationships required to effectively lead and regulate the primary industry sectors remain of critical importance regardless of where they are located. For example, the agriculture department chief executive and the head of the food safety agency or biosecurity agency need to work together closely, whether those functions are located in the department, attached to it, or outside the department. Similarly, biosecurity and food safety functions operate within a common international WTO framework, and the relationship between the heads of those agencies is important.

Coherence problems between executive functions cannot be resolved by co-locating those functions alone. Designers of regulatory regimes need to identify what personal and professional relationships are key to the effective operation of a regulatory regime, and assess which of those relationships are best managed within an organisation and which are amenable to management between organisations. This should inform decisions around the location of regulatory functions.

Structural change

Structural change within government departments has been described by Norman and Gill (2011) as “an addiction”. They report that internal restructurings are seen by chief executives as a way to:

- improve the mix of capabilities within a department and shore up capability gaps;
- “reboot” an organisation from a non-performing past;
- clarify performance expectations within the department;
- change the shared values and organisational culture;
- get different people onto a management team.

However, Norman and Gill find the costs of restructuring to be significant and there are immediate productivity dips. The limited evidence on effectiveness suggested that the benefits of restructuring take at least two years to emerge. The authors conclude that restructuring is used to create a perception of being decisive and in charge, and to avoid formal processes of performance management which may be more subject to legal challenge. They recommend that restructuring “should be subject to the same scrutiny as major investment decisions such as roads, information technology systems and buildings” and that
Departmental chief executives need to act “more like stewards of their organisations and less like owners” (pp. 15-16).

Mergers can lead to a loss of focus on core accountabilities during the transition process, particularly as experienced staff leave and new staff arrive. This can cause gaps in service delivery or inadequate risk management. It can also cause projects underway to lose momentum. Where management layers are restructured, staff are continuing their usual functions without the usual oversight and risk management.

The merger of NZFSA, MAF and the Ministry of Fisheries in 2010-11 disrupted the smooth operation of some regulatory regimes. The Meat Industry Association (MIA) attributed problems with export certification to capacity issues.

Nevertheless, this year has seen issues emerge which have left the Ministry (and their Minister) embarrassed by failings within MPI, most notably over exporter access to China. Essentially, the creation of MPI, with its new name, entailed changing official export certificates. This task was undertaken on top of the existing work within MPI. In this case, staff were focussed on their very busy market access tasks, and the additional job of getting new export certificates approved by the Chinese authorities was overlooked. The MIA had been warning for some time over how the very capable staff in the MPI market access team were having to deal with an enormous array of market access issues beyond their capability to meet. Because the absence of capability, what was a simple bureaucratic mistake relating to changed documentation turned into a significant block on New Zealand meat exports.

... [As the MPI Review makes clear, there was an organisational culture and a lack of resources that allowed a simple mistake to occur and prevented rapid escalation of the issue to senior management and the Minister. (sub. 40, p. 12)]

The Public Service Association considered that “structural changes, including mergers of agencies, frequently lead to loss of capability rather than its improvement” (sub. 26, p. 2). MAF noted this in the course of its 1998 Financial Review:

... the extent and duration of the capability loss is extended if restructurings follow one on the other with no period of stability to develop and rebuild systems. (MAF, 1998, p. 2)

Institutional changes occur not only for functional reasons. The FMA was established in 2011, combining the functions of the Securities Commission and Government Actuary which were disestablished, and incorporating other regulatory functions from the Ministry of Economic Development.

In deciding to establish a new financial markets authority, rather than merging the relevant regulatory functions of the Ministry of Economic Development and the Government Actuary into the existing Securities Commission, the main consideration was to signal value in making a change – to the regulator and the wider markets. Advice to Cabinet at the time noted that “it sends a clear signal to both market participants and the regulator that Government is looking for a different approach than currently taken by regulators” (Minister of Commerce, 2010, p. 1).

**F5.19** While there can be benefits to structural changes in regulatory agencies, they can take time to emerge, and will often be disruptive to the smooth operation of regulatory regimes in the interim.

**R5.7** Plans and strategies for undertaking structural change involving regulatory functions should explicitly discuss how the effective operation of those functions will be maintained during the change.
6 Governance, decision rights and discretion

Key points

- The exercise of regulatory powers and functions is constrained by rules, institutional and cultural factors, and governance arrangements. There are strengths and weaknesses in these institutional arrangements in New Zealand.

- Sector or industry experience can be an important voice in governance. There is some confusion about the role Crown entity board members who have been nominated by industry are expected to play as governors. The belief that these board members are representatives of industry is erroneous but appears to be widely held.

- There are risks with governance by non-executive part-time boards drawn from active participants from industry or the business world. The potential for conflicts of interest means that in some cases it is difficult to obtain a quorum of non-conflicted members for decision making.

- The variety of internal governance arrangements and allocation of decision-making rights in regulators appears to be ad hoc rather than based on sound governance principles.

- Ministerial decision making is appropriate in the case of decisions with:
  - significant value judgements, involving trade-offs that are not readily amenable to analysis
  - significant fiscal implications, or which are integral to a government’s economic strategy.

but such circumstances will be rare.

- In designing new regulatory regimes, it is most appropriate to vest significant regulatory decision-making powers in multi-member bodies, unless there are good reasons not to.

- In any system of authority there is tension between certainty and flexibility: between having definite rules and applying them consistently and even-handedly, and enabling decisions to be made according to the specific circumstances of the case and within a broader framework of goals and values.

- The exercise of discretion is constrained by legal and non-legal methods of control, including judicial review and the common law principles of administrative law, guidance and policy that the decision maker adopts to guide the exercise of discretion, cultural and institutional constraints and transparency.

  - There is a range of legal constraints on the exercise of discretionary decisions. In particular, there are strong protections where those decisions intrude on the civil and political rights enshrined in the New Zealand Bill of Rights Act 1990. However, New Zealand is unusual in not acknowledging or protecting property rights.

  - Despite the statutory and common law arrangements that require regulator transparency, several submissions raised concerns about inadequate access to information about regulatory approaches and reasons for decisions.

- Many regulatory agencies also develop policies and guidelines to decision makers who exercise discretion, and publish information about their decision-making processes. These policies and guidance help to ensure that decisions with similar circumstances are made consistently and fairly.
6.1 Introduction

This chapter covers three inter-related concepts: the internal governance of regulatory entities; who has decision making rights; and how much discretion is able to be exercised. In each case the powers, duties and responsibilities of governors and decision makers are bound by important rules and protections. This chapter discusses the strengths and weaknesses of these institutional arrangements in the New Zealand regulatory context.

6.2 The internal governance of Crown entities

Laking (2002) distinguishes between the external and internal governance of organisations:

- external governance – the authority exercised by the central organs of the state, such as the executive, legislature, central government departments, and so on; and
- internal governance – the systems of direction and control within an organisation that are, at the top level, the responsibility of the governing body and senior management.

Laking (2002) says that:

> The role and function of top-level internal governance in all cases is to protect the interest of the state in the public organisation by ensuring compliance with all applicable law, agreements or directives; proper performance (economy, efficiency and effectiveness) in the operations of the organisation; and protection of the rights and lawful interests of stakeholders. (p. 275)

The focus of this section of the report is on the governing role of Crown entity boards.

The role of boards

The Crown Entities Act 2004 outlines the collective and individual duties that board members of Crown entities owe to the minister responsible for the Crown entity (State Services Commission (SSC), 2013a). Their collective duties are to ensure that the entity:

- acts consistently with their objectives, functions, Statement of Intent, and Output Agreement; 29
- performs its functions efficiently and effectively, consistently with the spirit of service to the public, and in collaboration with other public entities, where practicable;
- operates in a financially responsible manner;
- complies with the Crown Entities Act requirements relating to its subsidiaries and other interests.

The individual duties of board members are to:

- comply with the Crown Entities Act and the entity’s enabling legislation;
- act with honesty and integrity, in good faith and not at the expense of the entity’s functions as permitted or required by law;
- exercise the care, diligence and skill that a reasonable person would exercise in the same circumstances, taking into account the nature of the entity and of the action, the position of the member and the nature of their responsibilities.

The respective roles of a Crown entity’s responsible minister and board are complementary (Table 6.1). In undertaking their functions, the minister is supported by a monitoring department (see Chapter 14).

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29 “Statement of performance expectations” will replace “Output Agreement” from 1 July 2014.
### Table 6.1  Roles of ministers and boards of Crown entities

<table>
<thead>
<tr>
<th>Role of the minister</th>
<th>Role of the board</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oversees and manages the Crown’s interests in and relationships with the entities that are within their portfolio</td>
<td>Sets the entity’s strategic direction</td>
</tr>
<tr>
<td>Represents the public interest in the entity (and, in private sector terms, is the de facto “shareholder”)</td>
<td>Exercises the entity’s powers and functions itself or through delegation, empowering the CEO and others to implement the board’s policies</td>
</tr>
<tr>
<td>Ensures an effective board is in place to govern the entity</td>
<td>Appoints and oversees performance of the CEO</td>
</tr>
<tr>
<td>Influences the entity’s strategic direction</td>
<td>Ensures the entity’s functions are performed efficiently and effectively</td>
</tr>
<tr>
<td>Monitors and reviews Crown entity performance and results</td>
<td>Manages risk and ensures compliance</td>
</tr>
<tr>
<td>Manages risks on behalf of the Crown</td>
<td>Provides assurance of fiscal responsibility</td>
</tr>
<tr>
<td>Carries out any statutory responsibilities</td>
<td>Maintains appropriate relationships with key stakeholders</td>
</tr>
</tbody>
</table>

*Source: SSC (2008)*

### The interests of board members

The Civil Aviation Act 1990 and the Maritime Transport Act 1994 provide for the relevant Minister to appoint board members of the Civil Aviation Authority and Maritime Safety Authority respectively. Members must be individuals whom the Minister considers will “represent the public interest” in civil aviation or maritime matters. Before appointing two of the members, the Minister must request, from organisations representing the relevant industry in New Zealand, the names of persons those organisations consider proper candidates for appointment to the Authority.

In its submission, the Civil Aviation Authority says that “However, in the CAA’s case, the Civil Aviation Act 1990 (at s 72A) expressly provides for two of the Authority Board members to be representative of the industry” (sub. 6, pp. 23-24).

Aviation New Zealand notes that there are two industry “representatives” on the CAA board, but complains “of recent times there has been no consultation with industry in terms of nominating potential candidates” (sub. 36, p. 38).

These references to industry representatives on boards appear to misstate the situation in two key respects.

- There is no apparent obligation on the Minister to appoint candidates nominated by organisations representing the relevant industry. This may be common practice, but the only obligation is to seek nominations.
- If appointed, those members are not industry representatives. Their clear function is to represent the public interest, and to fulfil their duties under the Crown Entities Act 2004.

There is clearly some confusion about the role those members who may have been nominated by industry are expected to play as governors. The belief that these board members are representatives of industry is erroneous but appears to be widely held.

There is evidence of confusion around the role that some members of Crown entity boards with industry backgrounds are expected to play.

There are good reasons to have individuals with experience in the sectors being regulated on the board of regulatory organisations. A common complaint in submissions from firms to the Commission was that regulators can lack a genuine understanding of regulated firms. In the Commission’s survey of 1,526
business, 37% disagreed that “regulators understand the issues facing your organisation”, with 25% agreeing.30

The potential for conflicts of interest

Maritime New Zealand notes the potential for real or perceived conflicts of interest arising from having industry participants in governance roles:

If the Board exercised the powers of the Director (i.e. made decisions about the privileges an organisation or individual holds), then arguably Board members should not have interests in, or be from, the civil aviation industry. (sub. 6, p. 24)

This risk is starker in the case of the Financial Markets Authority (FMA), which is governed by a 12-member non-executive part-time board (including associate board members who are treated as full members of the board pursuant to section 11 of the Financial Markets Authority Act 2011), drawn almost exclusively from active participants in the business world. It was reported to the Commission that a consequence of this is that the FMA has on several occasions struggled to reach a quorum of non-conflicted board members to take particular decisions. A quorum of the FMA board requires three members.

In the course of the Commission’s case study into regulation of the financial sector, interviewees raised similar concerns. The large non-executive board arrangement for the FMA was considered unworkable by some interviewees, with some asserting that it created conflicts of interest, slowed decision making, was less efficient than necessary and diluted accountability for decision making. A small full-time executive board was generally favoured by interviewees (Mortlock, 2014).

The SSC’s recently revised Board Appointment and Induction Guidelines (2013a) sensibly note that:

New Zealand’s comparatively small population and the limited number of people who possess particular combinations of skills and experience, mean it is always possible that questions of interests will arise. This will tend to put a focus on identifying and managing interests, rather than disqualifying all those who have interests. (p. 19)

The Commission is also concerned that in a small country like New Zealand the risks of governance members having to deal with potential conflicts of interests in the course of their work is heightened. If a large number of board members are unable to participate in individual decisions, the quality of those decisions may be jeopardised, or the effective governing of the agency may be undermined.

The effectiveness of a part-time board comprised of participants in the regulated sector (as in the Financial Markets Authority) should be reviewed by the State Services Commission before its wider application to other sectors of regulation.

Mechanisms for dealing with conflicts of interest

Acquiring the benefits of appropriate sector expertise on the governance of regulators, while avoiding perceived or real conflicts of interest, requires a number of mechanisms:

- comprehensive declaration of potential conflicts of interest, before candidates are appointed to boards;
- appropriate management of potential conflicts of interest of board members;
- a clear understanding of the role expected of board members.

Existing guidance material appears to comprehensively provide for the first two. The SSC’s guidance (2013a) describes an extensive range of interests to be considered and declared by candidates for appointment, and advice for how ministers should assess those interests when considering appointments.

30 Among the sub-categories of business most likely to agree that regulators understand the issues facing their business were transport, postal and warehousing firms (44% agreed). This may indicate some success in having individuals with expertise in aviation or maritime matters on the boards of those respective regulators. Firms most likely to disagree included those involved in agriculture, forestry and fishing (47% disagreed), rural businesses (46% disagreed) and exporters (45% disagreed).
SSC induction material for new members of Crown entity boards (2008) also provides a practical discussion of managing real or perceived conflicts of interest.

There is good SSC guidance on managing conflicts of interest for members of Crown entity boards.

The Crown Entities Act 2004 states that board members have an individual duty to act with honesty and integrity, and to act in the entity’s interests and not their own interests (ss. 54-55). While board members may be appointed for their particular backgrounds, experiences or expertise, they should not act in their governance capacity as “representatives” of any particular sectoral group.

The Organisation for Economic Co-operation and Development (OECD, 2013a) notes that where industry stakeholders are members of a regulator’s governing body, it is important to be clear that they are participating as experts rather than as representatives. It says that the risk of governors acting as representatives is heightened where the regulator has an explicit “industry development” objective – as the FMA does, for example.

The Victorian government’s principles for the governance of regulators (2010) make a similar point: that industry stakeholders on governing bodies are there to take decisions in the public interest rather than as representatives. However, it also states that where there is a need for formal representation of specific stakeholders, this should be addressed by establishing an advisory or consultative committee rather than through representation on the board.

**Issues in the New Zealand context**

The FMA told the Commission that industry participants in governance roles allowed it to more effectively evaluate what it described as the trade-offs involved in its dual objectives of regulating markets and promoting economic growth, and that its board provided particular expertise around the latter objective. However, the Financial Markets Authority Act 2011 makes clear that the FMA’s main objective is “to promote and facilitate the development of fair, efficient, and transparent financial markets”.

The Council of Trade Unions (CTU) considers that:

> [t]he independence, effectiveness and public confidence in a regulator can be enhanced by having balanced representation of affected interests in its governance structures. The balance is essential to prevent any suggestion of capture, but the presence of such parties can give assurance that the regulator is constantly reminded of the realities on the ground and there is monitoring of undue political influence or influence from any one party. It can also assist in creating a cooperative atmosphere for ongoing work despite differing interests. … New Zealand has moved much too far down the path of stripping governance boards of representatives of those affected. That should be reversed. (sub. 25, pp. 19, 26)

The Commission endorses the view of the OECD and the Victorian government. The CTU is right about the importance of different perspectives and the value that those with practical expertise and experience can bring. However where governors are framed as *representing* sectional interests, tensions will inevitably arise between the governance and representative roles. Board members should not be described as, or act as, sectoral representatives, to help ensure that this tension is resolved in favour of ensuring an agency effectively and lawfully exercises its functions and powers to achieve its statutory objectives.

Exceptions to this should be rare. One example might be where government established co-management arrangements with Māori or other groups.
Board members of Crown entities should not be appointed to act as representatives of external groups. Regardless of the backgrounds, experiences and prior or ongoing associations that make them valuable as members, their duty should always be to ensure the entity acts in a manner consistent with its statutory objectives and functions, and not as the representative or agent of any external group. The exception is where co-management arrangements are expressly intended.

The particular framing of the Civil Aviation Act 1990 and the Maritime Safety Act 1994, which provide for candidates for board membership to be nominated by representatives of the respective industries, has given rise to confusion about whether some board members are acting as representatives of external groups on the board of the regulator. Board induction guidance should be amended to emphasise that they are not.

The State Services Commission’s guidance about appointing board members to Crown entities and its induction material for new board members provide good information on the duties of members. But it should update these documents to emphasise that members are not appointed and should not act as the representative or agent of any external group.

### 6.3 The allocation of decision rights

There are a wide variety of decision-making models within New Zealand regulatory regimes, even among similar regulators such as those that regulate the financial and investment sectors (Figure 6.1).

**Figure 6.1 Decision rights in selected sector regulatory regimes**

- **Reserve Bank of New Zealand**
  - The regulatory powers of the RBNZ are vested in the Governor of the RBNZ – it is a single decision-maker model.
  - There is a RBNZ board, but it is solely responsible for assessing the performance of the Governor and RBNZ (and has specific responsibilities regarding the appointment of the Governor and Deputy Governor).
  - The RBNZ board has no powers in relation to the RBNZ’s regulatory functions. It can advise the Governor, but the advice is non-binding.

- **Financial Markets Authority**
  - The FMA governance model comprises a relatively large board, all of whom are non-executive.
  - The board is a decision-making body and exercises the powers of the FMA except to the extent that the board delegates specific powers to the CEO.

- **Commerce Commission**
  - The Commerce Commission is governed by a relatively small commission of mainly full-time commissioners.
  - The Commissioners have the authority to exercise the powers of the Commission.

- **Overseas Investment Regime**
  - An application by an overseas person to acquire certain types of sensitive land requires approval from the Minister of Finance and the Minister for Land Information.
  - The Minister of Finance has delegated to the regulator (the Overseas Investment Office) the power to make all decisions under the Act on whether or not to grant consent to an overseas investment in significant business assets.
  - The OIO is a unit within LINZ (a public sector department).

There are also hybrid models in the allocation of decision rights. For example, in the Civil Aviation Authority the Board takes decisions about policy and procedures, and the Director of Civil Aviation takes decisions about individual regulated parties.
This variety partly reflects that each regulator was established at different times and in different contexts. It also reflects a tendency for regulatory functions to be grafted onto existing regulatory agencies without the governance arrangements necessarily changing. This is the case with the Reserve Bank of New Zealand (RBNZ), for example, where its governance arrangements were established in 1989 and largely designed for its primary function of monetary policy. Little specific regard was given then to the governance issues applicable to its regulatory functions. Moreover, since 1989, its regulatory functions have expanded substantially, but its governance arrangements have not changed.

The variety of governance, funding and accountability arrangements also reflects that some are constituted as independent Crown entities (the FMA), some as government departments (the Overseas Investment Office) and some as entities of a unique institutional form – as with the RBNZ.

There may be sound reasons for some differences in governance arrangements across these regulators, given the different scale and scope of their respective regulatory functions, and their other responsibilities (for example, as with the RBNZ’s monetary policy role). However, at least in some respects, the differences appear to be *ad hoc* and not necessarily well anchored to sound regulatory governance principles.

F6.4 The variety of internal governance arrangements and allocation of decision-making rights in regulators appears to be *ad hoc* rather than based on sound governance principles.

**When should ministers take decisions?**

The allocation of decision-making power in regulatory regimes to ministers inherently means less independent regulation. In Figure 5.3 the Commission outlined features that indicate a need for less or more independence when establishing regulatory regimes. These features are salient not only to whether the regulatory functions are established in an agency close to or at arm’s length from ministers, but also who in the regulatory regime should be allocated decision-making powers.

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Box 6.1 **Submitters’ views on the role for ministers in decision making**

Value decisions were those most commonly cited by submitters as being appropriate for ministerial decision making. These sorts of decisions usually entail a balancing of trade-offs which are not easily resolved on a technical basis. In these situations, “good” decisions should reflect community valuations, and ministers are elected to reflect those values.

Tasman District Council considered that it would be useful to have “some criteria around contentiousness, costs implications, sensitivity, that might assist in determining where the locus of decisions rests with an elected representative or a public official” (sub. 1, p. 3).

Carter Holt Harvey was of the view that “regulation requiring value judgements should be retained at the highest reasonable ‘political’ level rather than devolved, to encourage accountability for subjective interpretation” (sub. 8, p. 8).

The FMA said: “In our experience, matters that are reserved to Ministerial decision-making are likely to be sensitive or in the national interest, and therefore may require a broader array of advisory inputs than purely that of the regulator. We would prefer that this type of decision-making be the exception rather than the rule, given that a Minister may be challenged over perceptions of independence” (sub. 53, p. 4).

By contrast, Aviation New Zealand considered that decisions which should be the preserve of the Minister included “where matters are akin to tertiary legislation … Rule making; policy decision which may not end up in a Rule; delegation of powers to external groups or individuals; international treaties, extensions of emergency rules; fees and charges” (sub. 36, p. 15).
Ministerial decision making is appropriate in the case of decisions with:

- significant value judgements, involving trade-offs that are not readily amenable to analysis
- significant fiscal implications, or which are integral to a government’s economic strategy.

Such circumstances will be rare. The Commission prefers mechanisms that allow for the transparent intervention of ministers as a safety valve (see Chapter 5), to the broad allocation of decision-making power to ministers.

Designers of regulatory regimes should avoid allocating regulatory decision-making powers to ministers unless good reasons are established. Decisions where ministerial decision making is likely to be appropriate include decisions with:

- significant value judgements, involving trade-offs that are not readily amenable to analysis
- significant fiscal implications, or which are integral to a government’s economic strategy.

Single member decision making or multi-member decision making?

In many circumstances, multi-member decision making can offer significant advantages (Figure 6.2).

**Figure 6.2** When single-member or multi-member decision making is appropriate

- the regulator has power to make administrative decisions that have significant commercial consequences—a group of decision makers is less likely to be ‘captured’ than an individual and a group will bring differing perspectives to decisions;
- the regulator has a large industry and functional scope and has responsibility for a high volume of regulation—the decision-making workload can be distributed across several members;
- the regulator is a general rather than industry-specific regulator—input from several areas of relevant expertise is available;
- the regulations being implemented are complex and principles-based, requiring a greater degree of judgement in their interpretation—collective decision making provides better balancing of judgement factors and minimises the risks of ‘maverick’ judgements; and/or
- regulatory consistency over time is very important—a multi-member decision-making body provides more ‘corporate memory’ over time as all members are unlikely to change at once.

- the area of regulation is well defined and the subject matter not particularly complex, or processes and decisions are largely standardised or routine such as in much of business or occupational licensing; or
- in some cases where the potential commercial, environmental or public safety risks of the regulated activities are relatively low.

Source: Adapted from Victorian State Services Authority, 2009.

In its submission Chorus also argued in favour of boards rather than individuals taking decisions: “The perception and actual decisions of an informed diverse group is likely to be more robust than the potential risks involved in individual judgements and personalities. This can also mitigate any concerns about regulatory capture while still enabling individuals to be informed and connected to the real world” (sub. 51, p. 11).

A prominent example of an individual being vested with significant decision-making power is the Governor of the Reserve Bank (Box 6.2).
This development in Reserve Bank decision making is a welcome evolution. In time, lessons about the effect of the Governing Committee on regulatory (and other) decisions would provide evidence about the benefits of different decision-making models in other areas of regulation.

Single decision makers do not operate in a vacuum. Typically, decisions are taken on the basis of analysis and advice. Individual decisions, whether taken by a minister or chief executive, reflect a judgement about the arguments for and against decisions which are made by others.

But there are limitations on individual decision makers. Compared to multi-member decision making approaches, individual decision makers are more subject to:

- bias that arises from having a single perspective;
- bounded rationality (limited information, time, and capability to process information)
- an overreliance on heuristics (decision making shortcuts)
- the particular incentives that apply to them individually, whether political, reputational, or financial.

Multi-member decision making processes can bring a broader range of skills and perspectives to bear on regulatory decisions, reducing the likelihood of error or maverick judgments.

Box 6.2 Decision making at the Reserve Bank of New Zealand

In its submission, the Reserve Bank said that it had “functioned well under the single decision-maker model since the late 1980s” (sub. 9, p. 5).

In the course of the Commission’s case study into regulation of the financial sector, interviewees raised some concerns about the single decision-maker model in the RBNZ. Some thought it concentrates too much power in one person and creates a risk of poor-quality decision making, including because of over-confidence.

Many favoured a model in which the governance of the RBNZ and other regulators is vested in a small (4–5) member full-time executive board, with a view to deriving the benefits of diversity of skill and experience and reducing the risk of dominance by one person. Some stakeholders noted that this governance structure is commonly applied in other countries, including in Australia in respect of the Australian Prudential Regulatory Authority and the Australian Securities and Investments Commission.

Indeed the Governor of the Reserve Bank is moving tentatively in that direction, as he noted in a speech in 2013:

In order to assist with major policy decisions, we recently introduced a Governing Committee, comprising the Governor, the two Deputy Governors and the Assistant Governor, under the chairmanship of the Governor. The Governing Committee will discuss all major monetary and financial policy decisions falling under the Bank’s responsibilities, including decisions on monetary policy, foreign exchange intervention, liquidity management policy, prudential policy (both micro and macro) and other regulatory policies. To date, individual Governors have taken responsibility for particular areas of the Bank, such as operations, monetary policy and financial stability. Going forward Governors will have more individual and collective involvement in key decisions taken across all areas of the Bank. This is the same decision-making framework adopted by the Bank of Canada, which also has a single decision-maker model. As with the Bank of Canada, the Governor retains the right of veto on committee decisions. The Committee formalises and expands past practice. (Wheeler, 2013)
In designing new regulatory regimes, it is most appropriate to vest significant regulatory decision-making powers in multi-member bodies, unless there are good reasons not to. But a range of day-to-day administrative decisions are more appropriately vested in individuals.

There is greater potential for errors or poor-quality decisions where individuals rather than groups take those decisions. Where individuals take day-to-day administrative decisions, internal review processes (see Chapter 10) can be a useful check to ensure such decisions are being exercised in a consistent way.

Designers of new regulatory regimes need to consider providing for the internal review of day-to-day administrative decisions which are taken by individuals.

The Commission asked government regulators who within their organisation took decisions about a range of activities: approval of activities; frequency and targeting of monitoring; issuing warnings; seizing property or contraband; and initiating prosecutions.

- Regulators appear to make extensive use of delegation, including from ministers to chief executives, boards to chief executives, chief executives to managers, boards to senior managers, and from one management tier to another.

- Overwhelmingly, regulators told us that these sorts of decisions were taken by governors or management (often senior management). Areas where decisions were taken by frontline staff included:
  - approval of activities pursuant to the Gambling Act 2003 by the Department of Internal Affairs;
  - monitoring and approval of energy efficiency regulations by the Energy Efficiency and Conservation Authority;
  - monitoring activity undertaken by the New Zealand Walking Access Commission;
  - seizing property/contraband under the Climate Change Response Act 2002 by the Environmental Protection Authority
  - issuing warning by Health & Safety inspectors of the Ministry of Business, Innovation and Employment31;
  - monitoring and approval of activity undertaken pursuant to the Cadastral Survey Act 2002 by Land Information New Zealand.

The Commission’s impression is that this understates the amount of decisions which are taken by frontline staff, in part because not all agencies responded to the information request. There are no clear patterns in terms of who makes different types of decisions.

Chapter 12 points to concerns on the part of regulatory staff about training and support for skills development. It also reports strong perceptions on the part of businesses that regulatory staff lacked skills and knowledge.

There is extensive delegation of regulatory decisions within New Zealand regulatory regimes. In practice decisions are taken by a range of compliance staff, managers, chief executives, boards and ministers.

31 This is now the responsibility of WorkSafe New Zealand.
Designers of regulatory regimes need to consider the capabilities required to take regulatory decisions in specifying the nature of decisions regulators need to take, assigning decision rights, and providing for delegation.

6.4 Discretion

Discretion arises when an official is empowered to exercise public authority and afforded scope to decide how that authority should be exercised in particular circumstances (Pratt & Sossin, 2009, p. 301). Regulatory discretions typically require the decision maker to exercise their own judgements within the parameters of legally acceptable options.

**Discretionary powers have increased**

There are a number of reasons why regulation has increasingly involved the use of discretionary decision-making:

- the increasing span of regulatory control;
- increasingly technical regulation;
- providing for unforeseen events;
- more principle/outcome based regulation.

**Span of control issues**

As the modern state has encroached into more areas of life, there has been an evident increase in discretionary powers. Legislatures, with their limited capacities and resources, manage the growth in the size, diversity, and complexity of regulation by delegating specific problems and undertakings to subordinate and specially created authorities. Control over a wide range of matters such as social welfare, public order, land use and resources planning, economic affairs, and licensing is delegated to officials with varying degrees of guidance as to the policy goals to be achieved or the standards by which they are to be achieved (Galligan, 1986).

**Increasingly technical regulation**

Discretion is not an inevitable consequence of delegation. However, a related explanation is the increasing belief that many regulatory activities are to be approached as technical or scientific problems to be dealt with by specialist agencies (Galligan, 1986). This does not mean that judgments by regulators should only be judged against technical and scientific criteria.

**Providing for unforeseen events**

John Locke, in his Second Treatise of Government (1690), recognised the inevitable place of discretion in governmental decision making. He wrote: “Where the legislative and executive power are in distinct hands, as they are in all moderated monarchies and well-framed governments, there the good of society requires that several things should be left to the discretion of him that has the executive power”. This was necessary because legislatures could not “foresee and provide all laws that may be useful to the community”.

**A move to principle-based/outcome-based regulation**

The change in the nature of the tasks undertaken by the state has led to the regulation being judged by its outcomes, not whether the decisions have been made by the impartial application of fixed rules. This naturally leads to a tendency towards the use of discretion (Galligan, 1986).

In New Zealand, the Public Service Act 1912 set up a professional career public service. Public servants were managed and employed by a permanent commission that was independent of political control. Walsh (1991) has argued that it introduced a bureaucratic, rule-based model of public service in order to combat political patronage and corruption. As Hughes and Smart note:
Prescribing a rigid set of processes, rules and hierarchies achieved equity, integrity and procedural due process in the public service. In practice, this meant hard constraints on managers. Control was centralised at the top of a strict hierarchy, with input control as a strong focus. As the Treasury argued (1987, p. 58), ‘the tendency [was] to keep managers’ discretion at a minimum’. (2012, pp. 3-4)

One of the features of the 1980s state sector reforms was to provide managers with greater control over employment and mix of inputs, to allow the more effective and efficient delivery of outputs and outcomes within a stronger performance management framework. Reform of specific regulatory regimes tended to provide more discretion in order to support the focus on outputs and outcomes.

Regulators submitted that the expectation on them to be risk-based inevitably entails the exercise of discretion. It follows that capability is a key consideration for regulators that exercise discretion.

The key issue here is the need for a more comprehensive understanding of the business of compliance in the sense that it’s about changing behaviour. Modern compliance thinking suggests this is about problem solving and risk management – involving the use of soft and hard interventions with the right tool needing to be chosen at the right time to address the right problem. The key to risk based approaches is in having effective information management (intelligence) systems to collect, collate and analyse information. This involves investment in people and technology beyond that used to undertake individual regulatory transactions. (CCCP, sub. 12, p. 9)

F6.11 Administrative discretion is a feature of many regulatory regimes. Principle-based or outcome-based regulatory regimes inherently involve the exercise of discretion, as do risk-based approaches to implementing regulation.

Does discretion lead to uncertainty?

In any system of authority there is tension between certainty and flexibility: between having definite rules and applying them consistently and even-handedly, and enabling decisions to be made according to the specific circumstances of the case and within a broader framework of goals and values (Galligan, 1986).

Rules that are narrowly drawn and strictly applied offer consistency and predictability in the way powers are exercised. They also provide a system of control on officials that minimises the opportunity for the arbitrary or unpredictable exercise of power.

Certainty and predictability as to how regulatory agencies will apply and enforce a given regulation can also be desirable from an economic perspective. The more certain and predictable the actions of institutions and their treatment of property and other rights, the more confidence business has to invest and develop ways of doing things better (Kalderimis, Nixon & Smith, 2013).

The Commission’s survey of businesses revealed that more than a third of businesses considered regulators to be unpredictable, and the reasons for their decisions to be unclear (Figure 6.3).

Figure 6.3 Business perceptions of the predictability and clarity of regulator decisions

<table>
<thead>
<tr>
<th>Regulators’ decisions are unpredictable</th>
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<tbody>
<tr>
<td>Strongly agree</td>
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<td>6%</td>
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<table>
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<tr>
<th>The reasons behind regulators’ decisions are clear</th>
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</thead>
<tbody>
<tr>
<td>Strongly agree</td>
</tr>
<tr>
<td>2%</td>
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</table>

Source: Colmar Brunton, 2013.
Certainty is not the only consideration

Overly detailed and complex rules may also in practice have the effect of undermining the achievement of policy objectives. An OECD report observed that “[p]eople lose confidence in regulators and governments if they are required to comply with technical rules that do not appear to relate to any substantive purpose” (2000, p. 16). The report highlighted the following features of strict rule-based approaches as particularly problematic:

- regulatory unreasonableness;
- imposition of uniform, detailed, and stringent rules in situations where they do not make sense; or
- regulatory unresponsiveness or failure to consider arguments by regulated enterprises that exceptions to the technical rules should be made.

The OECD report cited studies that show the negative effects of rigid and unresponsive rules on compliance rates. A study by Bardach and Kagan (1982) found that when business people felt that regulators were being overly legalistic when applying rules and imposing fines, they would tend to respond by scaling down their efforts to comply with the intent of the law. They would instead aim to achieve only the minimal level of compliance that the rules required. Other studies have shown that relying on strict, coercive strategies to achieve compliance often breaks down the goodwill and motivation of those actors who were already willing to be social responsible (Braithwaite, 1993).

Narrow and strictly applied rules can impose rigidity and an inability to accommodate new, unforeseen, complex, or unusual situations. The Reserve Bank’s submission recognised the necessity of its discretionary enforcement powers over financial regimes, “where issues that arise are often not ‘black and white’ and discretion in relation to the exercise of enforcement powers is necessary” (RBNZ, sub. 9, p. 8). The Electricity Authority (sub. 50) made a similar point about the desirability of discretion in dealing with complex situations or highly event-specific scenarios.

Rules also restrict what a decision maker may properly consider in making a decision. This may prevent making decisions that provide the best accommodation of values and purposes and which achieve the best result in the particular case (Galligan, 1986). ANZ’s submission stated: “the key benefit of regulatory discretion is that it can better align the operation and effect of regulation with the specific factual context in which it applies” (sub. 24, p. 9).

Certainty is important, but is not the only objective of regulation. Other general criteria – such as legitimacy, efficacy, and fairness – also need to be balanced in regulatory design.

Discretionary decision-making need not lead to uncertainty

As recognised by submitters, certainty and flexibility in regulatory rules each offer benefits and drawbacks. Tasman District Council submitted:

> The term “risk-based” is just another way for exercising a discretion as to whether or not to make a decision in a particular way. ... There are situations where prescription and certainty is appropriate and equally there are situations where flexibility and discretion should likewise be possible. It is not a question of one without the other. (sub. 1, p. 4)

Kalderimis, Whitford, and Brown (2013) argue that certainty and discretion should not be seen as diametric opposites or as the same type of concept. Certainty is an objective of regulatory design, while discretion accorded to institutions is a mechanism that can be used to achieve various objectives of regulatory design. As Kalderimis, Whitford, and Brown note:

> Thus, the use of discretion will, in some circumstances, increase certainty; in other cases, discretion may reduce certainty but serve other objectives (such as flexibility or durability), and the reduction in certainty caused by the presence of discretion may be mitigated by other mechanisms. (p. 2)

For example, the Reserve Bank of New Zealand Act 1989 vests considerable discretion in the Governor, but the Governor exercises those powers in such a way that preserves tolerable levels of certainty. In monetary policy this is done by having transparent objectives, providing comprehensive information on the economic...
context, regular statements signalling future policy intentions, and a usually incrementalist approach to the use of policy instruments.

There are a range of legal constraints and non-legal constraints on the exercise of discretion which help to prevent uncertainty.

**Constraints on discretion**

The exercise of discretion is constrained by legal and non-legal methods of control, including judicial review and the common law principles of administrative law; guidance and policy that the decision maker adopts to guide the exercise of discretion, cultural and institutional constraints and transparency.

The arbitrary exercise of excessive discretion would subvert the rule of law by making rule-making retroactive, “as the manner in which such discretion will be exercised is never knowable prospectively…” (Salembier, 2002, p. 172).

The central principle of the rule of law is that state power, to the extent that it affects individuals, must be exercised according to binding general rules made and known in advance, and must be of sufficient specificity to allow individuals to know with tolerable certainty their rights, obligations, and liabilities (Box 6.3).32

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**Box 6.3  The rule of law**

The rule of law has been defined in many ways, but in Commonwealth countries, it often encompasses such ideas as “the absence of arbitrary power on the part of the government”, equality before the law and the right to due process, and the central role of the common law which encapsulates such concepts as “the right to personal liberty or the right to public meeting” (Dicey, 1889, pp. 173-83).

Lord Bingham, former Lord Chief Justice of England and Wales, identified eight principles of the rule of law.

- The law should be accessible and so far as possible, intelligible, clear and predictable.
- Questions of legal right and liability should ordinarily be resolved by applying the law and not the exercise of discretion.
- The laws of the land should apply equally to all, save to the extent that objective differences justify differentiation.
- Ministers and public officers at all levels must exercise the powers conferred on them in good faith, fairly, for the purpose for which the powers were conferred, without exceeding the limits of such powers and not unreasonably.
- The law must afford adequate protection of fundamental human rights.
- Means must be provided for resolving, without prohibitive cost or inordinate delay, _bona fide_ civil disputes that the parties alone are unable to resolve.
- Adjudicative procedures provided by the state should be fair.
- The rule of law requires the state to comply with its obligations in international law as in national law.

*Source:* Bingham, 2010; Dicey, 1889.

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32 For classic accounts of the rule of law, see Fuller (1964) and Raz (1979).
There is a range of legal and non-legal constraints which means that the exercise of discretion need not be at odds with the rule of law. There are strengths and weaknesses of these constraints in the New Zealand context.

**Legal constraints on discretion**

Public sector decision makers do not have unfettered discretionary power. Although Parliament often confers wide discretions when empowering public authorities, discretionary power has legal limits: “[D]iscretion is not absolute or unfettered”.

When a statutory provision provides, for example, that “the Minister may make such orders as he or she thinks fit”, it does not literally mean what it says because that would enable arbitrary decision making (Joseph, 2007, p. 849). However unlimited the decision maker’s discretion may appear to be, there are legal limits on the exercise of that discretion.

Some limitations on the exercise of discretion may be explicit: for example, the purposes for which a particular power was given or the criteria to be applied in exercising it may be set out in the legislation. Other limits will be implied by the other parts of the legislation. Others will derive from general rule of law principles in the particular context of administrative law and the exercise of decision making powers (Figure 6.4).

**Figure 6.4** Administrative law principles about the exercise of discretion

In exercising discretionary powers, administrative law principles require decision makers to:

- use discretionary powers in good faith and for a proper purpose;
- base their decision on logically probative material (rational reasons, information that proves the issues in question, relevant and reliable evidence);
- consider only relevant considerations;
- give adequate weight to a matter of great importance, but not give excessive weight to a relevant factor of no great importance;
- exercise their discretion independently and not act under the command of any third person or body;
- give proper, genuine, and realistic consideration to the merits of the particular case, and not apply policy inflexibly; and
- observe the basic rules of procedural fairness.

Other principles of administrative law preclude public officials from:

- making decisions in matters in which they have an actual or reasonably perceived conflict of interest;
- improperly fettering their discretion (or that of future decision makers) by, for example, adopting a policy that prescribes decision making in certain circumstances;
- exercising a discretion in a way that is so unreasonable that no reasonable person would have exercised the power in that way;
- exercising a discretionary power in such a way that the result is uncertain;
- acting in a way that is biased or conveys a reasonable perception of bias;
- making decisions that are arbitrary, vague or fanciful;
- refusing to exercise a discretionary power in circumstances where the decision maker is under a duty to do so; and
- unreasonably delaying the making of a decision that the decision maker is under a duty to make.


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Chapter 10 more fully describes the role of judicial review as a check on the exercise of discretionary powers. It notes that judges undertaking judicial review will scrutinise administrative decisions more closely where those decisions infringe on fundamental rights. As the LAC guidelines note:

As the public powers to interfere with individuals’ rights and interests grow, many statutes have required greater procedural protections (sometimes using the phrase “principles of natural justice”). The courts have long shown themselves willing to “supply the omission of the legislature” if a statute which confers public power to affect rights and interests is silent about procedural protections. (2012, p. 169)

The New Zealand Bill of Rights Act 1990 also offers protection against certain rights being infringed in regulatory decision-making, unless the intrusion can be reasonably justified or is authorised by legislation (Box 6.4).

Box 6.4 New Zealand Bill of Rights Act 1990

The New Zealand Bill of Rights Act 1990 (BORA) protects a broad range of civil and political rights from being infringed by the legislative, executive, or judicial branches of government, or by “any person or body in the performance of any public function, power, or duty conferred or imposed on that person or body by or pursuant to law” (s. 3).

The rights protected may be “subject only to such reasonable limits prescribed by law as can be demonstrably justified in a free and democratic society” (s. 5).

Regulatory decisions are reviewable by the courts for breach of BORA. Decisions will be struck down by the courts if:

- they intrude on a right or freedom;
- the intrusion is neither reasonable nor demonstrably justified; and
- no authorisation for the intrusion can be inferred from the empowering act.

The effect is that administrative decisions must be proportionate – justified in the circumstances, in a free and democratic society – to withstand BORA challenge.

However, some submissions pointed to weaknesses in the protections accorded to other important rights. Federated Farmers was “particularly concerned about insufficient recognition let alone protection of private property rights.” (sub. 11, p. 2)

A paper from the New Zealand Institute for the Study of Competition and Regulation has noted that:

New Zealand is distinguished by having among the weakest protection of private rights in the OECD, a history of confiscation of private property rights, and a long-standing failure to recognise the protection of the basic human right of property rights. (Evans, Quigley and Counsell, 2009, p. 1)

A private members bill to enshrine private property rights in BORA was defeated in 2007 by 107 votes to 12, with the Select Committee report recording:

We acknowledge that there is significant public support for further legal protection of private property rights in New Zealand. We heard arguments that the absence of the right to own private property from the Act is anomalous. We also note that the enshrining of private property rights in legislation, often alongside personal rights, is common in other jurisdictions.

... We consider that the bill should not proceed. We are not fundamentally opposed to the principle of the bill, but given the possible consequences of its enactment, we do not support it in its current form. We consider that exhaustive research is needed into how private property rights can be protected in the New Zealand environment before any amendment to legislation should be considered. In addition, the impact of such amendments on existing legislation and their potential
Legal constraints on the exercise of discretionary power are important to ensure that decisions are taken consistently with Parliament’s objectives in establishing the regime, and actually contribute to the effectiveness of the regime by protecting decision-makers from tunnel vision:

From the perspective of an administrative agency, this proposition may seem counter-intuitive. Rule of law norms limit discretion, and thus, can be perceived as obstacles to effectiveness. They restrict the ability of agencies to “do whatever it takes” to get the job done, whatever that job may be. From the perspective of government officials, those restrictions make the achievement of policy objectives seem more difficult because problems cannot be tackled directly and independently. Instead the agency must share the enterprise with other state organs—relying upon the legislature to formulate effective general rules; and upon courts or tribunals to interpret rules properly and produce sensible results in particular cases. But in spite of this perception, these limitations make the actions of state actors more effective, not less so. They improve decisions by insulating decision-makers from compromise, politics, and their conviction that they alone know what is best. (Pardy, 2008, p. 4)

Cultural and institutional constraints
An official exercising power does so within a particular cultural and institutional context that materially shapes the exercise of power.

The attitudes, values, and behaviours of the individual and the institution within which they operate are critical to the process and outcome of decision making. Some writers have labelled these internal institutional constraints as the “inner check” (Waldo, 1984) or checks based on institutional professionalism and moral standards (Finer, 1941).

Certain features of an institution’s “decision architecture” (the institutional framework for determining how and by whom powers are exercised) will “channel” discretion and make it more (or less) likely that decisions made are fair and rational. One public administration academic identified the following features of an institution’s “decision architecture” as critical to ethical decision making (Cox, 2000, p. 249):

- fairness and equity are of paramount concern;
- “good” management is a product of capacity and desire;
- an ethic of “doing what is right”;

There is a range of legal constraints on the exercise of discretionary decisions. In particular, there are strong protections where those decisions intrude on the civil and political rights enshrined in the New Zealand Bill of Rights Act 1990. However, New Zealand is unusual in not acknowledging or protecting property rights.
multiple participants;
articulated value statements (used to preview and review decisions); and
accountability systems (grievance procedures).

The importance of a regulator’s culture is discussed in Chapter 7.

In addition to institutional constraints, underlying frameworks of legal and political principles shape the way that discretion is exercised. They also underpin the justification and legitimation of decision outcomes (Carter, 2009). These frameworks define the boundaries of behaviour and the capacity to act (Arendt, 2003). Levy and Spiller (1994) refer to these frameworks as the customs and other informal but broadly accepted norms that are generally understood to constrain the action of individuals or institutions.

Writing in the context of examining discretion in Anglo-Saxon jurisdictions, Galligan (1986) argues that the underlying framework of legal and political principles in these countries directs officials to exercise their discretionary powers in compliance with standards of rationality, purposiveness, and morality. These shared values and norms exist and operate independently from formal legal constraints. The frameworks help to:

- ensure that the exercise of power is based on reasons and that those reasons are applied consistently, fairly, and impartially;
- eliminate decision making by whim, chance, or caprice;
- develop general standards in making decisions/fair procedure; and
- open decision-making processes to external public scrutiny.

In the absence of institutional constraints and underlying frameworks that promote ethical decision making, explicit legal restraints on discretion may be ineffective. Levy and Spiller (1994) observe that the institutional and cultural realities of some countries may mean that the only way to constrain administrative arbitrariness is to almost totally withdraw administrative discretion.

**F6.13** Institutional and cultural constraints on the exercise of discretionary power support legal constraints by promoting ethical decision making.

**Transparency can shed light on the exercise of discretion**

Hood (2006) notes that “transparency is a term that has attained quasi-religious significance in debate over governance and institutional design” (p. 3). Transparency has a long pedigree. Writing in the 1790s, the English philosopher Jeremy Bentham declared:

I do really take it for an indisputable truth, and a truth that is one of the corner-stones of political science – the more strictly we are watched, the better we behave. (quoted in Hood, 2006, p. 9)

Heald (2006) describes the different application of transparency to different steps in the public sector production process Figure 6.5).

It adopts the standard framework of distinguishing between inputs, outputs, and outcomes. Each of these is characterized as ‘events’ and represented by a rectangle. ‘Events’ represent points/states that are externally visible and – at least in principle – measurable. Events are lined by ‘processes’, with the three rectangles being connected by two ellipses, labelled as ‘transformation’ (inputs into outputs) and ‘linkage’ (outputs into outcomes). Processes are not measurable in the same way as events, though they can be described, if the information is available. Generally, transformation processes are better understood than linkage processes, not least because intervening variables are more important and unpredictable in the later. (p. 30)
In New Zealand, as elsewhere, control of state activities has traditionally focused on inputs, with more recent focus on measuring public sector outputs (and an often-expressed desire to measure the elusive outcomes).

*Ex post* accountability mechanisms are designed to provide transparency around inputs and outputs. However, real-time mechanisms are needed to provide transparency around the transformation process and linkage process.

In a regulatory context, this means that regulators need to be transparent in two main ways: transparency of decisions and procedural transparency.

- **Transparency of decisions** – the regulator gives clear reasons when making a decision about a particular individual or firm (addressing the transformation process).

- **Procedural transparency** – the regulator provides clear justification and useful extra information about its regulatory processes more generally in terms of how those processes contribute to the desired outcomes of the regulatory regime (addressing the transformation and linkage processes).

IAG New Zealand’s submission notes a number of benefits to transparency, reinforcing the value of transparency to a range of participants in a regulatory regime:

Regulated market participants have a valid interest in the process, rationale and outcome of regulation. In a complex sector, or where there is complex regulation, it is especially important that the rationale for a regulatory decision is made apparent and is justified.

Further, transparency in the regulatory process is recognised as having a number of benefits, including:

- protection against regulatory capture and bias;
- mitigating inadequate public sector information availability;
- counterbalancing rigidity in regulatory style;
- addressing market uncertainty based on policy risk; and
- promoting meaningful accountability to affected parties. (sub. 10. p. 6)

Regulator transparency is required by law. The Official Information Act 1982 provides for making official information available to the public. Section 23 of the Act provides an express right to be given reasons for decisions that affect a person (including a business). In addition, regulators may be required under their own Acts to make certain information publicly available. For example, s. 62 of the Commerce Act requires the Commerce Commission to prepare and send key stakeholders a draft determination about restrictive trade practices, before it makes a final decision. Table 6.2 provides an indication of the types of information that New Zealand regulators make publicly available.
### Table 6.2 Public availability of documentation on regulatory practices and principles

<table>
<thead>
<tr>
<th>Regulator</th>
<th>Which regulatory practices and principles are documented and made publicly available?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broadcasting Standards Authority</td>
<td>Decisions are made public and reasons are provided in all decisions.</td>
</tr>
<tr>
<td>Civil Aviation Authority</td>
<td>Much of the information on the Authority’s approach to regulatory compliance is in its regulatory operating model. This is supported by much other material that is available through the website. Other detailed operations policy and procedural guidance is not generally publicly available. However, copies of relevant documents can be made available if required.</td>
</tr>
<tr>
<td>Commerce Commission</td>
<td>Major regulatory decisions typically have full reasons published with them. Also available are enforcement response guidelines, criminal prosecution guidelines, enforcement criteria, written reasons for merger clearance and authorisation determinations, merger and acquisitions authorisation guidelines (including process guidelines), fact sheets, and guidance on compliance issues for information disclosure.</td>
</tr>
<tr>
<td>Commission for Financial Literacy and Retirement Income</td>
<td>Analysis of submissions received on any new or varied Code of Practice, and the Retirement Commissioner’s recommendations.</td>
</tr>
<tr>
<td>Department of Conservation</td>
<td>Decision-making processes for significant regulatory decisions, policy on who to consult and when; reasons for significant regulatory decisions and guidance material for regulated parties in meeting regulatory obligations.</td>
</tr>
<tr>
<td>Department of Internal Affairs</td>
<td>Censorship policy and gambling compliance policy publicly available, along with enforcement action and gambling regulations. Also available are anti-money laundering codes of practice, guidelines and supervisory framework, reasons for significant charities regulatory decisions, and guidance material for charities in meeting regulatory obligations.</td>
</tr>
<tr>
<td>Electricity Authority</td>
<td>Consultation charter available (Code amendment principles on pages 4-6 of the Charter).</td>
</tr>
<tr>
<td>Energy Efficiency and Conservation Authority</td>
<td>Factsheets and website information on how to comply with regulations, compliance and enforcement Policy and website information on how to comply with regulations.</td>
</tr>
<tr>
<td>Environmental Protection Authority</td>
<td>Decision-making processes for significant regulatory decisions; policy on who to consult and when; reasons for significant regulatory decisions and guidance material for regulated parties in meeting regulatory obligations.</td>
</tr>
<tr>
<td>Financial Markets Authority</td>
<td>Decision-making processes for significant regulatory decisions; reasons for significant regulatory decisions; guidance material for regulated parties in meeting regulatory obligations and an enforcement policy and compliance focus guide.</td>
</tr>
<tr>
<td>Gas Industry Company Limited</td>
<td>Gas Industry Co makes few regulatory decisions. Where it does, it has little discretion. The decisions it can make are defined by specific processes in rules and regulations. The process for recommending regulations is set out in the Gas Act 1992.</td>
</tr>
<tr>
<td>Health and Disability Commissioner</td>
<td>Publication of decisions online and guidance material for complaints management in line with the Health and Disability Commissioner Act 1994 is online.</td>
</tr>
<tr>
<td>Land Information New Zealand</td>
<td>Decision-making processes and guidance material for all parties (staff and regulated parties).</td>
</tr>
<tr>
<td>Maritime New Zealand</td>
<td>Maritime New Zealand compliance operating model (includes prosecution policy).</td>
</tr>
<tr>
<td>Ministry of Business, Innovation and Employment</td>
<td>Decision-making processes for significant regulatory decisions are made publicly available through the publication of regulatory impact statements, and sometimes Cabinet papers online. For approved codes of practice, the public is notified of the decision when it is published in the Gazette. The two processes also set out the reasons for significant regulatory decisions for the public. Guidance material to help regulated parties meet their regulatory obligations is made publicly available through the Ministry’s website, as is the enforcement policy, which is a guide about when different enforcement mechanisms are to be used (for example, when</td>
</tr>
</tbody>
</table>
### Limited access to information about regulatory approaches and reasons for decisions

Despite the statutory and common law arrangements that require regulator transparency, several submissions raised concerns about inadequate access to information about regulatory approaches and reasons for decisions. Mortlock Consultants commented on the lack of requirements to publish statements of regulator approaches:

Some regulators are required by statute to publish statements of their approach to regulation – such as section 75 of the RBNZ Act, which requires the Reserve Bank to publish the principles on which it acts, or proposes to act, in determining applications for bank registration, and in imposing, varying, removing, or adding to conditions of registration. However, this requirement is not consistently applied across regulators; many are under no parallel obligation. Partly as a result of this, there is a lack of transparency in the policy framework applied by some regulators in interpreting their responsibilities and in exercising their powers. (sub. 31, p. 6)

IAG considers this criticism also applies to the transparency of regulatory decision making:

In our experience, transparency and stakeholder engagement often ends with formal consultation processes. The reasoning process of the regulator and the factors that have ultimately influenced its decision are not always made available to interested parties. (sub. 10, p. 6)
To the extent that lack of transparency is a concern, it may contribute to the perception by some businesses that regulatory decisions are unpredictable and unclear. Lack of clarity and unpredictability of regulatory decisions can in turn heighten investment uncertainty.

[Lack of transparency in the policy framework applied by some regulators in interpreting their responsibilities and in exercising their powers] impedes the accountability of regulators and makes it more difficult for regulated entities to interpret the actions of their regulators. (Mortlock Consultants, sub. 31, p. 6)

Chapter 4 discusses the potential benefits of requiring new regulators to publish a statement that explains their interpretation of their mandate, noting the general (but not universal) support for the Electricity Authority’s Interpretation of the Authority’s statutory objective (2011). One aim of the Electricity Authority’s statement is to support consistent decision making.

The Civil Aviation systems vests considerable discretion in the Director. In general we think this is appropriate however equally we believe the regulator must back decisions made with a high level of transparency and analytical capability. (Aviation New Zealand, sub. 36, pp. 30-31)

Table 6.2 indicates that publishing the reasons for decisions is common. Many regulatory agencies also develop policies and guidelines to decision makers that must exercise discretion, and information about their decision-making processes. These policies and guidance help to ensure that similar decisions are made consistently and fairly. Unlike legislation, policies and guidelines do not have the force of law and decision makers should be able to depart from them where appropriate.

The Office of the Ombudsman’s guide on good decision making (2012a) advises that policies and guidelines should:

- be straightforward and contain a clear purpose statement;
- be flexible to cover a range of circumstances;
- set out how they relate to the relevant legislation;
- set out the relevant considerations that the decision maker must take into account;
- be communicated to relevant staff; and
- be made available to the public.

The development of policy and guidelines about how decisions are to be taken can promote good decisions and good regulatory outcomes. Making these available to the public enables interested people to learn about the processes and potential outcomes of the decision-making process. It also helps to reduce any tension between certainty and discretion.

All regulators should publish and maintain up-to-date information about their regulatory decision making processes, including timelines and the information or principles that inform their regulatory decisions.

### 6.5 Summing up

Because discretionary decision making is inherent in prevalent regulatory approaches, the governance arrangements, norms and rules that influence and constrain that discretion are important.

The Commission has found that there is variation in governance and decision-making approaches among New Zealand regulators, mixed practice on the part of regulators as to how and why they take decisions, misunderstanding about the formal governance arrangements that ensure regulators remain focused on the objectives of their regime, and gaps in the legal protections which ensure regulators operate in a way that does not unjustifiably infringe on rights and freedoms.
Regulator culture and leadership

Key points

- “Regulator culture” refers to the shared norms, values and beliefs that influence the behaviour of staff working within a regulatory agency. These norms, values and beliefs are heavily influenced by:
  - the beliefs, values and assumptions of the founding leaders of the organisation;
  - the shared experiences of staff in the performance of the duties; and
  - new beliefs, values, and assumptions brought in by new staff, particularly new leaders.

- From outside an organisation it can be hard to distinguish problems arising from a “dysfunctional culture” from those arising from more tangible factors such as the design of legislation or capability issues. When looking to improve regulator performance, it is important to understand if what is required is a change of practice within a given culture, or a change in culture.

- While making generic conclusions is hard, the Commission’s analysis suggests the following points.
  - There is evidence of risk-averse cultures within New Zealand regulators. It is important to understand whether this culture is appropriate for achieving the regulator’s statutory objectives, or whether it has emerged as means of protecting the reputation of the regulatory body by reducing the likelihood of negative political or media attention.
  - Previous restructuring of regulatory organisations has required significant cultural shifts. Governments need to consider potential cultural issues when contemplating changes to the functions or structure of an existing regulator.
  - Stakeholders often perceive the quality of engagement as a “window” to the culture of a regulator. In making this connection, it is important to assess whether the regulator’s approach to engagement is driven by its values and beliefs, or whether it is driven by some other factor – such as the legislative environment or available resources.
  - A common understanding of the purpose and mission of a regulatory body is the first step in developing culture. While Chief Executives believe corporate culture is influencing the behaviour of frontline staff, survey evidence indicates that central government regulatory workers do not perceive that top managers communicate a clear organisational mission.

- The culture of a new regulatory body can be shaped in a number of ways.
  - Government can seed a “desirable” culture by appointing founding leaders with values, beliefs and experiences compatible with those it believes are most conducive to achieving the desired regulatory outcomes. However, selecting the “right people” does not guarantee that the “right” culture will emerge – the actions of founding leaders are the key to embedding culture.
  - Monitoring bodies and central agencies can use formal and informal mechanisms to reinforce favourable cultures in new regulatory bodies.

- While legislative provisions can codify certain actions (such as consultation), they do not guarantee that a regulatory body will develop deeply held values around the importance of the behaviours. The culture of the organisation will evolve as its members discover what works and what does not.

- Despite the conflicting views among theorists, a considerable amount of literature exists on the topic of cultural change management. The chapter draws on this literature to provide some principles for managing cultural change.
7.1 Introduction

Organisational culture affects how regulatory bodies undertake their duties and, as such, plays an important role in achieving regulatory objectives. However, while the importance of “culture” is widely recognised the concept remains ambiguous. An important aim of this chapter is to provide clarity around the concept of regulator culture in the hope of distinguishing “cultural problems” from the numerous other factors that incentivise and motivate regulator behaviour.

This chapter begins by drawing on the influential work of Schein (1984, 2010) to provide a framework through which to understand the concept of organisational culture. Then the characteristics of “good” organisational culture within regulatory organisations are discussed, followed by a discussion of the mechanisms through which culture is embedded into a new organisation.

7.2 What is regulator culture?

In this report, the term “regulator culture” is used to describe the norms, values and beliefs shared by staff working within a regulatory agency. These include the norms of behaviour and commonly held notions around the factors that are important for organisational success and how success is best achieved. Schein (2010) notes that the concept of culture covers a wide range of factors that influence behaviour. These include:

- Competencies that are passed on to new staff without necessarily being formally articulated;
- Mental models and cognitive frameworks that guide how tasks are to be approached; and
- The policies and ideological principles that guide the how staff interact with stakeholders.

Schein (2013) summarises the concept of culture as:

> Culture is best thought of as what a group has learned throughout its own history in solving its problems of external survival in internal integration. ...It is best conceptualised at its core as the shared, tacit assumptions that have come to be taken for granted and that determine the members’ daily behaviour. (p. 1)

Culture can be likened to a “psychological contract” that lays out the unwritten rules that govern how people within an organisation are expected to act, think and feel and how they can expect others to act, think and feel (Brewis & Willmott, 2012). So culture plays a key role in the internal coordination of staff and in how the organisation adapts to changes in its external environment.

The conceptualisation of culture as an organisational phenomenon is different, but inherently related, to the higher-level concept of regulatory culture that can exist at a level beyond an organisation (that is, the “regulatory culture of New Zealand”). Bohne (2011) argues that regulatory cultures are specifically characterised by:

- shared values and beliefs concerning the relationship between government, markets, and the individual;
- common legal and administrative traditions and principles;
- the extent to which public authorities enjoy regulatory discretion; and
- the distribution of regulatory competencies and related organisational structures. (p. 258).

These interconnected characteristics are the focus of other areas of the report and, as such, this chapter concentrates on the organisational culture of New Zealand regulatory bodies.

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34 Used in this way, the term “regulator culture” should be interpreted as short-hand for “the organisational culture of a regulatory body”.

Levels of regulator culture

Assessing the culture of an organisation is hard. At the most basic level, culture can be examined by looking at the visible attributes of a regulatory body – what some refer to as the “look and feel” of the organisation or the “artefacts” of the organisation (Figure 7.1). This includes, for example, the architecture of its offices, the design and style of its publications, the technology it uses, the language it embraces, its published organisational processes, and its style of interaction with internal parties.

Figure 7.1 Levels of regulator culture

While these visible “artefacts” of organisational culture can be readily observed, they are difficult to decipher. That is, while an observer can describe the “look and feel” of an organisation, it is hard to know whether this reflects the behaviour of the organisation or, more specifically, the extent to which artefacts reflect deeply held values and beliefs that actually drive behaviour (Gagliardi, 1990; 1999). Further, the interpretation of artefacts will inevitably be influenced by the beliefs and values of the person observing the artefacts. As Schein notes,

[it is] dangerous to try to infer deep assumptions from artefacts alone because a person’s interpretation will inevitably be projections of his or her own feelings and reactions. For example, when you see a very loose informal organisation, you may interpret it as ‘inefficient’ if your own background is based on the assumption that informality means playing around and not working. Or alternatively, if you see a very formal organisation, you may interpret that to be a sign of ‘lack of innovative capacity’ if your own experience is based on the assumption that formality means bureaucracy and standardisation. (Schein, p. 25, 2010)

At a deeper level, culture can be analysed by looking at the espoused values and beliefs of a regulator – commonly found in corporate documents such as organisational strategies, annual reports and statements of intent.

For some organisations, espoused values and beliefs may have emerged through time as a set of “tried and tested rules”. However, for others the espoused values may be “aspirational” rather than deeply engrained and widely accepted. This means they may not actually reflect the beliefs of those working within the organisation (Argyris & Schön, 1978; 1996). For example, a new regulator may espouse the importance of close relationships with other regulators while simultaneously rewarding actions that undermine the espoused value of “coordination” (such as by rewarding staff that “lay claim” to functions previously undertaken by an existing regulator).

The deepest level of cultural analysis involves examining the basic underlying assumptions that guide the behaviour of regulators. These are “unconscious and taken for granted ways of seeing the world and are the source of the values and artefacts” (Brewis & Willmott, 2012, p. 378).

The underlying values and assumptions of regulatory organisation ultimately guide behaviour, but these are the hardest element of culture to measure and examine.
The espoused values of new regulators may be “aspirational” rather than deeply engrained and widely accepted. This means such values may not actually reflect the beliefs of those working within the organisation or be reflected in their actions.

Subcultures within regulators

Regulator culture is influenced by the broader context in which the organisation operates and the interaction of subcultures within its workforce. The broader context includes the wider national culture and the institutions and laws that influence the formation of the regulator. Federated Farmers notes some of these broader forces in its submission:

New Zealand’s heritage, circumstances, culture and values, its size and geography, and its political environment all make for a unique regulatory “style”, which means that regulation that might be appropriate overseas may not be so in New Zealand. (Federated Farmers, sub. 11, p. 7)

Subcultures on the other hand, emerge within regulators as subgroups develop their own assumptions and methods for undertaking specific tasks. These subcultures can reflect functional units, geographic groups, professional groups, or the place in the regulator’s hierarchy.

- **Functional units**: These are groups within a regulator that undertake common tasks or groups of tasks. For example, regulators that implement multiple pieces of regulation may find subcultures emerging within the different units responsible for the different pieces of legislation.

- **Geographic groups**: Many regulators operate in multiple regions. These regional groups face their own set of local conditions and challenges. Through time, subcultures can emerge in response to conditions. As a result, how the geographic groups implement regulation can vary according to the predominant subculture of the local group.

- **Professional groups**: Occupations can develop subcultures of their own based, for example, on common educational backgrounds or the requirements of occupational licences. As Schein notes “…engineers, doctors, lawyers, accountants … will differ from each other in their basic beliefs, values, and tacit assumptions because they are doing fundamentally different things, have been trained differently, and have acquired a certain identity in practicing their occupation” (p. 261). Strong professional subgroups can create a situation where individuals have a stronger affiliation to their profession than to their organisation.

- **Place in the regulator’s hierarchy**: People working at the same level of an organisation’s hierarchy often undertake similar tasks. This shared experience can give rise to the development of a set of shared assumptions that can be thought of as the subculture of that group. For example, the “subculture of the senior management team” or the “subculture of inspection officers”.

7.3 **Forces shaping the culture of regulators**

Schein (2010) has argued that the organisational culture emerges from three sources:

1. the beliefs, values and assumptions of the founding members of organisations – particularly its leaders;

2. the shared experiences of group members as their organisation evolves; and

3. new beliefs, values, and assumptions brought in by new members and leaders.

While Schein’s model for culture formulation is derived with reference to the private sector, its theoretical foundations (rooted in psychological theories) hold for any group of people whose patterns of behaviour (and ultimate success) are informed by a history of shared learning and stable membership. Indeed, Schein argues that groups with a high turnover of staff and leaders, or that have not shared the experience of challenging situations, may not develop a set of shared assumptions (that is, the group may not have develop a shared culture).
Leaders as a source of regulator culture in new organisations

Founding leaders have a profound impact on the culture that emerges within a new regulatory agency. These leaders are important because they set the values and the environmental context in which the new regulator will operate. They do this by drawing on their own experiences, convictions and assumptions to propose answers to the questions that young organisations face about how to interact with stakeholders and how best to achieve their statutory purpose (Schein, 2010). In this way, founding leaders provide a source of ideas and behaviour models that support the operation of the regulatory organisation.

Several inquiry participants noted the importance of leadership. The submission from Minter Ellison Rudd Watts was typical of the sentiments expressed:

… leadership has a significant influence on the culture of an organisation. A good leader of a regulatory agency will encourage a productive and collaborative multi-disciplinary team environment within the organisation, and effective two way communication with external stakeholders. This is a key building block to ensure regulation is informed by the best available evidence. (sub. 28, p. 46)

Founding leaders also affect the “tone” of an organisation through their recruitment decisions. By recruiting staff that leaders feel are likely to share their convictions and assumptions, they are able to embed patterns of behaviour into a new organisation. This commonly involves recruiting staff with similar experiences or professional backgrounds as the founding leader. The mechanisms through which leaders embed culture are discussed in Section 7.8.

Experiences as a source of regulator culture

As a regulator matures, the approaches of the founding leaders (and the values and assumptions that underpin these approaches) are tested through their repeated application. Successful approaches become embedded in the beliefs and values of the organisations (Schein, 2010). Unsuccessful approaches are re-examined and new assumptions evolve to take their place (or existing assumptions are modified). In this way, the collective experiences of the groups within regulatory organisations combine to shape its culture. As Gordon (1991) notes:

“…culture formulation is neither a random event nor an action dependent solely on the personalities of founding leaders or current leaders, but it is, to a significant degree, an internal reaction to external imperatives”. (p. 404)

Problems can arise however if deeply embedded assumptions restrict the ability of an organisation to adapt to changes in its external environment. For example, problems can arise if the established “ways of doing things” are a barrier to adopting new technology or more modern management practices. The Commission has previously found evidence of such workplace cultures at some New Zealand’s seaports:

A major factor preventing the capture and sharing of additional value is the poor relationships between management, and workers and unions at some ports. These relationships resemble the ‘old school’

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Footnote: Founding leaders can be “formal” leaders in the sense of an organisational hierarchy and informal leaders within the organisation that lead groups in ways that lie outside the formal structure of the organisation.
adversarial model of industrial relations, rather than the ‘productive employment relationships’ envisioned as the object of the Employment Relations Act…

...In such workplace environments, entrenched positions and cultures tend to view negotiations in terms of a ‘winner’ and a ‘loser’, rather than an opportunity to develop mutually beneficial outcomes. This is particularly prevalent where management and unions do not share a common view on what constitutes a successful port operation. This can result in resistance to changes that are perceived as being inconsistent with either party’s preferred view of the future. (NZPC, 2012b, p. 138)

While not a regulatory example, the above excerpt highlights how deeply embedded assumptions, can have negative impacts on performance if they become outdated or inconsistent with the assumptions needed to promote success.

Similarly, problems can also arise if measures of “success” for a regulator (or subgroups within it) do not align with the intent of the regulation. This may arise, for example, if internal processes reward behaviour that promotes the interests of the organisation (or subgroup) at the expense of behaviours that promote good regulatory outcomes. These issues are inherently linked to those of transparency, accountability and performance monitoring discussed in Chapter 14.

**Injection of new members and leaders as a source of regulator culture**

Just as founding leaders bring with them their own experiences, beliefs and traditions, so too do new employees. This injection of new ideas, values and ways of doing things can influence organisational culture, particularly when they are the result of structural changes (such as the merging of two or more agencies) or the result of changes in key personnel such as the Chief Executive or members of the Senior Leadership Team.

![F7.2](image)

The culture that emerges within a new regulatory agency will be influenced by (1) the beliefs, values and assumptions of its founding leaders; (2) the experiences of members of the organisation as it matures; and (3) the injection of new beliefs, values and assumptions through new members.

### 7.4 Types of organisational cultures

This section provides a brief overview of two influential frameworks for classifying organisational cultures:

- Hood’s (1998) examination of four styles of public management organisation (the Grid and Group framework); and

The value of these frameworks does not come from classifying an organisation as having a single cultural type. Indeed attributes of several cultural types may be observable within the one organisation. The true usefulness of these typologies comes from:

- a) assisting designers of regulation in thinking about the cultural mix best suited to the risk being managed; and
- b) helping public sector leaders understand the prevailing culture within an existing organisation in order to identify when a rebalance may be needed (O’Donnell and Boyle, 2008).

**Grid and Group typology**

Hood’s book, *The Art of the State*, is arguably the most comprehensive attempt to examine the influences of culture within the context of regulatory organisations. The book draws on the work of anthropologist Mary Douglas (1982) to argue that it is possible to understand how an organisation behaves by examining the extent to which two key dimensions influence behaviour. Hood labels these dimensions “grid” and “group”.

The grid dimension refers to the extent to which public management is conducted according to well-understood and accepted rules. These rules reduce the extent to which behaviour is open to negotiation or individual discretion. The group dimension refers to the extent to which collective choice of the group constrains individual choice.

Hood combines these two dimensions into a matrix to illustrate four basic organisational approaches to public management: hierarchist, fatalistic, individualistic, and egalitarian (Table 7.1).

- **Hierarchist approach** - characteristic of organisations that are socially coherent (high “group”) and strongly influenced by well-established rules (high “grid”).

- **Fatalistic approach** - characteristic of organisations influenced by rules (high “grid”) but which have low levels of social cooperation and cohesion (low “group”). Hood notes that this approach to management will arise when “cooperation is rejected, distrust is widespread, and apathy reigns” (p. 9).

- **Individualistic approach** - characteristic of organisations that stress individual negotiation and bargaining. These organisations have low levels of social cohesion (low “group”) and are not strongly influenced by rules (low “grid”), preferring to handle decisions through negotiation rather than stipulated rules.

- **Egalitarian approach** - characteristic of organisations with a high level of social cohesion (high “group”) that is not strongly influenced by rules (low “grid”). These organisations tend to have highly participatory structures within which each issue is debated individually.

### Table 7.1 Four styles of public management organisations

<table>
<thead>
<tr>
<th>Grid</th>
<th>Group</th>
<th>Organisation Approach</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>Low</td>
<td>The Fatalist Way</td>
<td>Low cooperation, rule bound approaches to organisations. Example: Atomised societies sunk in rigid routines (Banfield, 1958).</td>
</tr>
<tr>
<td>High</td>
<td>High</td>
<td>The Hierarchist Way</td>
<td>Socially cohesive, rule-bound approaches to organisation. Example: Stereotype military structures (Dixon, 1976).</td>
</tr>
<tr>
<td>Low</td>
<td>Low</td>
<td>The Individualist Way</td>
<td>Atomised approaches to organisation that stress negotiation and bargaining. Example: Chicago school doctrines of “government by the market” (Self, 1993) and their antecedents.</td>
</tr>
<tr>
<td>Low</td>
<td>High</td>
<td>The Egalitarian Way</td>
<td>High-participation structures in which every decision is “up for grabs”. Example: “Dark green” doctrines of alternatives to conventional bureaucracy (Goodin, 1992).</td>
</tr>
</tbody>
</table>


An important contribution of Hood’s work is his analysis of the way that different organisational approaches respond to public management “disasters”. He argues that “responses to scandal or catastrophe in public management … are likely to be a key test of cultural bias” (p. 25). Specifically, Hood argues these four organisational approaches will respond to disaster in the following ways.

- **Hierarchist responses** will tend to emphasise the problem as arising from a lack of coordination, poor procedures and accountability (or a failure to adhere to existing rules and procedures). The solution is therefore to tighten the rules and authority structures so the event will not happen again.

- **Egalitarian responses** will tend to see rules and procedures as the source of the problem rather than the solution. They tend to view public management disasters as arising from the fact that public sector workers are forced to operate in rules-laden systems, where rules are often contradictory and there is a tacit expectation that they will be broken to “get the job done”. Egalitarian organisations would therefore see a greater level of worker empowerment as the solution to public sector disasters. This would let workers at the lower end of the hierarchy challenge authority and professional self-interest and “blow the whistle” on matters of public concern.
• Individualist responses will see the failure as stemming from too much collectivism and a misplaced faith in the value of rules, planning and authority structures (as opposed to price systems, tort law and well-designed incentive systems). From the individual perspective, the solution to disasters is to strengthen the incentives on individuals to perform. This means promoting competition between workers and organisations, and introducing mechanisms that resemble markets wherever possible.

• Fatalistic responses will view the disaster as a unique (one-off) event that, while tragic or embarrassing, was only foreseeable in hindsight. A fatalistic response will therefore argue that the world is inherently uncertain, and that even the most complex rules and procedures are subject to unpredictable events beyond their control. Accordingly, a fatalistic organisation would resist blaming an individual or system for the disaster and would see any attempt to do so as arbitrary and potentially counter-productive.

These responses are summarised in Table 7.2.

<table>
<thead>
<tr>
<th>Table 7.2 Responses to public management disasters</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fatalistic response</strong></td>
</tr>
<tr>
<td>Stress on: unpredictability of events and unintended effects</td>
</tr>
<tr>
<td>Blame: the “fickle finger of fate” (or chaos theory interpretation of how the world works)</td>
</tr>
<tr>
<td>Remedy: minimal anticipation, at most ad hoc response after event</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Individualist response</strong></th>
<th><strong>Egalitarian response</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Stress on: individual as self-interested rational choosers</td>
<td>Stress on: groups and power structures</td>
</tr>
<tr>
<td>Blame: faulty incentive structures through over-collectivisation and lack of price signals</td>
<td>Blame: abuse of power by top level government/corporate leaders, system corruption</td>
</tr>
<tr>
<td>Remedy: market-like mechanisms, competitions and leagues, information to support choice (such as rating systems)</td>
<td>Remedy: participation, communitarianism, whistle blowing.</td>
</tr>
</tbody>
</table>


**Competing Values Framework**

Another prominent typology for categorising organisational culture is the Competing Values Framework (CVF). Quinn and Rohrbaugh (1983) originally developed this typology. Bradley and Parker (2006) have used it more recently to examine the implications of culture in the context of “new public management” models.

The CVF is based around two dimensions of competing values:

• the extent to which an organisation is internally or externally focused (the horizontal axis); and
• the extent to which an organisation is flexible or controlled by rules and procedures (the vertical axis).

Based on these dimensions, the CVF identifies four broad types (models) of cultures (Bradley et al, 2006):

• **The Human Relations Model**: Cultures where a high value is placed on training and the development of human resources. These organisations tend to have a high level of moral and social cohesion, and emphasise teamwork with managers mentoring and encouraging staff;

• **The Open System Model**: Cultures with an emphasis on growth, innovation and entrepreneurship in which managers placing a high value on individual initiative and effort;

• **The Internal Process Model**: Cultures typified by rule-based hierarchical structures in which managers encourage conformity and adherence to established rules and formal processes. Bradley et al (2006) note (p. 90) that this model is typical of traditional public sector organisations;
• **Rational Goal Model**: Cultures that are production focused and goal oriented in which managers tend to emphasise efficiency, productivity and outcomes.

**Figure 7.3** The Competing Values Framework


### 7.5 Risk of misdiagnosing culture as a problem

Viewing culture through the lenses of artefacts, espoused values and underlying assumptions helps provide structure around observations of New Zealand regulators. Specifically, it provides a framework for thinking about whether observed behaviour is indeed the result of shared and deeply held assumptions, or is in fact the result of organisational processes and structures that, while adhered to, do not constitute the organisation’s “culture” as defined above. The above discussion also highlights the difficulties in deciphering organisational culture from outside an organisation.

The existence of subcultures raises further questions around whether observed behaviour is representative of the culture of the organisation as a whole, or simply that of the group whose behaviour is being observed.

These questions are important as, **having confirmed that a problem does actually exist**, government responses to a problem arising from a dysfunctional culture are significantly different to those that arise through, for example, poorly designed internal processes or a lack of capability.

Yet the influence of cultural norms on decision making is hard to assess due to the many factors that go into making regulatory decisions. As Meidinger (1987) notes,

> …critical aspects of regulation are in fact worked out in the daily interactions of members of regulatory communities. In these interactions structural constraints, political pressures, general cultural assumptions, legal requirements and bureaucratic procedures are actually turned into a form of regulatory culture which organises the activities of regulation. …Ironically, this is the aspect of regulation that we know least about. (p. 373)

Even so, it is vital to understand whether what is required is a **change in regulatory practice within a given culture**, or a change in culture. To do this requires targeted analysis of the culture within a regulatory agency and the institutional factors that impact the way it operates.
When looking to improve the performance of a regulator, it is vital to understand whether what is required is a change in regulatory practice within a given culture, or a change in culture. This requires targeted analysis of the culture within a regulatory agency and the institutional factors that impact the way it operates.

7.6 Inquiry participants’ views on what constitutes good regulatory culture

Submissions to the inquiry have identified a number of attributes as being conducive to achieving good regulatory outcomes. It is worth noting that while these attributes provide a sense of what is seen as a desirable regulator culture, not all attributes will be appropriate for all situations. Even so, the attributes of a “good” regulator culture identified in submissions provide a sense of the cultural characteristics that stakeholders see as important. These characteristics include:

- **Cultures that embrace the regulator’s role as an educator and facilitator of compliance, as opposed to an enforcer of rules**
  
  The culture of the organisation should educate, encourage and promote regulatory compliance, and avoid a pure compliance and process (box ticking) mentality. The regulators need to be able to engage at a technical level with the regulated and seek to help the regulated to comply. In other words, an effective regulator can take a constructive leadership role. (IPENZ, sub. 21, p. 11)

- **Cultures that encourage internal debate and robust evidence-based decision making**
  
  The opportunity for greater scrutiny of a regulator’s decisions may be a useful way of creating a culture of robust and evidence-based decision making. An expectation and measure of an efficient regulatory system should be that challenging decisions made by the regulator are not successfully appealed even where that opportunity exists. (Carter, Holt Harvey, sub. 8, p. 12)

- **Cultures with a high degree of individual accountability**
  
  Accountability and review arrangements drive the culture of an organisation, the quality of decisions, confidence in the regime and ultimately the ability of the regime to meet its objectives. This is particularly the case where the regulator is independent and where decisions may have direct impact on New Zealand’s productivity. (Genesis Energy, sub. 48, p. 6)

- **Cultures that encourage the exchange of information in an environment of trust**
  
  What is needed is what is sometimes referred to as a “just culture”, an atmosphere of trust in which people are encouraged, even rewarded, for providing essential safety-related information - but in which they are also abundantly clear about where the line must be drawn between acceptable and unacceptable behaviour. (Civil Aviation Authority, sub. 6, p. 67-68)

  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… (Ministry of Business, Innovation and Employment, sub. 52, p. 5)

- **Cultures that appropriately match the interface with regulated parties to the type of regulation being implemented**
  
  For example, Vector has argued that the culture of the Commerce Commission is influenced by its “protective” consumer protection functions, and that the resulting “adversarial” culture is not conducive to its functions as an economic regulator - which, Vector argues, requires a more facilitative culture. (sub. 29)

In addition to the areas identified in submissions, a number of characteristics can be taken from the extensive literature on public sector management. These include:

- **Cultures that are adaptive.** For example, Kotter and Heskett (1992) note that “only cultures that can help organisations anticipate and adapt to environmental change will be associated with superior performance over long periods of time” (p. 44);
Cultures that promote innovation and entrepreneurial activity: For example Moon (1999) advocates entrepreneurship as a means of promoting effectiveness and flexibility; and

Cultures that embrace “traditional” public sector values such as the provision of free and frank advice, service to the community and acting in the best interests of the nation (Van Wart, 1998).

There are also high-level characteristics that all public service agencies should have embedded in their organisational culture. These include openness, honesty, transparency, aversion to corruption and respect for the rights of New Zealand citizens.

7.7 The culture of New Zealand regulators

The inquiry timeframe does not allow for a detailed cultural evaluation of all New Zealand regulators. Even so, the Commission has sought to use a range of information sources to gain some insights into the culture of these organisations. The primary information sources used are:

- previously published government reports and research papers;
- results from the Commission’s survey of chief executives of regulatory agencies (NZPC, 2014a);
- results of a survey of Public Service Association (PSA) members undertaken by the PSA and Victoria University of Wellington (see Chapter 1 for an overview of the survey: VUW IRC & PSA, 2014);
- results from the Commission’s survey of 1,526 businesses (Colmar Brunton, 2013);
- submissions to the inquiry; and
- engagement meetings with inquiry participants.

The key insights from these information sources are summarised below.

Weak communication and learning cultures

Good communication can help a regulatory body respond rapidly to changes in its operating environment. These include:

- external changes such as the emergence of new risks or patterns of non-compliance; and
- internal changes such as the emergence of capability gaps or dysfunctional subcultures.

Where the need for good internal communication is embedded in the culture of a regulatory body, its members share a belief that this flow of information is vital for the success of the organisation. If this underlying assumption exists, leaders will develop systems and processes to facilitate the flow of information throughout the agency, and will actively promote these networks by rewarding those that use them.

Yet results from a recent survey that the PSA conducted indicate that poor communication is an issue within some New Zealand regulators. For example, the survey found that (on average) regulatory workers in central government disagree that knowledge and information are shared throughout their organisations. These workers were significantly less likely than non-regulatory workers to perceive that knowledge is shared.

Related to good communication is the ability of an organisation to learn from practical experience. Again the PSA survey suggests some shortcomings in the current practices of regulators. For example, the survey found that (on average) regulatory workers in central government disagree that management systems allow them to challenge poor practices. And regulatory workers are significantly less likely than non-regulatory...
workers to perceive that they can challenge practices. The Council of Trade Unions expressed similar views, noting that

\[\text{In reality it is likely to be very difficult for staff to go against the intended culture of the agency if a dissonant approach is required to provide sound advice and regulatory decisions. (sub. 25, p. 13)}\]

The Ministry of Business, Innovation and Employment (MBIE) argued in their submission that cultural and attitudinal barriers that prevent issues being raised and addressed are a possible indicator of future regulatory failure. They also note that

\[\text{...the response to issues and risks being raised has resulted in a cultural tendency to work-around systemic issues rather than addressing them. Given this seems to be a key component of all of our regulatory failures, we question whether these barriers may exist within a regulatory systems, or may extend across the public service more generally. (sub. 52, p. 3)}\]

Without in-depth analysis of each regulatory body, it is hard to know whether communication difficulties are the result of cultural factors or symptomatic of wider institutional or management problems. However, a number of cultural explanations are possible.

One explanation is that the increasingly technical nature of regulations has led to the need for modern regulators to employ people from a broad range of professional backgrounds. While today’s regulatory bodies still rely on “traditional” compliance professionals, they also need specialised technical skills in areas such as forensic accounting, environmental science, or engineering. These professions have their own professional beliefs, tacit assumptions, and language. The results of the PSA survey may reflect difficulties in integrating these professional subcultures into a single regulatory body. (Professional subcultures are discussed further below.)

An alternative (cultural) hypothesis is that communication problems are the result of geographic subcultures. Regional subcultures may have developed inward-looking cultures that do not value communication outside their sphere of influence.

Finally, as suggested by MBIE, cultural resistance to communication may be the result of negative experiences in the past – where “raising issues” has negatively impacted the “success” of a group. One example is where staff are criticised for the existence of a risk, rather than rewarded for making management aware of the risk. If this pattern is repeated, then (through time) the group will learn that communicating risks is detrimental to personal success.

The Commission is interested in hearing the views of stakeholder on these hypotheses.

The Commission notes that some regulatory agencies have strong learning cultures. For example, the 2012 Performance Improvement Framework Review of New Zealand Customs indicated strengths in this area. Similarly, the Civil Aviation Authority appears to have a strong culture of learning, which is evident by the emphasis it places on developing systems to identify emerging risks.
Culture of risk aversion impacts regulatory decisions

In some situations, a strong culture of risk aversion can lead to a “letter of the law” approach by regulatory staff, which can undermine the cost-effectiveness of the regulation for the community. For example, the regulator may be overly stringent in applying the rules, so that there are no incidents that might call into question the effectiveness of the regulator (regardless of the compliance costs on the regulated party).

In other situations, a culture of risk aversion can have the opposite impact and lead to a regulator being reluctant to prosecute for fear of the reputational damage if the prosecution is unsuccessful in court. The Compliance Common Capability Programme (CCCP) notes:

In respect to risk aversion in particular, being mainly concerned about risk to the regulator can either create a heavy handed approach (to avoid being seen not to do enough); or a light handed approach – to avoid being seen to be heavy handed and risk the possibility of “losing cases”… the way to overcome this is to ensure that regulators are competent, well trained and professional in their approach – and that organisations that have, for example, heavy reliance on industry personnel, are “balanced” by having professional regulators in their midst as well. This also deals with the issue of professional capture. (CCCP, sub. 12, p. 10)

Aviation New Zealand also comments on the impact of risk aversion:

Most regulators appear to hold preconceived notions of the “way” issues should be treated. They also tend to be quite risk averse and this acts as a hand break [sic] on industry. (sub. 36, p. 38)

So too does Federated Farmers:

What is clear to farmers is that New Zealand has a problem with both the volume of legislation and regulation passed and its quality. This is worsened by public, media, and political “angst” over real and imagined risks, accidents, and misdeeds. This angst has encouraged in both central and local government a culture of excessive risk aversion and a “government knows best” mentality. (sub. 11, p. 10)

The PSA survey results also reveal signs of risk aversion within regulatory organisations. The survey found that, on average, central government regulatory workers were significantly less likely than workers in non-regulatory roles to perceive that managers take prudent risks. Given the role of managers in providing leadership models for the organisation, these results are indicative of risk-averse cultures.

The Commission’s survey of 1,526 businesses (Colmar Brunton, 2013) also adds weight to the evidence of risk aversion within some regulatory agencies. The survey found that 32% of businesses agreed with the notion that regulators were inflexible and adopted a letter of the law approach (20% disagreeing) (see Figure 7.4). Interestingly, 45% of the businesses that felt regulators were inflexible were from the “rental, hiring and real estate services industry”. Further, businesses in rural areas rather than urban areas were more likely to find regulators inflexible. 37

There may be several explanations for these results. However, in light of the above discussion it is reasonable to suggest that the results are due in part to risk aversion.

Arguably, the strongest indicator of risk-averse cultures came from the results of the Commission’s survey of Chief Executives of regulatory organisations. This survey found that 48% (11 out of 23 respondents) of responding Chief Executives agreed with the statement “Agencies are often too risk averse when enforcing regulations” (26%, or 6 respondents disagreed).

37 For details of these classifications, see Colmar Brunton (2013), available on the Commission’s website.
Importantly, there will be many situations where a risk-averse approach is appropriate for achieving the objectives of regulation – for example, where non-compliance would lead to a loss of life or wide scale, irreversible environmental damage. The important issue is whether a risk-averse culture is the appropriate and efficient response to the nature of the harm being managed, or whether the culture has emerged to protect the reputation of the organisation (at the expense of achieving the intent of the regulation).

The importance of appropriate risk-taking was highlighted in the Better Public Service Advisory Group Report:

Our current and future public management challenges will require a greater onus on citizen voice, innovation and calculated risk-taking – not just because these cultural dimensions are valuable in their own right, but because they will be the only way to achieve improved results for New Zealanders while attaining year-on-year efficiency and effectiveness improvements. Chief executives, and their Ministers, will have to be able to effectively manage risk and distinguish those low-risk environments from areas where a willingness to provide “room to fail” is critical to fostering a culture of innovation. (SSC, 2011, p. 51)

There is evidence of a risk-averse culture within some New Zealand regulators. It is important to understand whether this culture has emerged as an appropriate and efficient response to the nature of the harm being managed or as a means of protecting the reputation of the regulatory body (or its employees).

Adopting new approaches to compliance often requires cultural shifts

Adopting new approaches to monitoring and enforcement can result in tension between the cultures of “traditional” enforcement staff and organisational leaders. This tension arises because of deeply held assumptions around what is required to manage a given risk. For example, inspectors who believe that “successful regulators” monitor all regulated parties equally may find it hard to adjust to an approach based on monitoring high-risk parties only.

A number of submissions highlighted the need to manage this culture change. For example, the Meat Industry Association notes:

The MIA supports the VADE (voluntary, assisted, directed, enforced) model of regulatory compliance. The industry has very powerful incentives for voluntary compliance … so the most appropriate compliance measures from regulatory agencies should be engagement with industry, clearly articulated risks and outcomes, and performance reporting to companies. In some cases, this means the cultures
and behaviours of regulatory agencies have had to change from a rigid inspection and zero-tolerance enforcement approach. The MIA applauds Verification Services in MPI for their ongoing efforts to create a culture of working with and alongside processors, rather than take a rigid inspectorial approach. (Meat Industry Association of New Zealand, sub. 40, p. 9)

The Civil Aviation Authority states:

The CAA is moving from being a technocratic organisation to being much more a risk-focused regulator. That has required a culture change internally which, while retaining the strengths of the technocratic approach, utilises a much more risk-based approach to its role. This requires the CAA to focus on which risks are to be targeted rather than which technical problem is to be addressed. The change in operating mode also requires questions of internal resourcing and priority setting to be addressed. (Civil Aviation Authority, sub. 6, p. 65)

The experiences of the Ministry for Primary Industries (MPI)’s Verification Services and the Civil Aviation Authority suggest that some regulators have had success in managing the cultural impacts of a shift from traditional to new approaches to monitoring and enforcement. There are likely to be lessons from these exercises that could be shared with other regulatory agencies looking to adopt similar changes to the way they operate.

**Professional subcultures have positive and negative impacts**

Regulators often rely extensively on having a large number of technical staff to carry out specialist regulatory functions. Professions bring with them ways of thinking about problems, and value sets for deciding what the “right” thing to do is. Regulators often draw staff from a limited number of professional backgrounds – be they engineers, scientists, lawyers, economists, or public health specialists.

Having staff with common professional backgrounds can have a hugely positive influence on the performance of a regulator where the culture of the profession strongly aligns with the objectives of the organisation. Under such circumstances, common backgrounds can help develop mutual (unspoken) expectations around the level of quality and professionalism that is demanded of staff. For example, a 2011 performance review of Statistics New Zealand noted:

> Statistics NZ has a strong set of professional values embedded in its DNA. The traditional professional values were clear in all contacts throughout the organisation. These are statistical excellence, integrity, confidentiality and data security. (Performance Improvement Framework Report on Statistics New Zealand, 2011, p. 29)

However, homogeneity in the professional backgrounds can have a down side. For example, the more homogenous regulatory staff are, the more likely it is that the views of that profession will be privileged over others, and that other legitimate options or ideas will be passed over. In this way, strong professional cultures can work against adopting new ideas and practices.

Mighty River Power raised this issue in its submission:

> Regulatory staff working in the electricity sector tend to have backgrounds in economics or engineering, particularly in the economic regulation of network businesses. … This can lead to a reliance on quantitative assessment methodologies and economic theory rather than consideration of more qualitative impacts which are more uncertain. For example, what the longer term dynamic response will be from market participants to the proposed reform or how the electricity market reform plays out in the real world where New Zealand’s geography, generation mix and small dispersed population pose significant challenges that are arguably not duplicated elsewhere in the world. (sub. 30, p. 13)

The existence of a dominant occupational culture may also affect the relationship and interface between the regulator and regulated parties. Where a regulator has a particularly strong professional culture, tensions may arise when engaging with parties that share a completely different set of underlying assumptions. For example, it is common to hear regulated parties accuse regulators of not understanding the “commercial realities” of their industry.

Further, the CCCP notes that the need for regulators to have staff with industry experience creates the potential for “certain professional or industry cultures [to] ‘clash’ with state sector values and cultures”
(CCCP, sub. 12, p. 10). If not adequately managed, this clash of cultures can impair internal communication and delay action, raising the risk of systemic problems in regulatory regimes going unnoticed until major regulatory failures occur.

The likelihood that systemic failures in regulatory regimes will go unchecked is higher when regulators have poor internal communication, lack the ability to learn from experience and have professional subcultures that are resistant to change.

**Cultural implications of changing the functions of a regulator**

The culture (and subcultures) of regulatory agencies are heavily influenced by shared experiences of success. These successes give rise to a common set of assumptions about how success is achieved. The assumptions are in turn passed on to new members of the organisation as the “the way things are done around here”.

Yet as discussed in Chapter 5, government agencies can be subject to relatively frequent shifts in their structure, roles and functions. Restructures are often accompanied by changes in operating procedures, management approaches or accountability arrangements. Such changes can be met with resistance where they challenge existing ways of doing things. As Schein explains,

> any challenge or questioning of a basic assumption will release anxiety and defensiveness. In this sense, the shared basic assumptions that make up the culture of a group can be thought of, both at the individual and group level as psychological cognitive defence mechanisms that permit the group to continue to function. At the same time, culture at this level provides its members with a sense of identity and identifies the values that provide self-esteem. ... Recognising these critical factors make us aware why “changing culture” is so anxiety provoking. (p. 29)

In such situations, elements of the “new” culture that are consistent with the pre-existing culture will likely be adopted. Tasks, approaches or methodologies that run counter to the existing culture will be met with resistance. This can become problematic if the approaches needed to be “successful” in achieving the new functions are not consistent with the existing culture.

For example, a regulator whose organisational culture has emerged around policing “bright line” rules may not have developed a culture that is consistent with new functions that require a greater level of discretion and collaboration/cooperation with regulated parties. Here it is important to separate capability from culture. While the agency may be able to hire people with the required skills, these people may be constrained in their effectiveness if their new ways of operating run counter to the established way of doing things.

Evidence suggests that in the past entities and individuals have not fully understood such cultural impacts prior to changing the function or structure of regulatory agencies. For example, box 7.1 highlights that the changes required when New Zealand Transport Agency (NZTA) was created were “more significant than [was] initially apparent” (SSC, New Zealand Treasury & DPMC, 2011a, p.26).

The example of NZTA highlights a number of important points.

- Even with targeted measures, subcultures can be difficult to change.
- Organisations working in seemingly similar areas can develop very different cultures.
- Geography can play a strong role in forming and, importantly, maintaining subcultures.
- When new organisations are created, elements of each subculture are likely to be valuable to the new organisation – so are worth retaining.

38 Rules in which the distinction between compliance and non-compliance is clear.
Engagement is the “face” of regulator culture

It is clear from submissions to the inquiry (and the Commission’s engagement meetings) that many inquiry participants feel that regulator culture is strongly linked to the way it approaches consultation. For example, the IPENZ notes:

“The organisation’s culture can be evident (or not) from the type and extent of stakeholder engagement mechanism used in the design of regulation. The engagement process should be inclusive, collaborative, be prepared to listen, and ensure appropriate expertise is used in the deliberations on the input. (sub. 21, p. 11)"

Similarly, the New Zealand Bankers Association notes:

“An example to consider is the Reserve Bank. Its need for independence in regards to monetary policy is without question. However, there is a sense that this culture of independence also influences the way that the Reserve Bank has approached prudential policy and its role as a regulator. This has perhaps understandably resulted in a culture where at times the regulator appears reluctant to engage with the banking industry. (New Zealand Bankers Association, sub. 43, p. 8)"

There is little doubt that culture can influence how a regulator engages with stakeholders. Even so, it is important to ask whether a perceived lack of engagement is driven by the regulator’s deeply held values, or whether it is driven by some other factor – such as the legislative environment, time constraints, resourcing requirements, the level of information that the regulator already has, and so on. As such, engagement is as much about good process and institutional design as it is about the culture of a regulator.

That said, regulators should be aware of the strong public perceptions of engagement as a “window” to the culture of an organisation. The topic of engagement is examined in Chapter 8.
Corporate missions and frontline staff

A common understanding of the purpose and mission of a group is a key step in developing a common culture. The mission of an organisation provides a shared sense of direction for staff and an aspirational goal against which success and failure can be measured. Developing this shared sense of purpose is widely accepted to be a key role of leaders within regulatory agencies. For example, the Commission’s survey of Chief Executives found that 91% (21 out of 23 respondents) agreed that the senior leadership team in an organisation drives corporate culture. Chief Executives also agreed that culture affects frontline staff, with 91% (21 out of 23 respondents) agreeing that corporate culture and values influence how frontline staff operate.

A different story emerges from the PSA survey. Results of this survey indicated that, on average, regulatory workers do not perceive that top managers communicate a clear organisational mission. However, the survey also illustrated that when workers did perceive that their managers clearly communicated the organisational mission, they were more likely to feel emotionally attached to the organisation, be more loyal to the organisation, and be more committed to the organisation.

7.8 Shaping the culture of a new regulator

The Commission has been asked to provide guidance that can be used to inform the design and establishment of new regulatory regimes and regulatory institutions. This raises the question of what steps (if any) the government can take to promote an “appropriate” culture within a new regulator.

At this point, it is important to note that within the academic literature:

- there is general agreement around the link between organisational performance and culture;
- there is general agreement around the role that leaders play in establishing the culture of new organisations;39
- there is far less agreement around the extent to which managers can modify a culture that is embedded within an existing organisation.

This section looks at how the government may be able to promote a “desirable” culture within new regulatory agencies. The following Section (7.9) takes a closer look at the debate around whether embedded cultures in existing regulators can be managed and changed.

Selecting the “right” leaders

The (formal and informal) actions of a regulator’s founding leaders will heavily influence its culture. This suggests that governments can “seed” the culture of a new agency by appointing founding leaders who

39 For some empirical studies on the relationship between culture and performance, see Berson and Oreg (2008), Ogbonna and Harris (2000) and Tsui, Wang Xin and Wu (2006).
have values, beliefs and experiences that are consistent with its vision of the “ideal” culture. To do this requires a deep understanding of the type of culture that is most likely to be effective given factors such as:

- the nature of the risk being regulated;
- the pace of change in the technology impacting either the risk or the regulator’s ability to monitor the risk;
- the professional skills needed to administer the regulation;
- the characteristics of the regulated parties; and
- the political environment.

For example, regulation of infectious diseases may require a regulator that will promote a dynamic, open culture in which issues are quickly communicated through informal channels to enable new risks to be assessed and workshoped. Other forms of regulation, such as border security and customs, may require a regulator to promote a greater level of formality and adherence to structured hierarchies.

Yet the factors shaping culture are many and varied. Selecting the “right people” - even if they can be effectively and accurately described, identified and appointed - does not guarantee that an appropriate culture will emerge. It is the actions of the appointed leaders that are important, not their espoused values.

Table 7.3 provides examples of the mechanisms through which leaders can embed culture into a new organisation.

### Table 7.3 How leaders can embed culture

<table>
<thead>
<tr>
<th>Embedding mechanism</th>
<th>Comment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regularly (and consistently) paying attention to areas they believe are important for success.</td>
<td>Illustrating a strong commitment to performance management of important areas sends clear signals to members of the organisation about the behaviours that leaders see as important. For example, if a leader believes “customer service” is important, they may closely monitor customer satisfaction surveys or complaints from the public.</td>
</tr>
<tr>
<td>Allocating resources in a way that is consistent with the espoused values of the organisation.</td>
<td>If public participation is an aspirational value of the organisation, the leader can ensure that budgets contain adequate provision for this activity.</td>
</tr>
<tr>
<td>Deliberate role modelling, teaching and coaching of desired behaviours.</td>
<td>Founding leaders provide a key source of ideas and behaviour models for new organisations. By being seen to “walk the talk”, a leader can instil confidence that management encourages a given behaviour. This is particularly important in times of organisational crisis when anxiety among staff is high. How leaders behave during such periods can have a profound impact on the culture within the organisation. Related to this is investing in management and leadership training that is in line with the desired values of the organisation.</td>
</tr>
<tr>
<td>Allocating rewards and status to staff that demonstrate behaviour consistent with the desired culture of the organisation.</td>
<td>Leaders can send a strong message to staff by clearly linking reward and punishment to demonstrated behaviour. This is particularly important as “[o]nly by observing actual promotions and performance reviews can newcomers figure out what the underlying assumptions are by which the organisation works” (Schein, 2010, p. 249).</td>
</tr>
<tr>
<td>Organisational systems and procedures.</td>
<td>In addition to providing structure and predictability, systems and procedures can be used to signal areas that a new leader believes are important.</td>
</tr>
</tbody>
</table>
### Embedding mechanism

| Formal statements of organisational values and beliefs. | These statements can help in establishing the aspirational values of a new regulator. However, as O’Farrell (2006) notes, without leadership and action such statements are “simply rhetoric” (p. 8). |


| F7.10 | Government can “seed” the culture of a new regulatory agency by appointing founding leaders who have values, beliefs and experiences that are consistent with its vision of the “ideal” culture. However, selecting the “right people” does not guarantee that the “right” culture will emerge – the actions of founding leaders are the key embedding mechanism. |

| F7.11 | When establishing a new regulator, it is important to have founding leaders in place from the start of the organisation. This will provide the leader with the opportunity to influence the cultural foundations of the organisation. The use of “interim leaders” is to be avoided where possible. |

### Signalling the desirable processes within legislation

Parliament can use legislation to signal the importance of specific actions or behaviours of a regulator. For example, requirements on regulators can convey different levels of importance and compulsion. Phrases such as “the regulator must consider X” or “the regulator should have regard to Y” provide signals of the significance that a regulator should assign to actions or behaviours.

Seen through the lens of cultural analysis, such provisions offer markers against which to measure the “success” of the (formal or informal) organisation. As such, legislative provisions give clues to the types of culture that are conducive to good performance. This is separate from their legal purpose.

Legislative provisions, however, do not guarantee a specific culture will emerge. As noted previously, culture exists outside formal rules and processes. For example, a legislative requirement to consult does not guarantee that an agency will develop deeply held values around the importance of public consultation. On the contrary, if the regulator views consultation as adding cost and delaying decisions (and so hindering performance), then a culture of “going through the motions” of consultation may emerge. Measures aimed at promoting a given culture will therefore likely be undermined unless these measures are consistent with how the success of the organisation will be measured.

Of course, none of this is to say that culture is the only driver of organisational behaviour. Individuals respond to any number of incentives and motivations – many of which are outlined in this inquiry report.

| F7.12 | While legislative provision can codify required actions, they do not guarantee that a regulator will develop deeply held values around the importance of those actions. |

### Demonstrating support for the values of founding leaders

Monitoring bodies and central agencies can influence the culture of new regulators by demonstrating public support for favourable values and behaviours. Just as founding leaders of new organisations embed culture by rewarding and modelling behaviour, leaders of oversight bodies can reinforce favourable values by expressing approval for them.

For example, support for a new regulator’s engagement processes can help to embed a culture of partnership and collaboration. Similarly, public support for the independence of a regulator can help to embed a culture of impartiality.
These informal measures can serve to confirm the assumptions and beliefs of founding leaders. This is particularly important during the early stages of a regulator’s existence when cultural norms are formed. Of course, such measures are imprecise and their impact will be secondary to more powerful embedding mechanisms such as those outlined in Table 7.3.

**F7.13** Monitoring bodies and central agencies can use formal and informal mechanisms to reinforce favourable cultures in new regulatory bodies.

### 7.9 Changing culture of an existing regulator

The previous section looked at what the government can do to promote the development of culture within a new regulatory agency. This sections explores whether culture can be changed and, if so, how.

#### Culture change – the academic debate

There is debate in the academic literature around the extent to which embedded organisational cultures can be changed. Commenting on this debate O’Donnel et al (2008) note:

The literature on culture change … is somewhat ambivalent on this point. On the one hand, examples can be identified where interventions can influence culture. But on the other hand, some academics warn of the danger of attempting to influence the more superficial aspects of culture such as symbols and ceremonies, while ignoring the more pervasive and deep-seated aspects of culture such as values and beliefs. These more deep-seated aspects of culture are much more difficult to influence. (p. ix)

It is possible to distinguish two broad views within the literature on organisational culture. Brewis et al (2012) label these theoretic views as the “has” perspective and the “is” perspective of organisational culture.

The “has” (or mainstream) perspective likens organisational culture to an input into production which, as with any other input, managers can shape and modify. This perspective is popular with management consultants and sees culture as something that is “driven from the top” and disseminated throughout the organisation by senior management. In doing so managers are able to narrow the scope for unfavourable behaviour by narrowing the discretion that employees have over decisions (Jackson and Carter, 2000).

The “has” perspective can be illustrated by the following quote from Peters and Waterman (1982):

All that stuff you have been dismissing for so long as the intractable, irrational, intuitive, informal organisation can be managed. Clearly, it is as much or more to do with the way things work (or don’t) around your companies as the formal structures and strategies do … (p. 11)

An alternative position is presented by proponents of the “is” perspective. This perspective views organisational culture through an anthropological lens (as opposed to a management lens). It argues that culture is something that emerges organically as workers learn to make sense of their work environment. This perspective places greater focus on culture as a product of collective thinking and, as such, is sceptical about the management of culture – particularly the ability to change culture quickly.

The fact experts that are divided about the extent to which culture can be “managed” highlights the importance of promoting the development of an “appropriate” culture from the start of the organisation. It also reaffirms the importance of founding leaders in setting the cultural foundations on which the organisation will operate. Foundations, once established, are hard, if not impossible, to fully remove.

**F7.14** There is disagreement in the academic literature around the extent and pace at which embedded cultures can actually change. This debate reaffirms the importance of promoting an “appropriate” culture from the inception of a regulatory body.
Some principles for effective culture change

Despite the conflicting views among theorists, a considerable amount of literature exists on the topic of change management. This literature typically focuses on three different areas (Anderson and Ackermann-Anderson, 2010):

- *developmental* changes impacting day-to-day operations such as change processes, skills and internal procedures;
- *transitional* changes such as periodic changes to organisational structure or corporate strategies;
- *transformational* changes addressing “big picture” issues that impact the underlying assumptions of an organisation and that tend to be ongoing and adaptive.

The line between these forms of change can be hard to determine. A simple transitional change (such as a change in how regulated parties are monitored) may end up requiring transformational change if the new practice runs counter to the existing assumptions and belief of the workforce.

Lewin’s (1947) influential theory of change places emphasis on diagnosing a system before introducing significant changes. His approach focuses on psychological processes, and advocates that individuals and groups must go through a process of “unlearning” their existing views and beliefs and then “relearning” beliefs that are consistent with the desired change. Lewin refers to this process as “unfreezing, changing and refreezing” (p. 43).

Building on Lewin’s model, Schein (2010) has suggested five principles for managing culture change. These principles are set out below.

- **Principle 1**: Survival anxiety must be greater than learning anxiety. That is, the fear that something bad will happen to the group if they do not change must be greater than the group’s fear of learning new ways of operating.
- **Principle 2**: Leaders should look to motivate change by reducing fear of learning new things, rather than increasing survival anxiety.
- **Principle 3**: The change goal must be clearly defined in terms of the specific operational problem to be fixed (as opposed to the culture problem that must be addressed).
- **Principle 4**: Old cultural elements can be destroyed by removing the people who carry those elements. But new cultural elements can only be learned if the new behaviour leads to success.
- **Principle 5**: Cultural change is always transformative change that requires a period of unlearning and psychological pain.

Katzenbach, Steffen and Kronley (2012) also provide principles for achieving cultural change.40

- **Match strategy and culture**: Executives often underestimate how much the effectiveness of a strategy depends on it aligning with an organisation’s culture. Strategies that run counter to the existing culture are likely to take longer to implement, and cost more, than those that capitalise on current cultural strengths.
- **Focus on a few critical shifts in behaviour**: This requires a good understanding of what behaviours the current culture (positively and negatively) affects, and identifying key areas where cultural changes are likely to have the largest impact on performance.
- **Integrate formal and informal interventions**: While leaders often address the formal change mechanisms (such as reporting lines, decision lines and processes), they often overlook informal mechanisms (such as

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40 For further examples of change principles, see Fernandez and Rainey (2006) and associated references.
networking, ad hoc conversations and peer interactions). These mechanisms can be powerful catalysts for cultural change.

- Honour the strengths of the existing culture: It is highly likely that elements of the existing culture align with the vision for change. Leaders must be aware of these cultural strengths, publicly acknowledge them and use them to achieve the desired organisational change. Change strategies are most effective when “positive” cultural attributes are leveraged against “negative” attributes to achieve the desired behaviour change.

- Measure and monitor cultural evolution: This will allow leaders to identify backsliding and undertake corrective action if needed. Evidence of improvements can also help to reaffirm that the benefits of the change and help to maintain momentum.

The Commission’s analysis of the formation of MPI also provides a number of lessons relevant to a discussion of cultural change. These are set out in Box 7.2.

The above principles highlight the need for public sector leaders to be acutely aware of the psychological factors that both help with and resist change. Reliance on “template” change management solutions (or consultants that use them) is likely to result in a superficial assessment of organisational culture and management strategies that struggle to have lasting impacts on staff behaviour.

Box 7.2   Culture and leadership lessons from the formation of the Ministry for Primary Industries

Expect and plan for having to manage for a range of views
Restructurings and mergers impact on managers/staff and stakeholders in different ways. Staff and stakeholders may perceive them differently given their backgrounds, experience and so on. There is likely to be a range of views on the restructurings that may take some time to change. This should be expected. Ensuring an effective response to such a range of views points to the need to be quite systematic, planned and consistent about change, and to communicate continuously throughout the process.

Having a clear organisational strategy
There are benefits to having a single clear organisational strategy that provides a clear focus. This is an essential step with any major merging or restructuring.

The strategy needs to truly reflect and encapsulate the core purpose(s) of the organisation so as to ensure the management focuses its attention on the right issues. A misaligned strategy can risk diverting senior management attention rather than focusing it. The strategy must reflect, rather than conflict with, the organisation’s legislative or regulatory functions. If it does not, staff will be left trying to resolve the tension between the two functions.

While restructurings and mergers can formally bring functions together, aligning actual thinking and developing deeper relationships can take much longer. Exercises that involve staff in setting the overall organisational strategy and determining its values can prove very helpful for starting to align thinking, build new relationships and make staff feel included in the new organisation. In other words, the way such strategy work is brought together is also important. MPI appears to have received quite positive internal feedback for its strategy and values exercises.

New managers can bring new ideas
New managers can bring refreshing new approaches to some challenging projects and gain traction on them as a result. New managers can bring more open minds and a willingness to try new approaches that existing managers might be less open or willing to try.

Understanding work already under way
That said, new ideas are not always new and are not always better. The key to success seems to be adapting and aligning new thinking with what is going on currently. Changes introduced without a
sufficient understanding of the status quo risk unnecessarily undermining existing change efforts or repeating past mistakes.

These effects risk proving more destructive the more times changes are made (for example, with restructurings). This risks staff cynicism about how long any new initiatives might last, for example. In other words, if managers move quickly to replace existing incomplete projects/initiatives with new ones, they risk sending an implicit message about the longevity of the new ones as well.

This also emphasises the need to ensure new managers are properly inducted into the new organisation. This should involve providing them with sufficient background to truly understand the systems and functions they will be responsible for – particularly before they make any major decisions.
8 Consultation and engagement

Key points

- When implementing regulation, engagement can help to reassure the community that good regulatory process is being followed and that the decisions of regulators are robust, well informed and well reasoned.

- The choice of engagement mechanism should be influenced by the goal of the interaction, and by the relative efficiency of alternative engagement mechanisms. Goals can range from informing stakeholders of their regulatory obligations, to involving them in regulatory decisions, to empowering them to make decisions.

- In general, the greater the level of public participation the more critical it becomes to ensure a common understanding of the goals of the engagement process. Failure to do this can result in unrealistic expectations around the extent to which participants can affect the decisions of regulators.

- When developing engagement strategies, regulators need to examine both the fairness and proficiency of alternative mechanisms. In practice, both the way a mechanism is implemented and the capability of the regulator influence both proficiency and fairness.

- Officials need to consider whether to leave engagement strategies to the discretion of the regulator, or whether statutory provisions are required to promote regulatory objectives of Parliament or protect fundamental principles of natural justice.

  - This decision should be made in the context of other features of the regulatory regime – particularly the extent of discretionary powers the regulator will hold, their level of independence, and the strength of accountability mechanisms.

- Inquiry participants have raised concerns around the current engagement practices of some New Zealand regulators. These include insufficient time for engagement, a perception that regulators enter engagement processes with predetermined views, and concerns that some regulators lack the capacity to engage affectively. The Commission has also heard positive feedback around the approaches adopted by some regulators – notably the New Zealand Transport Agency (NZTA) and the Environmental Protection Authority (EPA).

- Stakeholders also advocated more extensive use of advisory groups and greater involvement of consumers in decision making (for example, through mechanisms such as “constructive engagement” and “negotiated settlements”).

- “Constructive engagement” and “negotiated settlements” can have drawbacks. Stakeholders can lack the expertise, resources or time to engage effectively in technical decisions, it can be hard to ensure that the views of the broader community are represented, and it can generate unrealistic expectations around how much stakeholders can affect the decisions of regulators.

8.1 Introduction

Effective engagement is important for both the design and implementation of regulations. This chapter examines engagement by regulators implementing regulation, and explores how regulators can promote good engagement practices when designing new regulatory regimes. The chapter discusses the views of inquiry participants on current engagement practices; in particular, whether more participatory approaches to engagement are required. The chapter is set out as follows:
why engagement is important (Section 8.2);
the regulatory relationship (Section 8.3);
selecting engagement mechanism (Section 8.4);
consultation and common law principles (Section 8.4);
stakeholder views on current engagement practices (Section 8.6); and
the use of statutory requirements to consult (Section 8.7).

8.2 Why engagement is important

When implementing regulation, effective engagement can help to reassure the community that good regulatory process is being followed, and that the decisions of regulators are robust, well informed and well reasoned. This promotes confidence that the decisions of regulators are in the public interest and that they are evidenced-based and impartial. This in turn helps build trust in both the regulatory system and in the regulator. It also helps strengthen the legitimacy of the regime and improve the durability of regulator decisions.

Conversely, insufficient engagement can weaken community confidence and trust in both the regulatory regime and in the regulator’s ability to deliver sound decisions. Low community confidence can undermine the objectives of regulation by deterring compliance or making the decisions of regulators more likely to be judicially reviewed. The Legislation Advisory Committee (LAC) guidelines highlight the importance of consultation in developing legislation:

A well designed and implemented consultation programme can contribute to higher quality legislation, identification of more effective alternatives, lower administration costs, better compliance, and faster regulatory responses to changing conditions. Just as important, consultation can improve the credibility and legitimacy of Government action, win the support of groups involved in the decision process, and increase acceptance by those affected. (LAC, 2012, pp. 29-30)

At a more fundamental level, common law principles highlight that consultation is not only important for efficient design and implementation of regulations, but also for protecting the right of New Zealanders to natural justice.
8.3 The regulatory relationship

Regulators undertake a number of activities that involve interacting with regulated parties and the wider community. These range from passive interactions (such as the provision of information on a website) to more active forms of interaction (such as site inspections and formal consultation processes).

Figure 8.1 Points of interaction between regulators and regulated parties

The nature of the regulation and the characteristics of the regulated population both impact the form and frequency of interaction.

Some regulations, such as the issuing of a vehicle registration, require little interaction between the regulator and a regulated party. These tend to give rise to “distant” regulatory relationships based on formal processes and procedures.

Other forms of regulation require frequent interaction between the regulator and regulated parties. This frequent interaction provides an opportunity for each side to develop an understanding of the reasons that underpin the other side’s position. Frequent interaction also provides a greater potential for interpersonal relationships to develop between key staff and for a positive relationship to evolve between the two parties. Walshe and Boyd (2007) note:

When a positive relationship exists, there is some shared sense of purpose, and mutual recognition of each other’s expertise and contribution; a negative relationship is characterised by a clash of values or ways of working, distrust or even hostility, and adversarial behaviours. (p. 21)

Where regulation focuses on an industry with relatively few firms, it is generally easier for the regulator to identify regulated parties and to develop closer regulatory relationships with them. Conversely, where regulations covers a large number of diverse parties, developing a detailed understanding of each participant is more difficult.

The Commission’s business survey supports this assertion. The survey found that businesses with over 50 employees and businesses with a yearly turnover of more than $10 million were more likely than smaller businesses to agree that regulators listened to their views and considered those views when making decisions.

Comments from the Civil Aviation Authority (CAA) inquiry submission further highlight how the characteristics of the regulated party can influence the interface with regulatory agencies:

A particular issue for the CAA is the dichotomy it faces in consulting its stakeholders. There is a significant difference between consulting the big (almost monopoly players) versus, say, the recreational (i.e., the non-commercial flier), versus the small (often under-capitalised) entities in the sector. The ability to reach out to these various groups, using language that each understands, and
then develop and apply a common set of rules ensures a complicated consultation and regulatory change process. (CAA, sub. 5, p. 52)

Of course, regulators also need to consider their relationship with a broader set of stakeholders, particularly those that benefit from regulation, such as end-users of network utility services and people whose lives are made safer by regulation. The CAA notes this point in its submission:

The relationship a regulator has with its regulated sector is very important, but is only one of a number of relationships with key stakeholders that must be considered. These relationships are dynamic, shifting and developing in terms of importance and form.

The regulator must consider the impact of its compliance decisions on all of its stakeholders, not just the regulated sector it oversees. (CAA, sub. 6, pp. 53-54)

Similarly, the Council of Trade Unions (CTU) notes:

Our emphasis is on representation of those needing protection. We recognise that there can be advantages in consulting the parties being regulated. However, that should not be allowed to give them unbalanced access to or influence over the regulator. This is a difficult task particularly when the regulated parties are large, wealthy, influential and powerful. Great care must be taken to ensure that ‘consultation’ does not in the end mean regulatory capture. (CTU, sub. 25, p. 26)

8.4 Selecting engagement strategy

Engagement can be used to achieve a range of regulatory goals. At its most basic level, it can inform stakeholders of their regulatory obligations, and provide information to help them comply. At the other end of the spectrum, engagement can be a used as a means of collaborating with stakeholders over regulatory decisions (or even empower them to reach the decisions). This range of goals is present in Figure 8.2 and raised in the submission from the CTU:

We would also distinguish between consultation on one hand and involvement or participation on the other. In occupational health and safety, there are well-established international principles in favour of the latter. (sub. 25, p. 25)

Each end of the spectrum implies a significantly different role for the regulator. On the left side (low levels of public participation), the regulator’s role is to make decisions and keep stakeholders informed of the decisions they make. On the right side (high levels of public participation), the role of the regulator is to facilitate public decision making and to implement the decisions of stakeholders.

In general, the greater the level of public participation the more critical it becomes to ensure a common understanding of the goals of the engagement process. Failure to do so can result in unrealistic expectations around how much participants can influence the decisions of regulators. Failing to ensure a common understanding can also undermine confidence in the engagement process and, indeed, confidence in the capability of the regulator. As Rothstein (2007) notes:

Conflicts can arise, for example, if regulators have an instrumental conception of participation as a useful ad hoc resource that can contribute procedural legitimacy to policy processes, but participants conceive of such processes as having a more substantial role in shaping regulatory outcomes and holding regulators to account. (p. 604)
In general, the greater the level of public participation the more critical it becomes that there is a common understanding of the scope for stakeholders to influence regulatory decisions. Failure to do so can undermine public confidence in engagement processes and in the competence of the regulator.

**Efficient and effective engagement**

Regulators have a range of engagement tools at their disposal. A stocktake by Rowe and Frewer (2005) found more than 100 different engagement mechanisms used in the United Kingdom and United States alone.

Regulatory bodies must decide which mechanism (or combination of mechanisms) will be most effective in meeting the specific goal of engagement. As the Regulatory Impact Analysis (RIA) Handbook notes, “good consultation is fit for purpose and tailored to both the nature and magnitude of the proposals, and the needs of stakeholders” (New Zealand Treasury, 2013b, p. 32).

The “effectiveness” of a mechanism consists of two dimensions:

1. **Fairness**: Fairness is the ability of the mechanism to meet society’s expectations of transparency, representativeness, and equity. This dimension of effectiveness is inherently linked to principles of natural justice (discussed further below).

2. **Proficiency**: Proficiency is the ability of the mechanism to achieve the specific engagement goal of the regulator. A key element of proficiency is whether the mechanism will collect and transfer the required information with minimum distortion or reduction in accuracy.

Importantly, the proficiency of a mechanism is situation specific. A mechanism that is proficient in collecting information from one group of stakeholders may be inadequate for collecting information from another. For example, an online survey may not be appropriate for groups with low internet access, or a neighbourhood meeting may not be suitable in sparsely populated areas where attendance would require travelling long distances.

This means regulatory bodies need to consider not only the appropriate tool to match the goal, but the appropriate tool to match the characteristics of the group being consulted. For example, Box 8.2 provides some insights on communicating with small businesses on regulatory issues.
In practice, the way the mechanism is implemented influences proficiency and fairness. A seemingly fair mechanism can be implemented unfairly. For example, questions in a stakeholder survey may have an inherent bias. Similarly, if poorly implemented, a mechanism that initially seemed the most proficient at collecting information may turn out to provide inaccurate or misleading information.

How well the mechanism is implemented is innately linked to the capability of the regulatory body. Capability issues are explored further in Chapter 12.

In addition to effectiveness, regulatory bodies must also consider the efficiency of a mechanism. Efficiency is the ability of the mechanism to deliver the required information in a cost-competitive manner when compared with alternative mechanisms (Rowe & Frewer, 2000). Again, the way a mechanism is implemented will significantly impact on how efficient a mechanism actually is.

When developing engagement strategies, regulators need to examine both the fairness and proficiency of alternative mechanisms. Both proficiency and fairness are influenced by the manner in which mechanisms are implemented.

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**Box 8.2  Regulator communication with small business**

A recent inquiry by the Australian Productivity Commission (APC) into regulatory engagement with small business makes a number of observations relevant to this report. These include:

- the time spent by businesses understanding regulations can be substantially reduced, and the likelihood of regulators’ activities delivering good outcomes increased, when regulator communication is effective, and advice and guidance are accessible;
- given the growing number and range of regulations that businesses need to be aware of, a premium should be placed on brevity and clarity;
- small businesses are much more likely than large businesses to rely on third parties, including industry and professional associations and intermediaries such as tax agents, to receive information on regulatory requirements (leading practice regulators are reflecting this in their communication strategies);
- regulators should provide ready access to advice and guidance via a multi-channel strategy, including printed guidance, websites, seminars, help desks and face-to-face interaction;
- websites tend to be the first line of communication with business and third parties – if well set out and maintained, comprehensive and easy to navigate, websites can be particularly helpful to small businesses, many of which undertake compliance activity outside business hours;
- regulators should tailor their delivery approach to reflect the diversity of small businesses – such as those that are regionally dispersed or have a high proportion of owners from non-English speaking backgrounds – subject to an assessment of the costs and benefits; and
- effective complaints handling and grievance processes – which have a degree of independence from the enforcement activities of the regulator – build business confidence in regulatory arrangements and promote better regulatory outcomes.

*Source: APC, 2013a, p. 141.*

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**Pros and cons of different approaches**

The wide variety of engagement mechanisms makes it impossible to review every one. This section groups engagement mechanisms into four broad approaches (Decker, 2013). These are consult-and-respond, advisory committees and panels, stakeholder dialogue, and negotiated agreement.
Consult-and-respond approaches
This group captures a broad range of mechanisms perhaps described as the “traditional” approaches to engagement. These approaches give stakeholders the opportunity to respond to engagement documents and issues raised by the regulator, with the regulator making the final decision.

Consult-and-respond approaches have the advantage that all interested parties can participate. They therefore canvass opinions from a wide range of perspectives. This can help regulators get the “full picture”, rather than just the collective views of specific interests. Consult-and-respond approaches also tend to be relatively easy and inexpensive to implement.

On the down side, consult-and-respond mechanisms may be less effective in dealing with issues that are highly technical or that require specialist knowledge. In such situations, reliance on consult-and-respond approaches can result in large, well-resourced stakeholders dominating consultation processes. In addition, participants involved in consult-and-respond processes may find it hard to see the impact they are having on decisions, leading to disenchantment with the process.

Advisory committees and panels
Advisory approaches commonly involve groups of experts and/or stakeholder representatives who are brought together to advise the regulator on decisions. They can be established by statute or on the initiative of the regulator. Again, the regulator makes the final decision.

The advantage of advisory committees over normal consult-and-respond approaches is that they allow for experts from outside the regulator to provide input into regulatory decisions. They can also provide an avenue for non-expert stakeholders to gain a fuller understanding of the issues and so enable them to represent the views of the wider community more effectively.

Yet it can be hard to ensure that the panel or committee is sufficiently representative of all stakeholders. For instance, it can be unclear whether “institutionalised” advocacy bodies represent the needs of all stakeholders or only certain types of stakeholders. Further, it can be hard to find participants with the requisite skills to contribute to complex decisions.

Stakeholder dialogue approaches
In recent years, approaches that promote dialogue between regulated parties, consumers and other stakeholders have become more popular. These approaches are based on the idea that complex regulatory problems are often best addressed by encouraging stakeholders to develop a mutual understanding of each other’s views, opinions and preferences.

Two such approaches are constructive engagement and consumer challenge panels – most commonly used in the regulation of network utilities. Broadly speaking, these mechanisms involve regulators requiring regulated parties to consult formally with consumers/stakeholders on aspects of their operation. The aim of the consultation is to agree on regulatory solutions that reflect both the views of the regulated company and the preferences of their customers or wider stakeholders. These solutions are presented to the regulator to consider when making its determinations. The key difference between these mechanisms and that of negotiated agreements (discussed below) is that decision rights remain with the regulator.

These mechanisms encourage regulated parties to build relationships with stakeholders and, in doing so, develop a deeper understanding of their preferences and willingness to pay for different activities. They can also remove misunderstandings that act as a barrier to mutually agreeable outcomes. This was a key lesson from the Land and Water Forum (LWF), whose chair (Alastair Bisley) has noted:

That is the essential (though not the only) thing to understand about collaboration. You talk to the people you disagree with. Not just once, but again and again … And if you do listen carefully to what they say, you may come to realise that they are not the idiots that you thought they were! You may even stop entirely believing your own propaganda! And if these things do happen, your creative juices can start flowing, and you can begin to find common ground, and to come up with answers … (Bisley, 2013)
Yet (as can be the case with advisory bodies) stakeholders can lack the technical expertise to engage effectively in some regulatory decisions. This can result in questions around the fairness of the process, and concerns around whether all interests are adequately represented. These approaches can also be costly for regulators to oversee and for consumers to participate in.

**Negotiated agreements**

Negotiated agreements may be applied in a broad range of regulatory situations - from setting access prices for natural monopolies to establishing environmental planning provisions in local plans. Broadly, the approach involves regulated parties and relevant stakeholders negotiating aspects of regulatory compliance. If an agreement is reached the regulator approves the outcomes of the process, avoiding the need to go through the full regulatory procedure.

When negotiated settlements are used, the role of the regulator fundamentally changes from decision maker to overseer of the negotiating process and facilitator of an agreement. That is, the regulator transfers some aspects of decision making to the parties participating in the agreement. The LWF has advocated such a process (Box 8.3).

### Box 8.3  Land and Water Forum

The LWF is made up from representatives from a range of industry groups, electricity generators, environmental and recreational non-governmental organisations, iwi, scientists, and other organisations with a stake in freshwater and land management. Central and local government observers attend the LWF. The LWF’s role is to develop a common direction for freshwater management and provide advice to the Government.

Since 2009, the LWF has conducted stakeholder-led collaborative processes to consider reform of New Zealand’s freshwater management system. It has produced three reports identifying outcomes and goals for freshwater management and making recommendations on the methods, tools, and governance processes required for setting and managing limits on water quality and quantity. It has also undertaken public engagement on its recommendations.

In its second report, the LWF recommended the implementation of collaborative processes for setting freshwater objectives and limits at a regional level through regional policy statements and related plans made under the Resource Management Act 1991 (RMA). It also recommended changes to how national instruments are developed.

The LWF proposed that regional councils be able (after appropriate engagement with their respective communities) to elect to follow a collaborative process in policy and plan making. A collaborative stakeholder group would work together with the council and community to develop freshwater policy or plan provisions, consider public submissions, and commission independent evaluations. The LWF also recommended a collaborative process, at the national level, for developing freshwater-related National Policy Statements and National Environmental Standards.

**The Government’s response**

In March 2013 the Government released a paper “Freshwater Reform 2013 and Beyond”. It stated that the RMA will be amended to provide a collaborative planning process that councils may choose when preparing, changing, and reviewing freshwater policy statements and plans. Councils will have a choice whether to use the existing process or the proposed new collaborative planning model.

In August 2013, the Minister for the Environment, Amy Adams, said, during debate on the third reading of the Resource Management Amendment Bill, that she intended to introduce a further resource management reform bill later that year that would introduce collaborative freshwater planning. (Hansard, 27 August 2013, vol. 693, p. 12851). To date, this bill has not been introduced.

It is important to draw a distinction between *negotiated agreements* on the one hand, and *negotiation of settlements* on the other. *Negotiated agreements* are deliberate, *ex ante* negotiations aimed at achieving a
desired regulator outcome in an efficient, flexible and mutually beneficial manner. *Negotiation of settlements* aims to remedy a regulatory breach in an efficient and cost effective manner, such as once non-compliance has occurred. Negotiation of settlements is discussed in Chapter 11.

Advocates of negotiated agreements argue that the approach increases economic welfare because the parties can reach compromises that may not be available to regulators (for example due to rigid statutory requirements). This can result in efficiency gains, as regulatory outcomes more closely represent stakeholder preferences. Advocates of negotiated agreements also argue that the approach produces more durable and politically acceptable regulatory outcomes.

As with all engagement approaches, negotiated agreements have potential drawbacks. For example, there is a risk that not all relevant views will be adequately represented during negotiations. This can raise questions over the legitimacy of the agreement reached. Negotiations also raise the possibility that groups may have an incentive to do “side deals” that are not in the public interest. Further, concerns over transparency can arise when an agreement is presented as a “package” of measures without presenting the detailed assumptions upon which the agreement was reached. This can create a perception of negotiated agreements being a “black box” (see Littlechild, 2010).

**The use of collaborative processes – issues to consider**

Inquiry participants have expressed the view that better outcomes could be achieved if regulators adopted more collaborative approaches to decision making. In particular, the Commission heard calls for greater use of constructive engagement and negotiated agreements.

The suitability of these engagement mechanisms depends on the specific circumstance under consideration. Based on the lessons from the LWF and overseas, a number of issues are central to the successful use of collaborative approaches. These include the need to:

- understand the extent to which the process is constrained by legal and institutional factors;
- have political commitment to act on the results of the outcomes of collaborative processes;
- understand the information imbalance between regulated companies and consumer representatives;
- ensure that participants are representative of the wider community; and
- have in place clear processes under which the mechanism will operate.

Each of these points is elaborated on below.

**Understand the factors that limit the ability to influence decisions**

The success of any collaborative approach will depend on all parties having a shared understanding of the boundaries of influence of the group. Failure to do so can result in unrealistic expectations about how much the group can impact decisions. This in turn can undermine confidence in the decision-making process.

In practice, the statutory duties of the regulator can limit the scope of potential influence (Ofwat, 2010). Statutory duties allocated by Parliament cannot simply be “passed on” to a third party to execute (unless provision is made in legislation that allows for it). The existence of statutory duties restricts the ability of the regulator to be “flexible” on certain issues, therefore taking potentially agreeable outcomes “off the table”. This limits negotiations to issues where the regulator has discretionary powers.

Owen (2013) comments, in the context of the Australian Energy Regulator (AER), that

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41 For example, the negotiated settlement process overseen by the US Federal Energy Regulatory Commission allows parties to propose “black box settlements” where the rates or revenue are specified, but are not linked to particular assumptions. In these circumstances, each party will make their own preferred assumptions about the parameter values (Littlechild, 2010).

42 For a discussion on experiences with constructive engagement and negotiated settlements, see, for example, Littlechild, 2011, 2012a, 2012b, Decker, 2013, and Owen, 2013.
…there is an important question as to how much influence consumers can have on network costs through the AER price review process, which will depend upon the extent to which the regulator is working within constraints brought about by standards and legal requirements that have already been determined. (p. 25)

Rothstein (2007) made similar observations in his study of participatory approaches in the United Kingdom:

…[T]he substantive contributions of participative processes to policy knowledge are shaped by the design and organization of regulatory regimes. The scope, architecture, and operating rules of regulatory frameworks, for example, structure questions that can be asked, the kinds and standards of evidence that can be considered, and the policy solutions that can be pursued. Information supplied by participative processes, therefore, may get filtered out if it is hard to fit with regulatory requirements, expectations, and remits. (p. 601)

In contrast, Littlechild (2010) notes that, in the United States, the Federal Energy Regulatory Commission (FERC) is required by statute to offer the possibility of settlements.43 Littlechild further notes that under FERC’s regulations “failure of a party to attend a settlement conference will constitute a waiver to all objections to any order or ruling or agreement arising out of it” (p. 8).

**Q8.1**

Are there any examples of legislative rigidity that may prevent regulators from using participatory processes and/or making decisions that would benefit both consumers and regulated parties? What evidence is there of this? What lessons could be learnt from these examples?

**Commitment to implement outcomes of collaborative processes**

Collaborative approaches commonly involve a significant commitment of a participant’s time and resources. For participants to make this commitment, they must have a reasonable expectation that the regulator will act on any outcomes. The LWF notes:

Participants will not reach a consensus unless they feel that their responsibility to do so is real, inescapable and not constrained. They must feel that the decision-makers will have serious regard for it, and will not allow it to be subverted. Parties to a collaborative process must feel that they have been asked to lead.

**Understanding the information needs and imbalance**

Making informed regulatory decisions commonly requires specialist knowledge of complex areas (such as environmental science, engineering or financial accounting). While some parties to a collaborative process may possess this knowledge, others will not. This creates the possibility that the collaborative processes will result in inefficient or inequitable outcomes.

It is important that this information imbalance is well understood and that steps are taken during the design of collaborative approaches to minimise the extent to which imbalances create inefficiencies in the process.

Three possible ways to minimise any imbalance are technical assistance via an independent body, close supervision of the information provided in the process, and using “expert stakeholders”.

An independent public body can provide technical assistance. For example, in the United States an independent body called the Office of Administrative Litigation (OAL) is charged with representing the public interest in cases involving the price of interstate gas pipeline and electricity transmission. The OAL provides a team of experts to work on settlements (Littlechild, 2010). In a similar way, the LWF was supported by expertise from the National Institute of Water and Atmospheric Research and Landcare Research.

Another way to manage information asymmetries is through the regulator closely supervising the information provided to the process. For example, the regulator can specify the information parties must

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43 For example the Administrative Procedure Act requires that the FERC “shall give all interested parties the opportunity for (1) the submission and consideration of facts, arguments, offers of settlement, or proposals adjustment when time, the nature of the proceedings and the public interest permit”. (Administrative Procedure Act Pub.L. 79-404, 60 Stat. 237, enacted 11 June 1946, as cited in Littlechild, 2010).
supply and the form in which the information is supplied. The regulator can also ensure that the participants have access to technical experts to help them interpret the information. For example, Ofwat has raised the possibility of it requiring companies to provide “evidence of understanding and informed and fruitful discussion on major topics”. (Ofwat, 2010, p. 36)

Finally, it may be possible for the regulator to select “expert stakeholders” who are people drawn from relevant professional fields with expertise in a specific area. These experts take on the role of consumer/stakeholder advocates in negotiated agreements or constructive engagement processes. An example of this approach is the Consumer Challenge Panel recently established by the AER. The panel consists of 13 members with “significant local and international expertise, spanning a range of fields including economic regulation, energy networks and consumer representation” (AER website).

Where expert consumers are used, care must be taken to avoid conflicts of interest – an issue highlighted in Chapter 6 with reference to the difficulties experienced by the Financial Markets Authority (FMA) to reach a quorum of non-conflicted board members.

A low level of stakeholder expertise can also affect the extent to which policy makers view collaborative processes as a legitimate source of information. Commenting on their use in risk regulation, Rothstein (2007) notes:

…risk regulation is often characterized by established networks of scientists, producers, and policy officials within which ideas about legitimate expertise and knowledge are accredited and reproduced (cf. Rothstein et al., 1999). In some cases, information from participative processes may be accorded a lower value by policy makers because participants may simply have less to contribute than other established actors with particular fields of expertise. (p. 604)

Of course, in some regulatory situations key stakeholders will hold significant expertise of their own. For example, the customers of airports and electricity transmission companies, and airlines and electricity retailers, generally have deep market knowledge and access to the specialist technical skills. However, these “customers” are typically not the final consumers of regulated services. Regulators therefore need to be alert to the fact that the interests of the immediate “customers” may not necessary align with the final consumers (who may end up paying for the contents of the agreement).

Select participants that represent the wider interests of the community

For negotiated agreements and constructive engagement processes to be successful, the wider community must view them as legitimate. Perceptions of legitimacy are influenced, among other things, by the extent to which consumer advocates are seen as representative of a broad range of interests.

Eppel (2013) summarised the approach adopted by the LWF:

The LWF took the view that the process needed to have around the table all the people who could effectively say ‘no’. Moreover, Bisley says, you need the person who is going to carry the flag for the organisation they represent and bring the commitment of their organisation with them, which might not always be an easy pathway to agreement when organisations are coming from very different positions, but will ensure [that] if and when a position is reached that the member does speak for the support of their organisation.

To promote a wide exchange of views, some jurisdictions allow interested parties to be admitted as “interveners”. These parties generally participate in discussions on a specific subset of issues of particular interest to them (Littlechild, 2010). More broadly, representation can occur through industry bodies, chambers of commerce and social advocacy groups, where each of these organisations will have different levels of technical knowledge. The process of selecting representatives must be carefully managed to prevent representation being seen as merely token.

The need for good processes

The success of collaborative approaches hinges on having well-thought-out processes. These processes need to be in place from the start of discussions. Overseas experience suggests that these processes should clearly articulate:
• the scope of decisions up for negotiation or discussion;
• the roles, responsibilities and accountabilities of each party involved in the discussion;
• the procedures and timeline for discussions;
• the information that must be exchanged by the parties;
• a mechanism for monitoring the accuracy and quality of the information exchanged;
• the conditions under which the regulator will intervene in the process;
• the processes should agreement not be reached; and
• the regulator’s expectations around the range of interests that should be considered.

8.5 Engagement and common law principles

New Zealand common law, such as case law, contains a number of important legal principles that affect how and when regulators must engage with stakeholders. These principles are part of the rules of natural justice, which the New Zealand Bill of Rights Act 1990 affirms.44

The two main aspects to natural justice are:

1. parties should be given adequate notice and opportunity to be heard; and
2. the decision makers should be disinterested and unbiased.

The application of these principles is highly dependent on the particular context. In general, their application will depend on:

• the nature of the power exercised: for example, the court will apply a higher standard to a decision maker who discharges a judicial function than, say, a decision maker within a business;
• the nature of the interest affected: for example, where a decision may affect liberty, livelihood, or reputation of an individual, higher standards of natural justice are applicable; and
• the severity of the sanction a decision maker may impose: for example, higher standards are likely to apply where a decision may constrain the liberty and livelihood of an individual.

Another relevant principle is the doctrine of “legitimate expectation”. This refers to a situation where the government or public body creates a reasonable expectation that they will behave in a certain way or undertake certain courses of action. A legitimate expectation to consult could arise:

• where a public body has given a promise or assurance to consult (this could be express or implied);
• from statements of intent;
• from a regular practice giving rise to a reasonable implication that a practice will continue; or
• from the creation of machinery for a hearing process.

Further, the principles of natural justice hold that adverse findings must not be made against people without them first being given an opportunity to reply to the alleged wrongdoing.45

New Zealand case law also lays down certain requirements for proper consultation. The courts have stressed as a central theme the genuine possibility for consultation to influence decisions. For example,

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44 The New Zealand Bill of Rights Act 1990 affirms the right to natural justice whenever a decision maker has power to make a determination of an "adjudicative character" over a person’s "rights, obligations, or interests protected or recognised by law" (s. 27(1)).
45 This principle is often referred to by the Latin phrase audi alteram partem ("hear the other side").
McGechan J in the High Court in *Air New Zealand and others v Wellington International Airport Limited and others* (1992) stated:

Consultation must allow sufficient time, and a genuine effort must be made. It is in reality not a charade. The concept is grasped most clearly by an approach in principle. To consult is not merely to tell or present. Nor, at the other extreme is it to agree. Consultation does not necessarily involve negotiation toward an agreement, although the latter not uncommonly can follow, as the tendency in consultation is to seek at least consensus. Consultation is an intermediate situation involving meaningful discussion.

Elaborating on the consultation principles and their application, McGechan goes on to say:

Implicit in the concept is a requirement that the party consulted will be (or will be made) adequately informed so as to be able to make intelligent and useful responses. It is also implicit that the party obliged to consult, while quite entitled to have a working plan already in mind, must keep its mind open and be ready to change and even start afresh. Beyond that, there are no universal requirements as to form. Any manner of oral or written interchange which allows adequate expression and consideration of views will suffice. Nor is there any universal requirement as to duration. In some situations adequate consultation could take place in one telephone call. In other contexts it might require years of formal meetings. Generalities are not helpful.

McGechan J in *West Coast United Council v Prebble* (1988) succinctly explained:

Consultation involves the statement of a proposal not yet fully decided upon, listening to what others have to say, considering their responses and then deciding what will be done.

These common law principles mean that the absence of specific statutory provisions requiring consultation does not necessarily relieve a regulator of its obligation to consult. While the extent of this obligation is context specific, it is important that both regulators and officials designing regulation are aware of these fundamental principles of law when considering their engagement strategies.

New Zealand common law, such as case law, contains a number of important principles that affect how and when regulators have an obligation to consult and what constitutes proper consultation.

### 8.6 Stakeholder views on current engagement practices

Inquiry participants have highlighted a number of concerns around the way engagement is currently undertaken in New Zealand. This section provides a summary of the key themes emerging from participants, namely concerns about:

- the amount of time allowed for consultation;
- the impact of pre-existing views and opinions of regulators;
- the clarity of regulatory options being consulted on;
- the capability of regulators to engage effectively; and
- consultation overload.

The section then discusses stakeholder views on advisory groups.

### Time allowed for consultation

Arguably the most common criticism of current engagement practices is that they provide too little time or opportunity for consultation. For example, the New Zealand Bankers Association (NZBA) notes:

A recent example of this was the Consultation Paper on Housing Capital requirements issued by the Reserve Bank. The paper was released on 26 March and submissions closed on 15 April, giving banks just over three weeks to respond, during a period in which three of the four banks being consulted
would have been working on half yearly reporting. Furthermore, it was one of four papers released in a three-week period, most of which required the same staff members to respond, causing practical difficulties for banks. (NZ Bankers Association, sub. 43, pp. 4-5)

Minter Ellison Rudd Watts expressed similar concerns about the pace of engagement:

The policy making process contains a number of distinct phases, and care needs to be taken not to rush the consultation process by producing an omnibus paper which moves rapidly from “problem definition” to “applicable solutions”, “costs benefit analysis of solutions”, “implementation process”, and “legal drafting”. (Minter Ellison Rudd Watts, sub. 28, p. 43)

And Mighty River Power stated:

The time pressures placed on the Electricity Authority for recent reform have led to pressure to conflate the stages of the traditional regulatory impact assessment process and reduce the role of engagement primarily to a proposal/respond model.

This can be expedient where there is general consensus around problem definition and the need for reform, or where issues are technical in nature and largely uncontroversial. But it can have draw backs. For example the introduction of significant revisions to the Transmission Pricing Methodology after some limited consultation with Transpower meant that time and resources had to be devoted by a range of stakeholders to understand the very complex proposals, initially over a relatively short period of time. The Authority has recognised the limitations of this approach and has sought to consult further which we support. (Mighty River Power, sub. 30, p. 13)

In contrast, Federated Farmers praised NZTA for their engagement during the development of transport rules:

The Federation was satisfied with the way in which both the Ministry and NZTA consulted with it while developing the new rules [for the use of agricultural vehicles on-road]. We were consulted throughout the development period and were given a heads up on regulatory decisions before they were made. Officials from the Ministry and NZTA were always willing to listen to our suggestions even…when they did not agree and we always felt we understood the reasons things couldn’t be done as we wished…

… Importantly, both the Ministry and NZTA have continued to engage with Federated Farmers in a positive and constructive way and to show this is not a “flash in the pan”, officials have taken a similar approach when consulting on the Vehicle Licensing Review. (Federated Farmers, sub. 11, p. 14)

Business NZ and others expressed similar, positive sentiments about the EPA’s approach:

The EPA has taken an open and consultative approach to the development of its regulatory framework and has listened (though not always agreed with) industry views. This conversation, which commenced even before the EEZ [Exclusive Economic Zone] law had been passed, has been viewed extremely positively by industry who feels that they have had the chance to influence the attainment of mutually positive outcomes, rather than the usual sense of regulators simply shedding all of the possible risks they can on to industry. (BusinessNZ, sub. 19, p. 24)

Mighty River Power praised the collaborative approach of the Commerce Commission:

Another example of good practice is provided by the Commerce Commission, which generally takes a collaborative approach to problem definition. When considering its approach to information disclosure for Transpower the Commission held a workshop to get industry participants’ views ahead of formulating its approach. The Commission contacted industry participants directly and actively encouraged workshop attendance. (sub. 30, p. 13)

Pre-existing opinions and beliefs

Engagement can appear to be “policy advocacy” if used to justify a decision that has already been made. If regulated parties believe the regulator has already made up its mind, the engagement process may be seen as disingenuous. On this point, the ANZ submission notes:

If a regulator is to be criticised from time to time, it will typically be for not being sufficiently transparent in its decision-making or for exhibiting confirmation bias – for example, not being willing to alter an initial view in the light of consultation responses. (sub. 24, p. 6)
The NZBA and Genesis Energy questioned the sincerity of some engagement processes:

Regulators frequently appear to view engagement as a ‘box ticking’ exercise rather than a genuine effort to gain feedback, timeframes for the engagement process are often unworkable, and in general consultation practices run counter to the expectations set out in the Government statement on regulation. (NZBA, sub. 43, pp. 4-5)

While engagement with the advisory groups works well, consultation with stakeholders, in our view, needs to be improved. There is an increasing perception that the Authority is unwilling to change its initial position in response to submissions. As a result, the consultation process is seen as formulaic rather than meaningful. (Genesis Energy, sub. 48, p. 14)

**Capability of regulators to engage effectively**

Inquiry participants have highlighted that some regulators appear not to have the technical capability to understand and respond to information they receive during engagement processes. The submission of Insurance Australia Group (IAG) notes:

It is important to note that meaningful stakeholder engagement also relies on a regulator having the capability to translate stakeholder messages and views into considerations that inform regulatory outcomes. Appropriate transparency and accountability mechanisms are also needed to ensure that there are incentives to do so. In this way, many of the core elements of high-quality regulation are interconnected and self-reinforcing, and should be considered in a holistic sense. (IAG, sub. 10, p. 6)

Conversely, the EPA has taken specific steps to develop internal capability to engage with Māori. These steps are discussed in Chapter 9. A broader discussion of regulator capability is provided in Chapter 12.

**Consultation overload**

While some stakeholders lamented the absence of effective engagement, others highlighted the risk of too much engagement slowing down decision making. For example, KLR Investments believes that the level of consultation required under telecommunication regulation has slowed industry development. They also note that consultation often occurs on a matter-by-matter basis as opposed to parallel processes addressing several matters.

Inquiry participants also highlighted the cost of consultation and the fact that the pace of regulatory change can make it hard for companies to “keep up” with numerous processes occurring across a range of government agencies.

**Stakeholder views on existing advisory groups**

In general, inquiry participants supported the use of advisory groups and other collaborative approaches to engagement. Aviation New Zealand notes their value in the exchange of ideas:

We value these [advisory] groups as they enable ideas to be exchanged and better understanding developed. (Aviation NZ, sub. 36, p. 33)

Similarly, the CAA notes the role of advisory groups in improving the regulators’ understanding of the markets they regulate:

An advisory board can add value by exposing the management (and the main board) to new thinking, thereby broadening horizons, improving understanding of the organisation’s markets, risks and future drivers of growth, challenging assumptions and guarding against groupthink. Advisors can directly benefit organisational performance. (Civil Aviation Authority, sub. 6, p. 59)

The CAA also notes the fundamental importance of clearly specifying the remit of any advisory board:

To be effective, an advisory board needs a clear remit. An advisory board can support the board or the CEO by providing expert insight or contacts, but it must be clear where ultimate decision-making authority and collective responsibility lie. The advisory board must have an unambiguous mission and definition, with the structure, background and financial arrangements clear. The commitment must come from an appropriate point in the organisation. (sub. 6, p. 59)
Yet, a number of submitters cautioned the potential for capture:

Advisory boards may work well where broader public consultation is not viable because of technical
(specialist) nature of the material. They will not work well when impartiality is impractical due to
fundamental commercial conflicts. (Transpower, sub. 32, p. 10)

Advisory boards can work well if an appropriate range of people are appointed. However they can be
captured by board members’ individual interests. They have limitations as they only have a limited
number of members, which can mean certain perspectives are not heard until late in process when
consultation is undertaken. (IPENZ, sub. 21, p. 11)

While advisory boards may have a place, they cannot be seen, as they too often have, as substitute for
effective involvement of interested parties in decision making. When they have a marginal influence
they can disillusion people rather than encourage their involvement. We consider that New Zealand has
moved much too far down the path of stripping governance boards of representatives of those
affected. That should be reversed. In addition there should be requirements that where regulations,
codes of practice, compliance strategies and the like are being developed or reviewed, their
involvement is mandatory. (CTU, sub. 21, p. 26)

Other stakeholders raised concerns around the manner in which advisory groups are implemented. Genesis
Energy notes:

The advisory group process works very well when utilised. The Authority appears to fully engage with
the advisory panels, gives appropriate weight to their papers and often adopts their recommendations.
However, in our view the advisory groups are not used often enough, particularly in relation to material
matters. (sub. 47, pp. 8-10)

Both KLR Investments and Aviation New Zealand noted the limited involvement with consumers:

In addition, there is no requirement for the Commerce Commission to use industry advisory groups and
it tends to instruct experts from academia. There are also limited processes for consumer engagement.
(KLR Investments, sub. 18, p. 9)

However there is a limit to which a small industry can engage with multiple advisory boards as we still
have businesses to run. We think good high quality dialogue in terms of communication and
consultation with the industry as opposed to an advisory Board probably works best in this industry.
(Aviation NZ, sub. 36, p. 33)

Inquiry participants have raised concerns around the current engagement practices of
some New Zealand regulators. These include insufficient time for engagement, a
perception that regulators enter engagement with predetermined views and concerns that
some regulators lack the capacity to engage affectively. The Commission has also heard
positive feedback around the approaches adopted by some regulators – notably NZTA
and the EPA.

8.7 The use of statutory requirements to consult

Legal requirements to engage should not be seen as a substitute for regulators adopting good regulatory
practices. Officials need to consider the need for statutory requirements to consult in the context of other
institutional factors that influence the behaviour of regulators. These include the:

- extent to which the regulator has discretionary law making powers (Chapter 6);
- arrangements for decision review (Chapter 10);
- funding arrangements of regulators (Chapter 13)
- transparency of decision-making processes (Chapter 6); and
- strength of performance monitoring and accountability mechanisms (Chapter 14).
Further, officials need to be clear on the relationship between existing common law obligations to consult and any proposed statutory obligations.

**Existing statutory requirements to consult**

The use of statutory requirements to consult is a common feature of New Zealand regulation. Of the more than 50 Acts examined as part of the Commission’s inquiry, over half contain some form of consultation requirement. These requirements varied considerably in terms of:

- the level of prescription around who should be consulted and how consultation should take place; and
- the extent to which consultation with specific groups is discretionary or mandatory.

Figure 8.3 provides a high-level typology of current statutory provisions. The typology highlights four broad categories of provisions.

- **Low-discretion/high-prescription**: These provisions create a clear obligation on regulators to consult (low-discretion) and specify either the party to be consulted or the mechanisms of consultation (high-prescription).
- **High-discretion/high-prescription**: These provisions list specific groups or methods of consultation (high-prescription), but leave the decision on whether to consult to the discretion of the regulator (high-discretion).
- **Low-discretion/low-prescription**: These provisions create a clear obligation on regulators to consult (low-discretion) but do not specify which parties to consult or which mechanisms to use (low-prescription).
- **High-discretion/low-prescription**: These provisions leave the decisions on when and how to consult to the discretion of the regulator.

There appear to be no “hard and fast rules” to when and how consultation provisions are used in legislation. Given the breadth of issues covered by this inquiry, this is to be expected. However, some general observations are possible.

- Low-discretion/high-prescription provisions tend to be used when there are a small number of stakeholders whose views are central to good decisions making. These stakeholder groups tend to have relatively stable membership.
- High-discretion/low-prescription provisions tend to be used to enable the regulator to consult with certain groups, rather than specify that those groups should be consulted.
- Low-discretion/low-prescription clauses tend to be used when consultation is central to the decision, yet the groups to be consulted are variable and therefore hard to predict ex ante.

While these general observations provide some insight into how consultation provisions have been used historically, a far more important question is whether the provisions are fit-for-purpose. The inquiry issues paper raised the topic of consultation requirements. While the Commission received numerous submissions on the way that consultation is undertaken, the adequacy of statutory provisions has not emerged as a major issue. The Commission is therefore interested in receiving stakeholder views on the adequacy of existing statutory requirements to consult.

**Q8.2** Are there examples of consultation provisions that are working well, or alternatively, not as well as they should? What factors contribute to a consultation provisions working well/poorly?
### Figure 8.3 Examples of consultation provisions in New Zealand legislation

<table>
<thead>
<tr>
<th>Low-discretion/high-prescription</th>
<th>High-discretion/high-prescription</th>
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<tbody>
<tr>
<td><strong>Examples:</strong></td>
<td><strong>Examples:</strong></td>
</tr>
<tr>
<td>Civil Aviation Act, s 38 (4): “Fees and charges in respect of the use of any airport operated or managed by an airport authority shall not be prescribed, except on the advice of the Minister given after consultation with that airport authority.”</td>
<td>Reserve Bank of New Zealand Act 1989 s 121A: “A statutory manager may consult a prescribed Australian financial authority about whether an action the statutory manager proposes to take is likely to have a detrimental effect on financial system stability in Australia”.</td>
</tr>
<tr>
<td>Gambling Act 2003, s 318: “Gambling Commission must convene a meeting to consult on proposed integrated gambling strategy and proposed levy rates. The following persons must be requested to attend the meeting…”</td>
<td>The Inspector-General of Intelligence and Security Act 1996 s 12: “The Inspector-General … may consult with the Controller and Auditor-General in relation to any matter with a view to avoiding inquiries being conducted into that matter by both the Inspector-General and the Controller and Auditor-General”.</td>
</tr>
<tr>
<td>Hazardous Substances and New Organisms Act 1996, s 49F: in determining whether to approve or decline an application under s 49D to use agricultural compound or medicine in special emergency, the Environmental Protection Agency must consult, and have particular regard to the views of, the Department of Conservation; and consult and consider the views of any other interested government agency”.</td>
<td>Low-discretion/low-prescription</td>
</tr>
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<td>Example:</td>
<td>Example:</td>
</tr>
<tr>
<td>Telecommunications Act 2001 s 156O: “In deciding whether to take the action referred to in subsection (2)(b)(i), the Commission must consult with interested parties”.</td>
<td>Overseas Investment Act 2005, s 14: the Minister, in considering whether or not to grant consent to an overseas investment transaction, ”may consult with any other person or persons, as the Minister or Ministers think appropriate…”</td>
</tr>
<tr>
<td>Animal Welfare Act 1999 s 41: “Before publishing guidelines under this section or any amendment (other than a minor amendment) to any such guidelines, the Director-General must consult with those persons considered by the Director-General to be representative of the classes of persons having an interest in the guidelines or the amendment”.</td>
<td>Biosecurity Act 1993, s 7A: “Before making a decision under subsection (1), the responsible Minister—… (b) may consult such other persons as the responsible Minister considers are representative of the persons likely to be affected by the eradication attempt”.</td>
</tr>
<tr>
<td>Financial Markets Authority Act 2011 s 69: “The FMA must consult about that request with— (a) the persons or organisations that the FMA considers are able to represent the views of those specified persons who are liable to pay a levy under that section; and (b) any other representatives of persons whom the FMA believes to be significantly affected by a levy.”</td>
<td>Transport Act s 99A: “When approving a programme, the Agency may consult with any persons that the Agency considers appropriate having regard to the nature of the programme and the persons to whom it is targeted”.</td>
</tr>
</tbody>
</table>

**Notes:**
1. Emphasis added by the Productivity Commission.

### Issues to consider when contemplating statutory provisions

This section discusses six questions that can help officials as they consider when (and in which form) statutory consultation provisions to include in the design of legislation. These questions are not a "checklist", but a guide for deeper analysis and thought.

- Absent of the statutory provision being considered, will other institutional arrangements provide adequate incentive for regulators to consult in a manner consistent with the proposed provision?
- Will the regulator be given discretionary law-making powers (that is, where they are empowered to exercise public authority and afforded scope to decide how to exercise that authority in particular circumstances)?
- Do other pieces of legislation provide an obligation to consult in a manner consistent with the proposed provision?
- Are there parties whose interests may otherwise be overlooked if statutory protection is not provided?
- Are there groups whose input is particularly important for achieving the objectives of the regulation?
- What would be the practical impact of the proposed provision on the decision-making processes in terms of cost, speed of decisions, and other aspects?

Each question is discussed below.

**Will other institutional arrangements provide adequate incentive to consult?**

Statutory provisions to consult create an obligation on regulators to undertake certain processes. Failure to undertake these processes makes the regulator’s decisions vulnerable to judicial review.

Consultation is not an end in itself; rather it is a tool that regulators use to achieve a specific goal. Officials therefore need to consider whether the broader institutional environment provides adequate incentives to use this tool efficiently and effectively, or more specifically, in a way that is consistent with efficiently achieving the desired regulatory outcomes. Such incentives arise from:

- transparency and accountability arrangements;
- performance review regimes; and
- the potential for judicial review of decisions.

In light of the incentives that these elements of regulatory design create, officials need to consider whether the potential costs of the statutory provision outweigh the benefits. The costs of the provision may include adding (unnecessarily) operating cost and delays into the system, or drawing the regulator’s resources away from higher-value uses.

**Has the regulator been allocated discretionary law making powers?**

In democratic systems, elected representatives (often ministers) are empowered to weigh up society’s competing objectives and to make decisions that they believe promote the public interest.

Where Parliament has delegated these decisions to a regulator, it is important that the necessary checks and balances are in place to promote transparent, informed and accountable decision making. One way to promote informed decisions, and greater scrutiny of decision making, is through statutory requirements to consult with parties affected by the decision. Conversely, prescriptive regimes that provide few discretionary powers may require fewer obligations on the regulator to consult during implementation (but may require a greater level of engagement during the design of the regulation).

**Does other legislation provide a requirement to consult?**

Often the actions of regulators are bound by multiple pieces of legislation. In considering the use (and extent) of consultation provisions, officials need to be aware of the existing requirements for regulators to consult, and the consistency of these requirements with those being proposed in the new regulatory regime.

One example of a seemingly inconsistent requirement was highlighted in the Commission’s recent work on local government regulation. The Commission found that often local authorities are bound by the Local Government Act 2002 to undertake community consultation on issues over which they have very little discretion. For example, despite the fact that local authorities have little discretion in making some bylaws, there is a blanket requirement that all new bylaws or changes to bylaws go through the Special Consultative Procedure (NZPC, 2013a).

**Are there specific parties whose interests may be overlooked?**

Regulations typically affect a diverse range of stakeholders. In some instances, there may be potential for the interests of certain groups to be overlooked and for important views to go unheard. Such a situation may arise, for example, if the views of well-funded and well-organised stakeholders are given prominence over less-coordinated, poorly resourced interests.

Where failure to consult constitutes a breach of natural justice, stakeholders may have recourse to the
courts. However, judicial processes are typically costly and complex. This may present a barrier to diffuse, poorly resourced parties taking such action. In these circumstances, statutory provisions may be required to promote consideration of the views of these groups.

Is some information critical to avoiding large social losses?
The case for statutory provisions to consult may be stronger when:

- successful implementation of the regulation is dependent upon critical information held by stakeholders; and
- regulatory failure would result in significant and irreversible costs to society.

If these two conditions exist, then the need for statutory certainty may be higher than in normal regulatory circumstances.

What are the practical implications of the proposed provision?
As noted above, statutory provisions vary greatly in terms of their level of prescription and discretion given to regulators. How a provision is structured can have practical implications for how a regulator operates. For example, the details of a provision to consult can affect:

- the cost of decisions and the speed with which they are made (this is particularly relevant in emergency situations where a rapid response to an event is required);
- the weight a regulator gives to the views of specific stakeholders;
- how the regulator allocates its budget (and the budget flexibility the regulator has); and
- the skills and capability that a regulator needs.

It is also worth reiterating that the absence of a statutory provision does not relieve a regulator from their obligation to consult. Common law principles of natural justice are still relevant. Indeed, even when legislation provides a statutory provision, the courts may supplement the provision by reference to common law standards of fairness (Joseph (2007) pp. 957–58). As an English case decided in 1863 famously declared, “the justice of the common law will supply the omission of the legislature”.46

The greater the level of prescription and the clearer the intent of Parliament, the less likely the courts are to supplement the provision. As such, officials need to assess the possibility that changes in the regulatory environment may make the provision ineffective or counterproductive. This could arise, for example, if new stakeholders emerge that a low-discretion/high-prescription provision does not recognise. Such a provision may not only fail to recognise the interests of these stakeholders, but may frustrate the courts’ attempts to rectify the problem.

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46 Cooper v Wandsworth Board of Works (1863).
Statutory consultation requirements are potentially most useful when:

- there is a likelihood that failure to consult would breach natural justice principles – for example regulation involves a significant use of the State’s coercive powers that could impair the civil liberty, livelihood or property rights of individuals;
- regulators have wide discretionary rule-making powers that involve making judgements about what is in the public interest;
- there are social equity reasons for specifying the consultation processes that should be followed for a specific group - for example where the affected group may not have the resources or capacity to effectively participate in a conventional consultation process;
- the affected community holds information on trade-offs and technical issues necessary for the regulator to make sound decisions.
Chapter 9 | The Treaty of Waitangi in regulatory design and practice

9 The Treaty of Waitangi in regulatory design and practice

Key points

- The continuing evolution of the relationship between the Treaty partners, and how the courts interpret the principles of the Treaty, can generate considerable uncertainty for those applying them in regulatory regimes.

- References to Treaty principles can be found in statutes in which Māori have strong iwi and hapū relationships. There does not appear to be a consistent description of the application of Treaty principles in statutes. Statutes with references to Treaty principles often contain regulatory provisions and create obligations on a range of parties that are not the Crown.

- The inclusion of Treaty clauses can be seen as an insurance policy for both Māori and the Crown. A Treaty clause is a legal acknowledgement of Māori interests and rights, and provides a clearer definition of the Crown’s responsibility with respect to those rights (that in the absence of a specific clause might be interpreted more broadly).

- This chapter provides a set of factors that officials should consider in recommending the inclusion of Treaty clauses in statutes that establish regulatory regimes or regulatory agencies.

- There is a question whether an overarching Treaty clause in an appropriate statute (separate from the jurisdiction the Treaty of Waitangi Act 1975 confers on the Waitangi Tribunal to investigate actions inconsistent with Treaty principles) that signals the Crown’s intent with respect to the principles of the Treaty of Waitangi, would improve the operation of regulatory regimes in New Zealand. The Commission is seeking views on this issue.

- Excellence in regulatory practice cannot be legislated for. Good practice in upholding Treaty principles of partnership, mutual respect and good faith depends on senior leadership, good internal policies and processes, and guidance for staff and stakeholders.

- The Commission has reviewed 10 examples from government agencies of guidance on how to apply Treaty principles. The overall quality of guidance material can be improved.

- The assessment framework used in reviewing the guidance material could be used as a tool to help regulatory agencies develop their own guidance about the application of Treaty principles.

- Sharing good regulatory practice is one way to raise the standard of practice among regulators. Lessons from the experience of the Environmental Protection Authority (EPA) have been identified. An important lesson for other regulators is that investing in good relationships to develop trust can pay off in reduced costs and better regulatory decision making.

9.1 Introduction

An important issue in establishing regulatory regimes is ensuring that the principles of the Treaty of Waitangi are appropriately taken into account both in design and in practice. Statutes that have regulatory provisions or confer regulatory powers and responsibilities can also contain references to Treaty principles. However, even where “Treaty clauses” are not present, agents of the Crown are expected to have regard for the principles of the Treaty of Waitangi. The continuing evolution of the relationship between the Treaty partners, and how the courts interpret the principles of the Treaty, can generate considerable uncertainty for those applying Treaty principles in the design and implementation of regulation. This chapter provides some guidance about the use of Treaty clauses in legislation. It provides a set of criteria to help regulatory agencies when developing guidance material about applying Treaty principles in their area of regulation. The chapter illustrates how recognising and respecting “the Crown’s responsibility to take account of the
principles of the Treaty of Waitangi” has influenced the processes and practices of one regulatory agency – the Environmental Protection Authority (EPA). The chapter concludes by summarising the guidance provided.

9.2 A Treaty between the Crown and Māori

The Treaty of Waitangi (Te Tiriti o Waitangi) was signed by representatives of the Crown and various Māori chiefs at Waitangi on 6 February 1840. (Box 9.1)

Box 9.1 The Treaty and its Articles

The Treaty is New Zealand’s key founding document. It is an agreement between the British Crown and over 500 Māori rangatira and was signed in 1840. On the day it was signed, there were versions in English and Māori.

**English text**

HER MAJESTY VICTORIA Queen of the United Kingdom of Great Britain and Ireland regarding with Her Royal Favor the Native Chiefs and Tribes of New Zealand and anxious to protect their just Rights and Property and to secure to them the enjoyment of Peace and Good Order has deemed it necessary in consequence of the great number of Her Majesty’s Subjects who have already settled in New Zealand and the rapid extension of Emigration both from Europe and Australia which is still in progress to constitute and appoint a functionary properly authorised to treat with the Aborigines of New Zealand for the recognition of Her Majesty’s Sovereign authority over the whole or any part of those islands – Her Majesty therefore being desirous to establish a settled form of Civil Government with a view to avert the evil consequences which must result from the absence of the necessary Laws and Institutions alike to the native population and to Her subjects has been graciously pleased to empower and to authorise me William Hobson a Captain in Her Majesty’s Royal Navy Consul and Lieutenant-Governor of such parts of New Zealand as may be or hereafter shall be ceded to her Majesty to invite the confederated and independent Chiefs of New Zealand to concur in the following Articles and Conditions.

**Article the first**

The Chiefs of the Confederation of the United Tribes of New Zealand and the separate and independent Chiefs who have not become members of the Confederation cede to Her Majesty the Queen of England absolutely and without reservation all the rights and powers of Sovereignty which the said Confederation or Individual Chiefs respectively exercise or possess, or may be supposed to exercise or to possess over their respective Territories as the sole sovereigns thereof.

**Article the second**

Her Majesty the Queen of England confirms and guarantees to the Chiefs and Tribes of New Zealand and to the respective families and individuals thereof the full exclusive and undisturbed possession of their Lands and Estates Forests Fisheries and other properties which they may collectively or individually possess so long as it is their wish and desire to retain the same in their possession; but the Chiefs of the United Tribes and the individual Chiefs yield to Her Majesty the exclusive right of Preemption over such lands as the proprietors thereof may be disposed to alienate at such prices as may be agreed upon between the respective Proprietors and persons appointed by Her Majesty to treat with them in that behalf.

**Article the third**

In consideration thereof Her Majesty the Queen of England extends to the Natives of New Zealand Her royal protection and imparts to them all the Rights and Privileges of British Subjects.

(signed) William Hobson, Lieutenant-Governor.

Now therefore We the Chiefs of the Confederation of the United Tribes of New Zealand being
What is the Crown?

The Treaty between the Crown and Māori opens up the question of “what is the Crown?” The answer is not simple. The Law Commission, in its paper *To bind their kings in chains* noted:

… it is a fundamental difficulty that the Crown is a metaphor lacking precise definition. (Law Commission SP6, 2000, p. 10)
It appears to be generally accepted, however, that it is the Executive arm of government (not the Judiciary or the Legislature). Further, while a number of definitions are provided in statute, beyond the Executive it can include departmental officials and government agents who undertake work on the Crown’s behalf. But public entities may not be agents of the Crown (despite having governmental functions) unless controlled by a minister or described by statute to be an agent – for example, universities, hospitals, and regulatory agencies (PCO, 2013).

A recent discussion paper by the Parliamentary Counsel Office notes that there is no standard definition of the Crown in legislation:

“The Crown” means, in its strict legal sense, the Queen in her public capacity as the bearer of governmental rights, powers, privileges and liabilities in New Zealand. The Crown has the legal personality of an individual and is able to own property, to spend money, or to make contracts. The Crown is commonly described as the executive branch of the New Zealand government and may be called the executive, the government, or the administration. (PCO, 2013, p. 23)

The Public Finance Act (1989) says that “the Crown or the Sovereign—

(a) means the Sovereign in right of New Zealand; and

(b) includes all Ministers of the Crown and all departments; but

(c) does not include—

(i) an Office of Parliament; or

(ii) a Crown entity; or

(iii) a State enterprise named in Schedule 1 of the State-Owned Enterprises Act 1986; or

(iv) a Schedule 4 organisation; or

(v) a Schedule 4A company; or

(vi) a mixed ownership model company.”

In its guidance, the State Services Commission (SSC) states that Crown entities are separate from the Crown and “are legal entities in their own right” (SSC, 2008). Similarly, local authorities are also “not the Crown and are therefore not the Treaty partner” (NZPC, 2013a, p. 177).

While a precise definition of the Crown is lacking, it is accepted as being the Executive arm of government.

Role of the courts and the Waitangi Tribunal

Despite being signed in 1840, breaches of the Treaty were not justiciable – capable of being decided by a court – until 1975.

Only customary rights were enforceable at law not Treaty rights *per se*. It is instructive to consider why that was so, not in an attempt to atone in some way for past breaches by the Crown of its obligations, but to understand why there was no effective remedy at law for the breaches.

In fact the reason why the Treaty was not justiciable in the courts can be simply stated. It has long been a principle of the law that the executive branch of government, that is to say the Cabinet and the departments of state, should not be able to make law: law-making is a matter for Parliament alone. Treaties normally involve international relations, and these are the preserve of the executive rather than of the Parliament. Accordingly, any treaty entered into by the executive of New Zealand has never been enforceable in the domestic courts unless and until its terms had statutory recognition. (Graham, 2001)
The Treaty of Waitangi Act was passed in 1975, which established the Waitangi Tribunal to inquire into claims made against the Crown for breaches of Treaty obligations.47 Notably, the Act referred to “the principles of the Treaty of Waitangi” rather than the Treaty itself:

And whereas it is desirable that a Tribunal be established to make recommendations on claims relating to the practical application of the principles of the Treaty and, for that purpose, to determine its meaning and effect and whether certain matters are inconsistent with those principles. (Treaty of Waitangi Act 1975 Preamble)

As Palmer (2001) explains, referencing Treaty principles “indicates it is the spirit and intent of the Treaty which is important, rather than its bare words. This is consistent with the constitutional significance of the Treaty and the broad, open textured reading of such documents” (p. 208).

In 1986 Cabinet agreed that at the policy approval stage for legislation, attention would be drawn to any implications from recognising Treaty principles. Around this time, references to Treaty principles began appearing in statutes. Early examples included the Environment Act (1986), the State-Owned Enterprises Act (1986) and the Conservation Act (1987).

The principles of the Treaty

When Parliament has included “Treaty clauses” in legislation, it has generally preferred to reference the principles of the Treaty rather than the Treaty itself. There are a number of reasons for this.

Principles are better able to cope with the historical nature of the agreement. There was a gap of 135 years between the Treaty being signed and it first being provided with legal status. Had it been a legal document from the time of its signing, it is possible case law built up over those years would have allowed more literal use of the Treaty, but in the absence of that precedence, a principles-based approach seemed sensible. Similarly, principles are better able to cope with change – new issues arise and ways of managing issues evolve. The Treaty relationship itself has evolved and will continue to evolve over time.

There are Māori and English versions of the Treaty. The two versions have a number of important differences. The Waitangi Tribunal has deemed that both versions should be taken into account when interpreting the scope of the Treaty. Principles more easily allow this to be done than a literal interpretation of the words.

Finally, principles should promote a more positive relationship between Māori and the Crown by allowing a focus on the spirit of the law rather than the more limiting and legalistic focus on the letter of the law.

From a constitutional perspective, one of the most important references to Treaty principles is section 9 of the State-Owned Enterprises Act 1986 which provides that “nothing in this Act shall permit the Crown to act in a manner that is inconsistent with the principles of the Treaty of Waitangi”. The courts first considered the nature of Treaty principles in a 1987 case that the New Zealand Māori Council brought against the Attorney-General for violation of section 9 (known as “the Lands case”). In doing so, the courts also rejected a strict interpretation of the Treaty, instead viewing it as a living instrument, capable of adapting to new and changing circumstances.

What are Treaty Principles?

The Courts, Waitangi Tribunal and the Executive have all offered their views on the nature of Treaty principles (Box 9.2).

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47 The Waitangi Tribunal enquires into contemporary and historical grievances. The Treaty of Waitangi Act 1975 established the Tribunal, focusing on action or inaction by the Crown only from the establishment of its Act. In 1985 the Act was amended, allowing the Tribunal to investigate breaches dating back to 1840.
These lists are neither exhaustive nor conclusive. The Courts are an important authoritative source on the meaning of the principles, but have also said that in interpreting the principles weight should be given to the opinions of the Waitangi Tribunal (New Zealand Māori Council v Attorney-General, 1992).

Are there key principles?
The Court of Appeal has stated that the Treaty of Waitangi enacts a relationship akin to a partnership and its central obligation is to act in good faith and work out answers in a spirit of honest cooperation (New Zealand Māori Council v Attorney-General, 1987). The principle of consultation can be regarded as

<table>
<thead>
<tr>
<th>Box 9.2 Treaty principles – three views</th>
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<tr>
<td><strong>The Executive</strong></td>
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<tr>
<td>- The government’s right to govern</td>
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<tr>
<td>- The right of iwi to self-management of their resources</td>
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<td>- Redress for past grievances</td>
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<tr>
<td>- Equality – all New Zealanders are equal before the law</td>
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<tr>
<td>- Reasonable cooperation by both parties.</td>
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<tr>
<td><strong>The Court of Appeal</strong></td>
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<tr>
<td>- A relationship of a fiduciary nature that reflects a partnership imposing the duty to act reasonably, honourably and in good faith</td>
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<tr>
<td>- The government should make informed decisions</td>
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<td>- The Crown should remedy past grievances</td>
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<tr>
<td>- Active protection of Māori interests by the Crown</td>
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<tr>
<td>- The Crown has the right to govern</td>
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<tr>
<td>- Māori retain rangatiratanga over their resources and taonga and have all the rights and privileges of citizenship.</td>
</tr>
<tr>
<td><strong>The Waitangi Tribunal</strong></td>
</tr>
<tr>
<td>- Partnership</td>
</tr>
<tr>
<td>- Fiduciary duties</td>
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<tr>
<td>- Reciprocity – being the cession of Māori sovereignty in exchange for the protection of rangatiratanga, leading to the duty to act reasonably, honourably and in good faith</td>
</tr>
<tr>
<td>- Redress for past grievances</td>
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<td>- Equal status of the Treaty parties</td>
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<tr>
<td>- The Crown cannot evade its obligations by conferring its authority on another body</td>
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<td>- Active protection of Māori interests by the Crown</td>
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<tr>
<td>- Options – the principle of choice</td>
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<td>- The courtesy of early consultation.</td>
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particularly important. Without it, Māori interests and values can be overlooked when developing and implementing legislation. In 1989 the Court of Appeal found that the principle of good faith “must extend to consultation on truly major issues” (New Zealand Māori Council v Attorney-General, 1989). In some circumstances the Crown’s obligations will go beyond consultation to include “active steps to protect Māori interests” (Ngāi Tahu Māori Trust Board v Director-General of Conservation, 1995).

How have the courts viewed the application of the principles?

How the courts have viewed the application of Treaty principles is explained in the 2001 Te Puni Kōkiri publication: A guide to the principles of the Treaty of Waitangi as expressed by the courts and the Waitangi Tribunal.

Where there is a specific reference to Treaty principles in legislation, the courts have assumed what might be described as a “process role”, similar to the role played by the courts in administrative law. In the event of a breach, the courts will likely issue a declaration that the proposed decision or action should be delayed so a process can be established that is designed to respect the relevant Māori interest or right. The Crown must then decide on appropriate policy in accordance with relevant legislation and, preferably, in consultation with Māori. Importantly, references to Treaty principles in legislation are to be interpreted in a way that is consistent with the purpose of the relevant Act (ibid).

The general presumption is that Parliament will legislate in accordance with the principles of the Treaty and will appropriately apply the principles on issues of relevance to Māori (Legislation Advisory Committee, 2012). This means the courts can, depending on the context, require that an agent of the Crown have regard to the principles of the Treaty, even if there is no specific Treaty clause (Attorney-General v New Zealand Māori Council, 1991). However, the scope and strength of these “statutory interpretation rights” are minimal, being taken into account only if there is ambiguity in how the law is to be applied in a given situation. If the provisions of the statute are not inconsistent with Treaty principles, but more than one interpretation is possible, then in the process of determining what Parliament intended, the courts will endeavour to interpret statutes in a manner consistent with the Treaty. This is similar to how the courts might take into account any number of factors external to the legislation, including the social, economic and environmental context, other statutes such as the Bill of Rights Act (1990), documents created during the legislation’s inception, and the common law (ibid).

Additionally, the Waitangi Tribunal’s view of how Treaty principles have been applied is important. Unlike the courts, the Tribunal has a much wider mandate to consider any breach by the Crown and its agents. While it does not have decision making functions with respect to its findings, its recommendations carry considerable authority with the courts.

For these reasons, those involved in the design of regulatory regimes and those implementing them should understand how their actions or inactions are consistent with Treaty principles. However, it must be acknowledged that the continuing evolution of the relationship between the Treaty partners, and how the principles of the Treaty are interpreted by the courts, can generate considerable uncertainty for those applying Treaty principles when designing and implementing regulation.

Those involved in designing and implementing regulatory regimes should understand how their actions or inactions are consistent with Treaty principles.

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48 All proposals to introduce a new bill to Parliament must clearly specify whether the regulation would comply with the principles of the Treaty of Waitangi, and to identify any variances (Cabinet Office, 2008). Similar requirements apply to proposed new Orders in Council (Cabinet Office, n.d). Disclosure Statements for government legislation must state “what steps have been taken to determine whether the policy to be given effect by the bill is consistent with the principles of the Treaty of Waitangi” (New Zealand Treasury, 2013a). There is also an expectation that Māori will be consulted appropriately where legislation affects their rights and interests as protected by Article 2, especially as some of these have been recognised at common law. The mandate of the Waitangi Tribunal is also significant.

49 Parliament retains the right to pass legislation that conflicts with the Treaty or which impairs or extinguishes customary rights. However, the general presumption that Parliament will legislate in accordance with the principles of the Treaty means that any legislative action which conflicts with the Treaty or customary rights must use “precise wording to achieve this end” (LAC, 2012).
F9.3 The courts interpret references to Treaty principles in legislation in a way that is consistent with the purpose of the relevant Act. In the event of a breach, the courts will likely issue a declaration that the proposed decision or action should be delayed so as to establish a process to respect the relevant Māori interest or right.

F9.4 That Parliament will legislate in accordance with the principles of the Treaty, and will appropriately apply the principles on issues of relevance to Māori, means the courts can, depending on the context, require that an agent of the Crown have regard to the principles of the Treaty, even if there is no specific Treaty clause. The scope and strength of these “statutory interpretation rights” are, however, minimal. The court only takes them into account if the law to be applied in a given situation is ambiguous.

F9.5 The Waitangi Tribunal has a wide mandate to consider any breach by the Crown and its agents. While it does not have decision-making functions with respect to its findings, its opinions carry considerable weight with the courts.

9.3 Treaty clauses in legislation that establish regulatory regimes

This section examines the characteristics of the statutes that contain references to the Treaty of Waitangi or Treaty principles. It discusses the incentives to include Treaty clauses as a means of ensuring that the principles of the Treaty of Waitangi are taken into account when implementing regulatory regimes, and some of the strengths and weaknesses of doing so. In this context, the chapter provides guidance about including references to the Treaty of Waitangi in legislation that establishes regulatory regimes or new regulators.

Treaty clauses in statutes

The Commission has identified 36 Principal Acts with references to the Treaty or Treaty principles. (Table 9.1)

Table 9.1 Primary legislation that references the Treaty of Waitangi

<table>
<thead>
<tr>
<th>Statute</th>
<th>Treaty reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Auckland War Memorial Museum Act 1996</td>
<td>“The duties, functions, and powers of the Board shall be… to observe and encourage the spirit of partnership and goodwill envisaged by the Treaty of Waitangi, the implications of mana Māori and elements in the care of Māori cultural property which only Māori can provide”.</td>
</tr>
<tr>
<td>Climate Change Response Act 2002</td>
<td>“In order to recognise and respect the Crown’s responsibility to give effect to the principles of the Treaty of Waitangi …” Māori are to be consulted prior to a number of specified decisions being taken.</td>
</tr>
<tr>
<td>Conservation Act 1987</td>
<td>“This Act shall so be interpreted and administered as to give effect to the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Crown Minerals Act 1991</td>
<td>“All persons exercising functions and powers under this Act shall have regard to the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Crown Pastoral Land Act 1998</td>
<td>“In acting under this Part, the Commissioner [of Crown Lands] must (to the extent that those matters are applicable) take into account … the principles of the Treaty of Waitangi”.</td>
</tr>
</tbody>
</table>

50 The table does not include Treaty Settlement Acts or references to Waitangi Day.
<table>
<thead>
<tr>
<th>Statute</th>
<th>Treaty reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education Act 1989</td>
<td>“It is the duty of the council of an institution, in the performance of its functions and the exercise of its powers … to acknowledge the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Employment Relations Act 2000</td>
<td>“The parties must recognise and support Part 3 of the New Zealand Public Health and Disability Act 2000 which, in order to recognise the principles of the Treaty of Waitangi and with a view to improving health outcomes for Māori, provides mechanisms to enable Māori to contribute to decision-making on, and to participate in the delivery of, health and disability services”.</td>
</tr>
<tr>
<td>Energy Efficiency and Conservation Act 2000</td>
<td>“In achieving the purpose of this Act, all persons exercising responsibilities, powers, or functions under it must take into account … the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Environment Act 1986</td>
<td>“An Act to … ensure that, in the management of natural and physical resources, full and balanced account is taken of … the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Environmental Protection Authority Act 2011</td>
<td>“In order to recognise and respect the Crown’s responsibility to take appropriate account of the principles of the Treaty of Waitangi …” the act provides for, among other things, the establishment of a Māori Advisory Committee.</td>
</tr>
<tr>
<td>Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012</td>
<td>“In order to recognise and respect the Crown’s responsibility to give effect to the principles of the Treaty of Waitangi for the purposes of this Act …” a number of sections provide for Māori consultation, recognition and notification.</td>
</tr>
<tr>
<td>Fisheries Act 1996</td>
<td>“The object of sections 175 to 185 is to make, in relation to areas of New Zealand fisheries waters (being estuarine or littoral coastal waters) that have customarily been of special significance to any iwi or hapū … [through] better provision for the recognition of rangatiratanga and of the right secured in relation to fisheries by Article II of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Hauraki Gulf Marine Park Act 2000</td>
<td>“Subject to subsections (2) and (4), the provisions of Part 3 relating to the Park must be so interpreted and administered as to give effect to the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Hazardous Substances and New Organisms Act 1996</td>
<td>“All persons exercising powers and functions under this Act shall take into account the principles of the Treaty of Waitangi”.</td>
</tr>
<tr>
<td>Historic Places Act 1993</td>
<td>“This Act must continue to be interpreted and administered to give effect to the principles of the Treaty of Waitangi, unless the context otherwise requires”.</td>
</tr>
<tr>
<td>Human Rights Act 1993</td>
<td>“The Commission has … the following functions … to promote by research, education, and discussion a better understanding of the human rights dimensions of the Treaty of Waitangi and their relationship with domestic and international human rights law”.</td>
</tr>
<tr>
<td></td>
<td>“In recommending persons for appointment as Commissioners or alternate Commissioners, the Minister must have regard to the need for Commissioners and alternate Commissioners appointed to have among them knowledge of, or experience in … the Treaty of Waitangi and rights of indigenous peoples”.</td>
</tr>
<tr>
<td>Judicature Act 1908</td>
<td>“If the appeal involves … an issue affecting … the Crown’s obligations under the Treaty of Waitangi … the Judge may direct that the Solicitor-General be served with the notice of appeal and with documents subsequently filed in the appeal”.</td>
</tr>
<tr>
<td>Land Transport Management Act 2003</td>
<td>“In order to recognise and respect the Crown’s responsibility to take appropriate account of principles of the Treaty of Waitangi …” a number of mechanisms are available to help Māori participate in the process of making decisions about land transport.</td>
</tr>
<tr>
<td>Local Government Act 2002</td>
<td>“In order to recognise and respect the Crown’s responsibility to take appropriate account of the principles of the Treaty of Waitangi …” two parts provide principles and requirements for local authorities that are intended to help Māori participate in the processes of local authorities to make decisions.</td>
</tr>
<tr>
<td>Statute</td>
<td>Treaty reference</td>
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</table>
| Local Government (Auckland Council) Act 2009                          | “[Part 7] establishes a board whose purpose is to assist the Auckland Council to make decisions, perform functions, and exercise powers by … ensuring that the Council acts in accordance with statutory provisions referring to the Treaty of Waitangi”.

| Local Legislation Act 1989                                            | “Nothing in subsection (1) affects the validity of, or affects or prevents the making of, any claim under the Treaty of Waitangi or based on a right arising or alleged to arise out of the Treaty (whether under the Treaty of Waitangi Act 1975 or otherwise)”.

| Māori Fisheries Act 2004                                              | “The Māori Fisheries Act 1989 was enacted to make better provision for the recognition of Māori commercial fishing rights secured by the Treaty of Waitangi”.

| Māori Language Act 1987                                               | “Whereas in the Treaty of Waitangi the Crown confirmed and guaranteed to the Māori people, among other things, all their taonga: And whereas the Māori language is one such taonga”.

| Māori Television Service (Te Aratuku Whakaata Irirangi Māori) Act 2003 | “In recognition that the Crown and Māori together have an obligation under the Treaty of Waitangi to preserve, protect, and promote te reo Māori the purpose of this Act is to provide for …” a number of functions, duties, rights, accountabilities and governance arrangements.

| Marine and Coastal Area (Takutai Moana) Act 2011                     | “In order to take account of the Treaty of Waitangi, this Act recognises, and promotes the exercise of customary interests of Māori in the common marine and coastal area …”

| Museum of Transport and Technology Act 2000                          | “In carrying out its functions under section 13, the Board must recognise and provide for, in such manner as it considers appropriate, the following: biculturalism and the spirit of partnership and goodwill envisaged by the Treaty of Waitangi”.

| New Zealand Geographic Board (Ngā Pou Taunaha o Aotearoa) Act 2008    | “In order to recognise and respect the Crown’s responsibility to take appropriate account of principles of the Treaty of Waitangi …” the Act confers on the Board the function of collecting, and encouraging the use of, original Māori names of geographic features on official charts and maps. Two members of the Board are appointed on the recommendation of the Minister of Māori Affairs.

| New Zealand Public Health and Disability Act 2000                     | “In order to recognise and respect the principles of the Treaty of Waitangi, and with a view to improving health outcomes for Māori, Part 3 provides for mechanisms to enable Māori to contribute to decision-making on, and to participate in the delivery of, health and disability services”.

| Nga Wai o Maniapoto (Waipa River) Act 2012                             | “A guiding principle is the Treaty of Waitangi, because Maniapoto and the Crown are partners under the Treaty of Waitangi and the agreements in the deed in relation to co-governance and co-management of the Waipa River, which are given effect through this Act, are sourced in this Treaty relationship”.

| Public Finance Act 1989                                               | “Nothing in [the Mixed ownership model companies Part of the Act] shall permit the Crown to act in a manner that is inconsistent with the principles of the Treaty of Waitangi”.

| Public Records Act 2005                                               | “In order to recognise and respect the Crown’s responsibility to take appropriate account of principles of the Treaty of Waitangi …” among other things, consultation with Māori and appointments to the Archives Council.

| Resource Management Act 1991                                          | “In achieving the purposes of this Act, all persons exercising functions and powers under it, in relation to managing the use, development, and protection of natural and physical resources, shall take into account the principles of the Treaty of Waitangi”.

| Royal Society of New Zealand Act 1997                                 | “The Council may co-opt members … if, in the opinion of the Council, it is necessary to do so having regard to the desirability of giving effect to the principles of the Treaty of Waitangi”.

| State-Owned Enterprises Act 1986                                      | “Nothing in this Act shall permit the Crown to act in a manner that is inconsistent with the principles of the Treaty of Waitangi”.

| Supreme Court Act 2003                                                | “The purpose of this Act is … to establish within New Zealand a new court of final appeal comprising New Zealand judges … to enable important legal matters, including
Statute  | Treaty reference
--- | ---
Te Ture Whenua Māori Act 1993  | "Whereas the Treaty of Waitangi established the special relationship between the Māori people and the Crown: And whereas it is desirable that the spirit of the exchange of kawanatanga for the protection of rangatiratanga embodied in the Treaty of Waitangi be reaffirmed".

Table 9.1 confirms Parliament’s preference for referencing principles rather than the Treaty itself.

The Table also reveals that:

- almost all statutes with Treaty clauses contain regulatory provisions of some kind;
- most references to the principles of the Treaty of Waitangi in legislation are in statutes governing physical resources and the environment, where Māori have strong iwi and hapū relationships, often involving kaitiaki relationships[^51] – including land, water, important sites, wāhi tapu and other taonga;
- some references are made to Treaty principles in legislation governing other areas in which Māori have an interest, for example, taonga such as the language (te reo) and health (hauora) and Māori protocol;
- there does not appear to be a consistent description of the application of Treaty principles in statutes;
- the statutes create obligations on a range of parties, and many are not the Crown, such as obligations on local government, Crown entities, Officers of Parliament and a Body Corporate.

[^51]: Kaitiakitanga forms one of two foundational and interlinked concepts within Māori thinking on environmental management. The first is whanaungatanga—the organisation of concepts and relationships through whakapapa or familial connections. As the Waitangi Tribunal explains:

> Kaitiakitanga is really a product of whanaungatanga – that is, it is an intergenerational obligation that arises by virtue of the kin relationship. It is not possible to have kaitiakitanga without whanaungatanga. In the same way, whanaungatanga always creates kaitiakitanga obligations. (Waitangi Tribunal, 2011, p. 105)

Because the relationship Māori have with the environment is described in terms of whakapapa, the claim that particular Māori groups have to kaitiakitanga is based on this sense of relationship. In Māori cosmology, there is little or no distinction between human ancestors and whenua, maunga or awa from which one descends (or to put it in the appropriate cultural context,”can whakapapa to”).

A note on the wording and priority given to Treaty principles in legislation

Where specific Treaty clauses have been incorporated into legislation, the priority to be given to Treaty principles depends on the wording of the clause and its status in the context of the statute. Important considerations include whether the principles are accorded priority, or they are one of a number of considerations; and whether the clause imposes a mandatory obligation or a discretionary power (Te Puni Kōkiri, 2001).

Provisions that “give effect” or “recognise and provide” are stronger standards (conduct must be consistent with the principles) than “take into account”, which in turn is stronger than having “particular regard”. To have “particular regard” often implies process obligations around, for example, consultation (Parliamentary Commissioner for the Environment, 2002). Where an Act containing a Treaty clause requires the administration of related Acts, the Treaty principles are also relevant to the administration of those Acts.

[^51]:
Officials from the Treasury and the Crown Law Office spoken to in the course of the inquiry have observed that Parliament has, in more recent years, become concerned at the resulting uncertainty and cost associated with broadly stated Treaty clauses. In response, Parliament now tends to favour more specific Treaty clauses that specify the action to be taken in satisfaction of Treaty principles. This tendency can be observed in the wording of clauses in more recent legislation. For example, to recognise and respect the Crown's responsibility to take account of the Treaty of Waitangi, the Environmental Protection Authority Act (2011) established a Māori Advisory Committee to advise the Authority on policy, process, and decisions. The Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act (2012) requires the Minister to establish and use a process that gives iwi adequate time and opportunity to comment on the subject matter of proposed regulations (s. 32) and requires the EPA to notify iwi authorities, customary marine title groups, and protected customary rights groups directly of consent applications that may affect them (s. 45).

While reducing cost and uncertainty, more narrowly defined clauses risk constraining the scope of Māori Treaty rights compared to broader clauses. Further, clauses that specify particular actions that must be taken to satisfy Treaty principles increases the risk that the Waitangi Tribunal (in response to Māori complaint) might investigate whether the actions undertaken are in breach of the Treaty.

F9.7 The priority to be given to references to Treaty principles in legislation depends on the wording of the clause and its status in the context of the statute.

Why have Treaty clauses been included in legislation?

Absent a detailed investigation, it is hard to conclude exactly why Treaty clauses have been incorporated into specific statutes. However, incentives are operating on both Treaty partners that are favourable to including Treaty clauses in legislation. These are briefly discussed here.

In preparing this chapter the Commission engaged with senior officials from Te Puni Kōkiri, the Treasury, the Ministry of Justice and the Crown Law Office. All have had extensive experience working with Treaty principles. The Commission also spoke with a number of Māori groups who have had experience with how the EPA has applied Treaty principles. As noted above, EPA has a Treaty clause in its Act and in a number of the Acts it administers.

Officials were asked how including Treaty clauses into law might have altered the behaviour of regulatory agencies. Officials were of the view that including Treaty clauses in legislation has been a powerful catalyst for changing agency behaviour.

Māori participants were universally in favour of Treaty clauses in legislation as a means of making sure that their interests are taken into account. Māori participants were concerned that if clauses are too narrowly specified, under pressure from stakeholders or ministers, an agency might resort to narrow legalistic interpretations of its obligations. In contrast, officials were of the view that empowering an impartial judiciary to rule on the Crown's compliance with Treaty principles has eased pressure from ministers. As the experience of the judiciary builds and precedent is established and refined, consistent decision making is promoted, so reducing uncertainty for all stakeholders.

There is a view that, in the absence of specific clauses, agencies administering legislation would not have upheld the principles of the Treaty. Of course, without the counter factual, it is hard to conclude what might have happened, and it is noted that many agencies have embraced Treaty principles without any Treaty clause in legislation. Even so, the view that Treaty clauses are necessary is borne out of a long-standing mistrust among Māori that, in the absence of specific clauses, agencies will fall short of expectations. Treaty clauses also provide Māori with legal recourse, and a number of Māori groups have developed a formidable and well-respected ability for accessing and using legal mechanisms to define and protect their interests and rights. However, it should be acknowledged that Māori ability to engage effectively with the judiciary to enforce their rights is patchy, both between iwi and across different policy and regulatory areas.

While Māori appear to have embraced Treaty clauses and legal mechanisms for ensuring that their rights and interests will be met, officials with an eye for risks to the Crown also have an incentive to recommend...
Treaty clauses – as a way of ensuring that agencies meet minimum performance standards with respect to Treaty principles.

There is a legal and a performance risk with respect to Treaty principles where agencies that administer regulatory regimes are not part of the Crown. The EPA, for example, is not formally part of the Crown and neither are local authorities. With respect to local government, the dominant view is that local government owes no responsibilities under the Treaty, apart from specific statutory obligations (Department of Internal Affairs, 2006).

One way that officials can militate against the risk to the Crown is to recommend that references to the principles of the Treaty of Waitangi be included in legislation administered by agencies, whether the agencies are part of the Crown or not. However, while the use of a Treaty clause sets a minimum standard, there are also incentives to narrowly define the actions expected of agencies, to reduce the risk that a clause will be more broadly interpreted than Parliament intended.

The incentives on Māori – to ensure that their interests and rights are protected in law, and on officials – to militate against risks to the Crown, appear to have driven both parties to favour including Treaty clauses in legislation. The incentives are particularly strong in areas where there are clear obligations to be met, especially with respect to Article Two which “confirms and guarantees to the Chiefs and Tribes of New Zealand and to the respective families and individuals thereof the full exclusive and undisturbed possession of their Lands and Estates Forests Fisheries” (English version). Indeed, the Courts have considered the principle of active protection mainly when focused on the property interests guaranteed to Māori in Article Two. Even so, the Waitangi Tribunal has also emphasised the Crown’s duty of active protection in the preamble to the Treaty and in Article Three (Te Puni Kōkiri, 2001). As Table 9.1 reveals, Treaty clauses have also been included in areas where the Crown is seen to have a duty of active protection of Māori interests, such as in health, and in protection of te reo.

While the legislative route can be viewed as an insurance policy for Māori and the Crown, it has its drawbacks. A legalistic approach to policy development and implementation can encourage a minimalist focus on complying with the letter of the law (despite Palmer’s (2001) statement that referencing Treaty principles in legislation better reflects the spirit and intent of the Treaty than the legal interpretation of “bare words”).

In this context, the next section proposes factors that officials should consider when advising on including a Treaty clause in legislation that establishes a new regulatory regime. The section then discusses an alternative approach to the current “case-by-case” approach to referencing Treaty principles in legislation.

Guidance for officials – getting Treaty clauses right

Considerable care is required when deciding the circumstances when legislation should include reference to Treaty principles. By including a Treaty clause in statute, it will be clear that legal provision is being made for Māori rights. It also signals the Crown’s intent, compared to the absence of such a clause. But the nature

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52 Local authorities have substantial regulatory functions and powers conferred on them by about 40 Primary Acts of Parliament (NZPC, 2013a).
53 Even legislative provisions may not be enough. The Waitangi Tribunal, in commenting on the Crown’s duty of active protection, expressed the view that: “… the Crown cannot avoid its duty of active protection by delegation to local authorities or other bodies (whether under legislative provisions or otherwise) of responsibility for the control of natural resources in terms which do not require such authorities or bodies to afford the same degree of protection as is required by the Treaty to be afforded the Crown. If the Crown chooses to so delegate it must do so in terms which ensure that its Treaty duty of protection is fulfilled”. (Waitangi Tribunal, 2011b).
and magnitude and implications of those rights may not be clear to the regulator, Māori, other stakeholders, and even the courts.

Legislative Advisory Committee guidelines (Chapter 5: Principles of the Treaty of Waitangi) provides advice for officials on consultation, managing conflict between Treaty principles and the legislation, and common law rights.

The Crown Law Office should be consulted on issues involving Treaty of Waitangi matters. It advises on the likely impact of particular wording. It does not advise on whether that impact is appropriate in the circumstances. This is the responsibility of the departmental officials most familiar with the subject areas and the nature of stakeholders. Officials are responsible for formulating their best advice to ministers on whether to introduce a clause, and the form it should take.

Te Puni Kōkiri should be consulted on all proposals that might have implications for Māori “as individuals, communities or tribal groupings”. Te Puni Kōkiri provides advice to government agencies on effective engagement with Māori, and on Treaty principles, on a case-by-case basis and more generally.

The advice of officials should take into account the perspectives of stakeholders interested in the policy being developed. However, a minister need not take the advice of officials, and may deal directly with stakeholders to arrive at a preferred position. A wider discussion of any Treaty clause can be expected at Cabinet before a government bill is introduced. Further opportunities exist for consideration first by a select committee after the bill’s first reading, and then by Parliament and the Committee of the Whole House as the bill travels through the legislative process.

Factors to consider when advising on Treaty clauses
The Commission proposes that officials should consider the following factors when developing their advice (Box 9.3).

<table>
<thead>
<tr>
<th>Box 9.3</th>
<th>Incorporating Treaty clauses in legislation establishing regulatory regimes</th>
</tr>
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</table>

**Māori**
- Whether Māori have a strong, relatively unified and legitimate interest in the policy being developed and/or how it is subsequently implemented.
- Whether Māori would have the capability, capacity and incentive to effectively litigate to protect their rights. If the legal rights are unenforceable by those given the rights, they will have little value.
- The extent to which the clause might negatively impact Māori or some groups of Māori (for example, strengthening rights to traditional kai moana could be at the expense of Māori recreational and Māori commercial take).
- Whether Māori trust the government to deliver appropriately on their Treaty interests in the absence of a Treaty clause.
- The extent to which a Treaty clause might be valued in its own right, for example, as an acknowledgement of mana or partnership.

**Stakeholders**
- The ability of stakeholders to meet any additional standards required of them, and the cost of their doing so. This requires considering the range of stakeholders likely to be impacted, their interests and capabilities.
- The degree of uncertainty/certainty likely to be generated for stakeholders, and the ability of those stakeholders to manage that uncertainty.
Chapter 9 | The Treaty of Waitangi in regulatory design and practice

Not all factors need to be present. Any one factor may be sufficient justification for a Treaty clause, although in practice a number of factors combined would provide a more compelling case. There are also trade-offs to be considered. For example it might be hard for Māori to effectively litigate to enforce their rights in statute (bullet point 2), but a Treaty clause would be valued as an acknowledgment of mana or partnership (bullet point 5). There are also trade-offs to be made between the interests of Māori, stakeholders and the Crown. And while the capacity of stakeholders to meet the standards required of them is a consideration (bullet point 6), including a Treaty clause will be a catalyst for stakeholders to develop the capability required. Whether a Treaty clause should be included in legislation requires careful judgement. It is not a decision to be made in a formulaic fashion. Instead it requires the careful balancing on a case-by-case basis of key considerations relating to the regulatory area and the likely impact on Māori, other stakeholders, and the Crown.

Factors to consider in specifying a narrow or broad Treaty clause

If a decision is made that including a Treaty clause is appropriate, the next step is to decide on the form of that clause. Possible factors to take into account when deciding whether to put in place a narrow or broad Treaty clause include:

- how hard it is to predict and define legitimate Treaty rights that might arise in the future in the policy area (this might be harder in areas subject to a high degree of change);
- the provisions in other related legislation – whether it is realistically practical for an agency administering multiple related pieces of legislation (often with the same stakeholders and Māori interests) to implement differently worded (narrow or broad) Treaty clauses;
- the ability of other stakeholders to manage the greater uncertainty and legal risk inherent in a broad clause;
- the risk the Waitangi Tribunal may find in favour of a Māori complainant who opposes a clause that is too narrow; and
- the greater legal risk to the Crown inherent in a broad Treaty clause.

If a narrow clause is chosen, the risks identified above could be partly managed by building in administrative mechanisms to drive broader regulatory performance against Treaty principles. Such mechanisms might include guidance for agencies or requiring agencies to disclose the steps they have taken to comply with Treaty principles.

Similarly, if a broader clause is chosen, greater certainty can be introduced by developing guidance or, more formally, a code in deemed regulations (see Table 2.1). Such mechanisms would also be easily changed as needed to better fit changing circumstances, capabilities and interests over time.
Whether a Treaty clause should be included in legislation requires careful judgement. It requires the careful balancing on a case-by-case basis of key considerations relating to the regulatory area, and the likely impact on Māori, other stakeholders, and the Crown.

An alternative approach

In the course of the inquiry, a number of participants expressed the view that putting Treaty clauses in legislation on a “case-by-case” basis implied that the Crown could be selective in choosing when and how it would be bound in legislation to uphold the principles of the Treaty of Waitangi. An alternative approach could be to have an overarching Treaty provision in legislation (separate from the jurisdiction the Treaty of Waitangi Act 1975 confers on the Waitangi Tribunal to investigate actions inconsistent with Treaty principles). The Bill of Rights Act or the State Sector Act were suggested as suitable locations for such a clause. This “chapeau” legislative provision would mean that all agencies administering Acts would be required to incorporate the principles as appropriate. It would not necessarily preclude including specific Treaty clauses in Acts to provide more guidance on how to apply the principles in specific circumstances. Specific clauses, however, should not diminish the obligations in the chapeau clause. The question for the Commission, consistent with the terms of reference for the inquiry (para. 1), is whether this would be a system-wide improvement in the operation of regulatory regimes in New Zealand? The Commission is interested in hearing further views on this matter.

Would an overarching Treaty clause in an appropriate statute (separate from the jurisdiction the Treaty of Waitangi Act 1975 confers on the Waitangi Tribunal to investigate actions inconsistent with Treaty principles), that signals the Crown’s intent with respect to the principles of the Treaty of Waitangi, improve the operation of regulatory regimes in New Zealand?

9.4 Guidance for good practice

While legal rights and obligations are enforceable in a court of law where behaviour falls below a minimum standard, excellence cannot be legislated for. Providing guidance on how to apply Treaty principles and sharing good practice can improve the practices of regulators in upholding the principles of the Treaty of Waitangi, as appropriate for their area of regulation.

In the submission from Environment Canterbury, Dame Margaret Bazley offers insight on effective approaches, and also points to the weaknesses of relying on legislative requirements:

Environment Canterbury has experience and insight to offer on effective approaches to working in partnership with Māori... in terms of its *Tuia* partnership with Ngai Tāhu. This partnership has been built from the ground up, and has been progressed from identifying and respecting past issues and grievances to working shoulder to shoulder to set in place new ways of working focussed on solutions and practical outcomes. *Tuia* is premised on mutual good faith and commitment to do what is right and in the best interest of the iwi and the region, not on narrow legislative requirements. (sub. 4, p. 1)

Good practice from regulators in upholding Treaty principles of partnership, mutual respect and good faith starts at the top. It depends crucially on the attitude and behaviours of the chief executive and senior management. It will require putting internal policies, processes and practices into place, and guidance for staff about how to apply the principles in their work.

This section looks at what guidance has been produced for applying Treaty principles in a range of contexts and for a range of purposes. The section also provides a framework for assessing Treaty guidance material. Section 9.5 looks at the leadership and the internal policies, processes and practices of one regulator in applying the principles of the Treaty of Waitangi.
The quality of guidance available

A number of government agencies have developed guidance about applying Treaty principles. The Commission located 10 examples for review:

- Best practice guidelines: Tangata whenua effects assessment – a roadmap for undertaking a Cultural Impact Assessment (CIA) under HSNO 1996 (Environmental Risk Management Authority, 1996);
- He tirohanga o kawa ki te Tiriti o Waitangi (Te Puni Kōkiri, 2001);
- Guidelines for cultural safety, the Treaty of Waitangi and Māori health in nursing education and practice (Nursing Council of New Zealand, 2011);
- New Zealand coastal policy statement 2010 guidance note policy 2: The Treaty of Waitangi, tangata whenua and Māori heritage (Department of Conservation, 2010);
- Guidelines for consulting with tangata whenua on the RMA: An update on case law (Ministry for the Environment, 2003);
- Guidelines for cultural assessment – Māori Under the Intellectual Disability (Compulsory Care and Rehabilitation) Act 2003 (Ministry of Health, 2004);
- Good practice guidelines for working with tangata whenua and Māori organisations: Consolidating our learnings (Landcare Research, 2005);
- Guidance on the Marine and Coastal Area (Takutai Moana) Act 2011 (Ministry of Justice, n.d.);
- Nga Ara Tohutohu Rangahau Māori guidelines for research and evaluation with Māori (Ministry of Social Development, 2004);
- Consistency with the Government’s Treaty of Waitangi obligations (in New Zealand Treasury, 2013a).

Some of the guidance has been written to help with policy development or with research, some by regulatory agencies to help with applications, and some for capability building. Not all of the guidance relates to regulation making or regulatory practice.

Guidance on any topic ought to cover what needs to be covered, be accurate and relevant and meet stakeholders’ needs. A number of sources provide tips and advice for producing guidance material. For example, the RMA quality planning resource website (www.qualityplanning.org.nz) advises councils on how to produce pamphlets and guidance material about resource consents. It advises that the material should be non-technical, readily available, and current.

In this section a framework is offered for assessing Treaty guidance material (Box 9.4). The framework is then applied to the guidance documents listed above. It makes transparent the criteria on which the guidance is being assessed, promotes assessment consistency across the different types of guidance material, and is able to identify specific areas where the material could be improved.54

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54 There are of course limitations to the assessment framework – it sheds no light on how well the guidance is being applied and it does not identify areas of government activity that need, but do not have, guidance material.
and non-iwi), how they are to be identified and built into the regulatory function, how to assess whether this is being done appropriately.

- Accurate and up to date: The information should be based on contemporary thinking in the subject area, and should be accurate and internally consistent.

- Relevant: The purpose of the guidelines should be clear. The information should be relevant to the regulatory subject area: the issues likely to arise, the nature of the stakeholders (including their interests and capabilities) and the purpose and objectives of the legislation.

- Accessible: The guidance material should be appropriate to guiding officials in their work. It should also be accessible to stakeholders to promote a shared understanding, manage expectations, reduce uncertainty and to promote agency accountability for their performance against the guidelines.

- Excessive prescription should be avoided: Māori are not a single homogenous group. Interests, values, historical circumstances capability and capacity vary widely across Māori communities. So there is no standard process for determining whether proposed regulation or its implementation will raise Treaty of Waitangi issues, or how those issues are best managed.

- Promotes best practice: While it is important that the guidelines help officials to identify and manage legal risk as appropriate, it is even more important that the guidance promote regulatory best practice.

- Good practice example: This helps to make the theory real for officials and stakeholders, aiding learning, acceptance and demonstrating relevance.

- Spill-over benefits: Where appropriate, the relevance of the approach outlined for other stakeholders should be identified. For example, issues focused on cultural sensitivity are relevant to many groups beyond Māori.

### Process

- Well promoted: The guidance should be accessible and well publicised. In some cases, training in its use should be available.

- Further information: The guidance should identify further relevant sources of information and contacts to aid officials (and others) in applying the information.

- Reviewed: There should be periodic reviews of the guidance, involving officials, experts and stakeholders to keep the guidance current and relevant.

An overall assessment is made about the quality of the material produced, with comments on a number of aspects noted below.  

**Overall assessment**

Nearly all of the guidance reviewed promoted best practice over simple legal compliance (7 out of the 10 reviewed). No guidance was considered so bad that it would not add value to stakeholders, although the difference between the best and the worst was significant. The guidance was rated on a scale of “passable” to “excellent”. Overall, the quality of the guidance was too low. The reasonable expectation of the Commission is that guidance should have rated “very good” or better on the assessment criteria, but only 3 achieved this standard.

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55 Assessment notes are in Appendix B. The Commission did not interview any agency that produced the guidance to seek their views. The guidance was taken and assessed as it was found. The Commission took the view that the target audience should be able to make use of the guidance without needing further explanation or clarification.
Meets the needs of stakeholders
The guidance prepared by the Ministry of Justice on the Marine and Coastal Area (Takutai Moana) Act 2011 was the only guidance reviewed that had sections specifically targeted to different stakeholder groups (Māori claimants, local authorities and business). In contrast, the guidance for cultural assessment under the Intellectual Disability (Compulsory Care and Rehabilitation) Act (2003) was not targeted to the range of stakeholders identified (a number of mental health professionals, a specialist in tikanga, and whānau). Different stakeholder needs could have been better met by providing a range of guidance products (for example, a pamphlet for the patient/whānau, a formal document for the health professionals, and another for the specialist in tikanga focusing on expectations and boundaries).

Accurate
While a few errors were detected in the guidance reviewed, it is of concern that at least one example appears inaccurate and misleading. Guidance prepared for the Environmental Risk Management Authority (ERMA), now the EPA, to help applicants prepare a cultural impact assessment, says applicants are expected to consider whether Treaty principles are “impacted by the proposed application, and if so how?” But the principles apply to Māori and the Crown. The applicant will usually be neither. The regulator and affected Māori should be making judgements on whether the application, if approved, would impact Treaty principles. This is not the role of the applicant. The guidance should have tried to more precisely articulate the nature of Treaty principles from the regulator’s point of view. This would have been more useful for the applicant and Māori.

Up-to-date guidance
The guidance on the Marine and Coastal Area (Takutai Moana) Act 2011 is up to date. And because applications under the Act are possible only up to 2017, it is unlikely to need further review/updating. There is a named contact for enquiries. In contrast, the guidance to improve research (undertaken for the Ministry of Social Development and its contractors), where that research requires input from Māori, seems not to have been kept current. Nor are the identified contacts current.

The Treaty
Where taken head on, the Treaty section often appeared somewhat forced and contrived – in many guidance documents it represented something of a “judder bar”. Typically, the Treaty was dealt with through referencing court decisions and Waitangi Tribunal opinions. Those documents that did not deal with the Treaty explicitly appeared to have the best logical flow and clarity.

The quality of guidance to help apply Treaty principles could be improved. None of the guidance reviewed was considered so bad that it would not add value to stakeholders, and overall the guidance promoted best practice over simple legal compliance. Even so, there was a significant difference between the best and worst examples. Only one example had sections specifically targeted to different stakeholder groups. Some guidance was misleading or inaccurate.

The framework was developed as a means of formally assessing the quality of guidance on how to apply Treaty principles according to a consistent set of criteria. But the framework could help regulatory agencies develop their own guidance as to how Treaty principles apply to their area of regulation. Agencies developing guidance material can use the criteria as a checklist to ensure that the guidance is accurate and covers what needs to be covered, is relevant and accessible to the range of stakeholders it is intended for, and promotes good practice. The framework reinforces the importance of guidance being readily available, easily found, and kept up to date.

The two examples that the Commission rated as “excellent” (Appendix B) also provide useful models for other agencies to look at when developing their own guidance about the application of Treaty principles.
9.5 Sharing good practice — the experience of the EPA

Sharing good regulatory practice is one way of raising the standard of practice among regulators. This section reviews the approach to and results achieved by the EPA in incorporating the principles of the Treaty of Waitangi into its decision making. The purpose is to distil lessons for other regulators to help them improve their performance against Treaty principles. This is taken from the full case study prepared for this inquiry: Pickens, 2014.

In undertaking the case study, key stakeholders and EPA personnel were interviewed (Box 9.5).

**Box 9.5  EPA case study interviewees**

**James Ataria**
James has been a member of Ngā Kaihautū Tikanga Taiao (the EPA Māori Advisory Committee) since its inception in July 2011, and prior to that was a member of ERMA’s Ngā Kaihautū. James has a doctorate in environmental toxicology and is a senior lecturer and Tumuaki of the Kaupapa Māori Unit, Faculty of Agriculture and Life Sciences at Lincoln University.

**Maria Bartlett**
Maria is a member of Te Herenga (the Māori National Network) and works for Te Rūnanga o Ngāi Tahu in its environmental policy team.

**Richard Hill**
Richard works with applicants to help them through the applications process. The applications relate mainly to biological controls. Richard has international experience of processes in this area.

**Tipene Wilson**
Tipene is the chair of Ngā Kaihautū and has 10 years’ experience with the EPA and its predecessor, ERMA. He is the chief executive of a consultancy firm specialising on maximising opportunity, creating value and building corporate and government capability to work productively with Māori, giving him wide experience of government regulators. He also undertakes projects for his marae and hapū.

**Malibu Hamilton**
Malibu is a long-term member of the Te Herenga Network, first with ERMA and more recently with the EPA. He had been heavily involved in the Royal Commission on Genetic Modification. He describes himself as a Māori environmental activist.

**Tim Hale**
Tim is the facility manager at AgResearch in Hamilton. He has a long association with ERMA and the EPA with respect to applications for new organisms.

**Maree Pene**
Maree is a member of Te Herenga and represents Ngāti Wairere. She has been involved with ERMA and EPA for many years, mainly in relation to GM issues. In these roles she has also been involved with a range of government regulators.

**Linda Faulkner**
Linda is responsible for Kaupapa Kura Taiao (the Māori Policy & Operations Group of the EPA). Her main role is to ensure that the EPA has policies, protocols, processes and programmes in place to ensure iwi/ Māori are appropriately involved in the EPA’s decision-making processes and activities.
Chapter 9 | The Treaty of Waitangi in regulatory design and practice

The Environmental Protection Authority

The EPA was established on 1 July 2011 by the Environmental Protection Authority Act 2011 as a Crown Agent. The EPA is a quasi-judicial body of 6–8 people appointed by the Minister for the Environment who are selected to represent a “balanced mix of knowledge and experience” in the appropriate areas. The Authority is supported by the staff and infrastructure of the government Agency and together the Authority and the Agency form the EPA (Figure 9.1).

Figure 9.1 The EPA

Objective of the EPA

The EPA must undertake functions under the EPA Act and environmental Acts in a way that “contributes to the efficient, effective and transparent management of New Zealand’s environment and natural and physical resources; and enables New Zealand to meet its international obligations.”

Legislation administered

- Hazardous Substances and New Organisms Act 1996 (HSNO Act)
- Resource Management Act 1991 (RMA)
- Climate Change Response Act 2002
- Ozone Layer Protection Act 1996
- Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012 (EEZ Act)
- Imports and Exports (Restrictions) Act 1988

Activities include

- Administering applications for major infrastructure projects of national significance.
- Regulating and administering approvals for new organisms - (plants, animals, genetically modified (GM) organisms).
- Regulating hazardous substances and chemicals.
- Administering the Emissions Trading Scheme and the New Zealand Emission Unit Register.
- Managing the environmental impact of activities in EEZ, including prospecting for petroleum and minerals, seismic surveying and scientific research, marine consents.

Much of the EPA’s work is spent facilitating the decision-making process for proposals from applicants for nationally significant resource management proposals under the Resource Management Act 1991 and administering proposals for new applications under the Hazardous Substances and New Organisms Act 1996.

Recent history

While the EPA is a relatively new body, at its core are the responsibilities carried forward from ERMA. To these have been added new responsibilities such as regulating activities in the Exclusive Economic Zone.

With respect to incorporating the principles of the Treaty of Waitangi into its decision making, ERMA had a strong culture of identifying, understanding and incorporating, as appropriate, Māori views into its processes. This had not always been the case. The 2001 Report of the Royal Commission on Genetic Modification found many Māori believed they were disenfranchised from ERMA’s processes. Specifically, the Commission found “Māori concerns that consultation is being carried out too late, is too brief and that, on occasion, isolated individuals have been expected to respond on behalf of one or more hapū or iwi, and even on a national basis” (chapter 11, p. 303). It was not only Māori who were dissatisfied with the process. Applicants requiring consent for activities found it hard to know who they should consult with, and there were complaints of the cost of doing so.
In response to the Commission’s findings, the government agreed to establish Ngā Kaihautū (the Māori Advisory Committee) to advise ERMA on issues relating to Māori. Further, in 2003 ERMA established Te Herenga (a national network of Māori representatives). Both bodies were carried forward into the EPA, although only Ngā Kaihautū has statutory backing.

The amalgamation of a number of regulatory functions previously undertaken by other agencies, and the addition of new functions, within the EPA was almost universally supported by stakeholders interviewed. Māori stakeholders spoke of amalgamation better accommodating the “big picture” perspective they favoured, in preference to having to navigate the different bureaucracies needed to settle issues that stretched across multiple agencies. The EPA had also “gone the extra mile” by facilitating Māori access to other regulators by, for example, inviting relevant regulators to hui and helping to build Māori capacity for engaging with those regulators.

The EPA’s approach to decision making

Consistent with the purpose statements of the legislation the EPA administers, the Authority takes a net-benefit approach to decision making. This means that if the expected benefits of an application are expected to outweigh the expected costs, then the application is approved. For example, the purpose of the RMA is to promote the sustainable management of natural and physical resources. This means managing the use, development, and protection of natural and physical resources in a way or at a rate that enables people and communities to provide for their social, economic, and cultural wellbeing (section 5). The EEZ Act 2012 is similarly focused on sustainable management (section 10(2)). Section 9(1) of the HSNO Act 1996 states that “the Governor-General may from time to time, by Order in Council, establish a methodology (which includes an assessment of monetary and non-monetary costs and benefits) for making decisions … and the Authority shall consistently apply that methodology when making such decisions”.

The HSNO (Methodology) Order 1998 articulates the principles to be taken into account when assessing costs and benefits (Box 9.6).

A balanced and even-handed approach to stakeholders and their interests was commented on by most interviewees. This is enabled by the net benefit approach to decision making. What is striking about the EPA’s approach, however, is that it does not limit its role to ensuring applicants comply with the regulatory standards required before an application is approved. EPA staff are able to help applicants prepare their applications. The conflicts of interest that would normally arise in this situation are minimal – the Authority acts autonomously, advised (but not instructed) by the Agency, with input from experts if required. This independence allows the Authority to better resist activist and other political influences that might affect the decision-making process. Conflicts or perceptions of bias are further minimised as the EPA also helps those impacted by applications, including Māori, to engage in processes relating to applications. Further, the HSNO Act requires the application and evaluation process to be open, transparent and public, features that promote accountability and better performance by the regulator. The pre-application stage involves applicants identifying all significant impacts and issues, and engaging with affected parties. During the
application phase, the application is open to public submissions to ensure concerns have been adequately addressed. A public hearing may be called for, and if called it must be held.

The EPA does not limit its role to ensuring that applicants comply with regulatory standards before an application is approved. Applicants are helped in preparing their applications and the EPA also helps those impacted by applications. Conflicts of interest are minimised because the application process is open, transparent and public.

The principles of the Treaty of Waitangi

The EPA’s Act provides that “in order to recognise and respect the Crown’s responsibility to take appropriate account of the Treaty of Waitangi, a Māori Advisory Committee will advise it on policy, process and decisions” (s. 4a) and “the EPA and any person acting on behalf of the EPA must comply with the requirements of an environment Act in relation to the Treaty, when exercising powers or functions under the Act” (s. 4b). Further, the RMA, HSNO, Climate Change and EEZ Acts administered by the EPA also contain provisions relating to the principles of the Treaty of Waitangi and the interests of Māori.

Notably, the EPA takes Treaty principles into account within the parameters provided by a net-benefit, decision-making approach (the assessment of expected costs and benefits as described above).

The EPA discharges its Treaty responsibilities under its legislation and the Acts it administers within a net-benefit, decision-making approach.

Stakeholders were universally supportive of the way the EPA was discharging its Treaty responsibilities under its legislation, with some even pointing to the Act as simply codifying what was the best approach for the EPA. Others pointed to the value of the Treaty clauses in cutting across what they viewed as unhelpful debate from stakeholders resisting incorporating Māori interests into the process.

However, there was also concern from some interviewees that the “narrow” Treaty clause in the EPA Act could result in a minimalistic interpretation of the EPA’s responsibilities. It was noted, for example, that while Ngā Kaihautū has statutory backing, the widely supported Te Heranga does not and so could be disbanded.

While incorporating Treaty clauses in legislation can be an important catalyst for change, its success is highly dependent on the motivation, incentives and capability of those who work within it. It also depends on goodwill, trust and a shared commitment to making it work. While some Māori stakeholders have been able to point to risk with respect to the Treaty clauses, to this point without exception those risks do not appear to have eventuated. This is in no small part due to the EPA’s investment in establishing and maintaining good relationships with its stakeholders.

An investment in good relationships

This section considers four mechanisms that the EPA uses to incorporate the Treaty principles into its decision making (Figure 9.2).
Figure 9.2 Mechanisms to incorporate Treaty principles in EPA decision making

Nga Kaihautū (Māori Advisory Committee)

- Māori resource and environmental managers, practitioners and experts who represent their iwi, hapū or Māori organisation. It includes those who values and interests are directly affected by EPA decisions.

Te Herenga (Māori National Network)

- EPA administers the membership database, coordinates activities, covers reasonable travel and related costs, facilitates meetings and organises minutes and information exchange.

Guidance

- EPA has produced guides, tools, case studies and other information to help applicants and other stakeholders.
- Includes published protocols to help decision makers to produce consistent, high-quality decisions appropriately incorporating Māori perspectives. Accessible to other stakeholders, giving them greater certainty over the process leading up to final decisions. Developed through consultation and active engagement with stakeholders.

Kaupapa Kura Taliao (Māori Policy and Operations Group)

- Leads the development and management of relationships with Māori to enable their participation in decision making and other EPA activities.
- Provides support to Nga Kaihautū and development of Māori cultural and Treaty capability internally for decision makers and staff. The General Manager is a member of the EPA’s Leadership Team.

Notes:
1. Inspired by Gordon Walters
Ngā Kaihautū (Māori Advisory Committee)

The Ngā Kaihautū members interviewed see their role as mainly that of “process guardians”. This means their role is to ensure Māori have adequate opportunity to contribute their views into the EPA decision-making process. Ngā Kaihautū also contributes its own views in a “safety valve” role, in particular if it considers the decision makers have not accessed the information they need through the consultation process. The Ngā Kaihautū interviewees were very clear that, while they do offer a Māori perspective, they do not represent the views of Māori.

Māori stakeholders interviewed valued the role played by Ngā Kaihautū, in particular its oversight role within the process that contributed to building trust. Applicants also valued the role it played in putting context around, and promoting an understanding of, submissions by Māori stakeholders on applications.

Te Herenga (Māori National Network)

On its establishment, there was an identified risk that Te Herenga might become a liability. For example, it might be captured and discredited by a few dominant personalities, see its role as combative, or might not be accepted by other stakeholders or by Māori more widely. These risks have not materialised. Of the mechanisms identified as driving EPAs success, none were spoken of more highly than Te Herenga, in particular from the Māori perspective.

Te Herenga has provided the face-to-face (kanohi ki te kanohi) relationship needed across all levels of policy development and implementation. That it is a permanent and formal structure has meant it has been easier to build capability and trust and realise the associated benefits. For example, the growing trust of Māori in Te Herenga is realising savings for Māori, as it has increasingly been relied on to accurately and effectively bring the views of Māori to the table on their behalf. A number of interviewees were also positive about Te Herenga being more hapū than iwi based. The protocols around how it operates and the involvement of Kāhui Kaumātua were believed to have worked to moderate extremes, promote consistency across the network and manage risks more generally.

From the perspective of applicants, Te Herenga has provided a useful filter for views on their applications and has promoted the right information getting to the right people, so reducing risks and costs to applicants.

From a system-wide perspective, it was noted Te Herenga, and Māori more widely, were sometimes the only submitters on some applications, and that their involvement in these cases was necessary for the integrity of the system and promoting robust decision making.

Some stakeholders spoke of the importance of adequately resourcing Māori to participate in consultation on applications. Some reimbursement of direct costs is made available to Māori stakeholders. However, some Māori thought obtaining Māori cultural information should be funded on a similar basis to contracting experts reviewing, for example, the impact of an application on the biota of a region. This is a difficult issue. The two situations are not directly comparable. A contractor is directly accountable to the funder for the product provided, and their services will be discontinued if the funder does not consider their advice is adding value. Māori stakeholders would not find these restrictions acceptable.

It should be acknowledged that Māori have additional steps and costs to incur when developing submissions, which need to be accommodated. At least to a point, the EPA appears to have done this. But the EPA appreciates that regulators need to monitor these expenses carefully, having regard to the capability of respective stakeholders and the importance of gaining their perspectives. Any funding must be directly related to gaining those perspectives.
The permanent and formal structure of the Māori National Network has meant that capability and trust has been built, and this is realising benefits. Te Herenga has increasingly been relied on to accurately and effectively bring the views of Māori to the table on their behalf.

Māori have additional steps and costs to incur when developing submissions, but care needs to be taken when considering funding, having regard to the capability of respective stakeholders and the importance of their perspectives, and ensuring funding is directly related to gaining those perspectives. Regulators need to monitor these expenses carefully.

Guidance
The Commission has reviewed the quality of a number of guidance documents across the public sector (section 9.4). The quality of the EPA’s documents is with the best of those reviewed, being well balanced, comprehensive, accessible, and focused on best practice rather than legalistic. EPA’s documents use practical examples, are relevant, and provide good links to extra information, including EPA contacts. Consistent with the other Treaty guidance reviewed, the Treaty section appears forced. It is unclear what it adds to the rest of the document. Rather than as a separate section, the Treaty might instead have been presented as the foundation within which the guidance is provided. Alternatively, it could be used to communicate directly with applicants about the nature of Treaty principles from the EPA’s perspective.

Providing guidance for applicants and other stakeholders about navigating the process is considered a core part of the EPA’s role as a regulator.

Kaupapa Kura Taiao (Māori Policy and Operations Group)
At this point, having Kaupapa Kura Taiao – a separate Māori Policy and Operations group – is regarded by the EPA as a superior model to using those resources to build Māori capability and capacity within the other units (integration). But a number of stakeholders thought that full integration would be the natural end point.

All stakeholders spoke very highly of the EPA staff, and in particular of Kaupapa Kura Taiao. In particular, they commented on its open and timely communication, accessibility, balanced approach, pro-active work, capability and credibility. Less tangibly, but importantly, stakeholders commented that its approach was promoting a necessary culture of respect and understanding between parties, and a shared desire to protect a system that stakeholders believed was serving their interests well. Nearly all stakeholders emphasised "good relationships" and "trust". To a large extent, this must be credited to the work and attitude of the EPA’s staff and its leadership. The EPA’s staff are the common ingredient across all the EPA’s systems and processes used to build Treaty principles into the EPA’s decision making.

Having produced a suite of guidance material, the EPA has shifted to working directly with stakeholders. This makes it even more important that the EPA has access to excellent staff. An obvious risk for the EPA to manage is retaining, motivating and training its staff.

Open and timely communication, accessibility, a balanced approach, pro-activity and a culture of respect and understanding must, to a large extent, be credited to the work and attitude of the EPA’s staff and its leadership.
Challenges from the EPA perspective

The EPA has avoided a legal and minimalist approach to Treaty principles in its legislation and in the legislation it administers, favouring an approach that facilitates achievement of its regulatory objectives through building strong relationships and trust.

The EPA was candid about the challenges it faces in maintaining its approach to incorporating Treaty principles in its decision making. The Authority is expecting that its decision making approach will increasingly face legal challenge at some point either by applicants or stakeholders, and that this may undermine the non-legalistic approach taken by the EPA, one based on building strong relationships and trust. It was also noted that while cultural impacts are included in the net benefit approach to decision making, as with all qualitative assessments, they carry less weight than quantitative assessments of costs and benefits.

There was some nervousness expressed about the recent addition of the EEZ legislation to EPA’s responsibilities, and whether the EPA’s current approach to applicants and stakeholders could be maintained under the EEZ legislative framework. This is despite the provisions in the EEZ Act for Māori consultation, recognition, and requirements to notify affected Māori groups of consent applications that may affect them.

EPA staff are justifiably proud of the EPA’s organisational culture and approach. Staff noted that the EPA’s reputation, with respect to the way the organisation incorporates the principles of the Treaty of Waitangi in its processes and in its decision making, is a result of the leadership of the Board and the Chief Executive. Changes in leadership can have a significant impact on attitudes, practices and processes, but the Treaty clause in the EPA’s legislation can provide some protection.

Lessons

All interviewees identified the EPA as the standard setter with respect to incorporating Treaty principles into its decision making, with a number commenting they believed this was also more widely acknowledged by their respective stakeholder groups.

The institutional structures and processes that the EPA uses have clearly worked for it in achieving its regulatory functions and meeting the diverse range of interests of its stakeholders. Some features of these arrangements might prove useful for other regulators. Even so, the arrangements should not be blindly copied. Rather, it should be acknowledged that the arrangements are a model that has brought the EPA positive change so that today it enjoys a high level of stakeholder support.

In designing their own arrangements to build Treaty principles into their decision making, regulators should focus on their own regulatory responsibilities and functions, and the capabilities, capacity and incentives of their stakeholders. To do this successfully is challenging, with significant risks and costs, in particular in the early years. But for many regulators, retaining the status quo is also a risky and costly strategy, and one which may become unsustainable and compromise the overall objectives of New Zealand’s regulatory regimes.

The arrangements adopted by the EPA are a model that has brought the EPA positive change and support from stakeholders. In designing institutional arrangements, processes and practices to incorporate Treaty principles into their work, regulators should focus on their own regulatory responsibilities and functions, and the capabilities, capacity and incentives of their stakeholders.

Looking to the EPA example, perhaps the most important lesson for other regulators is that the investment in developing good relationships reaps benefits. For the EPA, that investment has been in the form of:

- the cost of establishing and supporting Te Herenga and Ngā Kaihautū;
- holding Hui;
- developing and promulgating high-quality guidance;
- ensuring the EPA is accessible to enquiries where the guidance by itself is insufficient;
- the cost of EPA’s Māori Policy and Operations group, and integrating their work with the rest of the EPA;
- having the GM of the Māori Policy and Operations Group on the leadership team;
- promoting information exchange, and training opportunities.

Beyond this, and perhaps as at least as importantly, the EPA has actively developed a culture that promotes within its relationships, respect, openness, honesty, fair dealing and dignity for all. In turn, this has produced a strong dividend in the form of trust, a word emphasised by most of the stakeholders interviewed.

Stakeholders believe this investment has been reducing the cost on all parties involved in the application process (for example, litigation, consultation and ongoing coordination), while improving the quality of engagement and the resulting decisions. It has also brought buy-in to the success of the EPA approach and a shared commitment to making it work. Further, when decisions go against stakeholders, those decisions are now more readily accepted and are less likely to be contested or breed unhelpful cynicism. These dividends are expected to continue to accrue over time, although a few risks were identified by stakeholders that may require active management.

An important lesson from the EPA’s experience for other regulators is that the investment in developing good relationships pays off in the form of reduced cost on all parties involved in the application process, while improving the quality of engagement and the resulting decisions. It has achieved buy-in to the success of the EPA approach and a shared commitment to making it work. When decisions go against stakeholders, those decisions are now more readily accepted and are less likely to be contested.

Finally, the EPA appears to have successfully built the Treaty framework into its broader decision-making framework, which is strongly grounded in a public welfare approach – maximising expected benefits relative to expected costs (Figure 9.3). Too frequently the Treaty and public policy frameworks are treated as competing rather than complementary and reinforcing paradigms. These tensions were not found here.

**Figure 9.3**  Weaving Treaty principles with a net-benefit decision-making approach
9.6 Summing up

It is important that the principles of the Treaty of Waitangi are appropriately taken into account when designing and implementing regulatory regimes. The continuing evolution of the relationship between the Treaty partners, and how the principles of the Treaty are interpreted by the courts, can generate considerable uncertainty for those applying them in regulatory regimes. This chapter has provided some guidance to help work through the issues.

“Treaty clauses” – references to the principles of the Treaty of Waitangi – are in about 36 statutes. Treaty clauses are often in statutes where Māori have a relationship with the land, water, important sites, wāhi tapu and other taonga. There does not appear to be a consistent description of the application of Treaty principles in statutes. Most of the statutes contain regulatory provisions and create obligations on a range of parties that are not the Crown. The inclusion of Treaty clauses can be seen as an insurance policy for Māori and the Crown – a legal acknowledgement of Māori interests and rights, and a clearer definition of the Crown’s responsibility with respect to those rights (that in the absence of a specific clause might be interpreted more broadly).

Yet the legislative route does have drawbacks. A legalistic approach is somewhat at odds with the central Treaty principle of good faith. It is in this context that this chapter provides a set of factors that officials should consider in recommending the inclusion of Treaty clauses in statutes that establish regulatory regimes or regulatory agencies.

Excellence in regulatory practice with respect to Treaty principles, however, cannot be legislated for. Good practice in upholding Treaty principles of partnership, mutual respect and good faith depends on senior leadership, good internal policies and processes, and guidance for staff and stakeholders.

A number of examples of guidance about how to apply Treaty principles have been reviewed against a set of criteria. While the assessment criteria the Commission has used reveals that the overall quality of existing guidance material can be improved, the real value in the assessment framework is as a tool to help regulatory agencies develop their own guidance about how to apply Treaty principles in their area of regulation.

Sharing good regulatory practice is one way to raise the standard of practice among regulators. Lessons from the experience of the EPA are identified. Other regulators can adopt the lessons learned to improve their regulatory practice with respect to the principles of the Treaty of Waitangi. An important lesson for other regulators is that investing in developing trust through good relationships can pay off in reduced costs and better regulatory decision making.
10 Decision review

Key points

- Appeals of regulatory decisions involve the courts scrutinising the merits and correctness of those decisions. Judicial review involves the courts scrutinising the process and legality of decision making. These are distinct processes. “Merits review” are appeals that look at the correctness of a decision.

- Appeal rights of administrative decisions exist only where Parliament expressly provides for them. There is a perception that New Zealand statutes provide limited access to appeal of regulatory decisions, but this is not supported by research undertaken by the Commission. Most regulatory regimes provide for appeals, and only a small minority of regimes provide limited or no access to appeals.

- Judicial review is an inherent power of the High Court, and so does not need to be provided for in statute. There is no evidence that judicial review is ineffective in ensuring the lawfulness and reasonableness of the Executive’s actions.

- Judicial review is an important constitutional check on the exercise of state power, and protects the right of New Zealanders to be treated fairly and in accordance with the law. Attempts in legislation to exclude judicial review of the Executive are wholly undesirable.

- The breadth of judicial review and appeals can vary widely, but in practice significant overlap exists between judicial review and appeal in New Zealand. In New Zealand the scope of judicial review is comparatively broad and can sometimes include scrutinising the substantive merits of the Executive’s decisions.

- The overlap between judicial review and appeal means that judicial review already adequately provides many of the advantages that submitters ascribed to merits review or appeals. This includes sharpening the incentives on decision makers to come to the correct decisions.

- Appeal rights should be provided where the designers of regimes are confident the appeals will improve regulatory outcomes and support the objectives of the regulatory regime. This requires taking into account the costs and uncertainty that appeal rights create.

- In deciding whether to provide for appeal rights of complex or highly technical regulatory regimes, designers need to critically assess the institutional capability and expertise of the court or tribunal reviewing the decision, relative to the decision maker at first instance.

- A range of mechanisms are available that may support the institutional capability of the appellate body to deal with appeals of complex and highly technical decisions. Two mechanisms are using technical experts as lay judges and providing for more inquisitorial processes.

- The Legislation Advisory Committee (LAC) guidelines on review and appeal provide a good list of considerations to take into account when designing review and appeal provisions in regulatory regimes. The LAC notes that appeals:
  - scrutinise and correct individual decisions, with the aim of providing redress, and
  - maintain a high standard of public administration and public confidence in the legal system.

- Even so, the LAC notes that the value of appeals needs to be balanced against the considerations of cost, delay, significance of the subject matter, competence and expertise of the decision maker at first instance, and the need for finality.

- It is not clear the extent to which the LAC guidelines influence decisions about provision of appeals in the design or review of regulatory regimes.
10.1 Introduction

New Zealand is fortunate to have a judiciary that its citizens have confidence in – the second highest regarded in the Organisation for Economic Co-operation and Development (OECD, 2013b). In New Zealand, the courts have a constitutionally important role in supervising the actions of the Executive, ensuring that it acts reasonably, fairly, and within the bounds of the laws established by Parliament. Unlike other countries, New Zealand courts have no role in supervising Parliament. Courts have no ability to strike down or invalidate legislation passed by Parliament.

Judicial scrutiny of the exercise of Executive power is particularly important in the area of regulation, given the coercive nature of those powers.

Where Parliament provides for appeals, courts also provide a forum for parties to test that regulators have made “correct” decisions.

The courts also perform an essential role in interpreting legislation. What does it mean for a regime to operate in “the long-term interests of consumers”? Who is “a fit and proper person” to run certain businesses? Ultimately, the courts decide what these terms mean in practice.

Judicial review and appeals are distinct processes.

- Judicial review is concerned with the legality of the decision. A reviewing court must examine the process and procedures of decision making and ask whether the decision should be allowed to stand.
- In contrast, appeals involve adjudication on the merits and may involve the court substituting its own decision for that of the decision maker (Joseph, 2007).

This chapter discusses the review of regulatory decisions, with a particular focus on judicial oversight of regulators in areas that are highly complex and technical.

- Section 10.2 outlines the types of decision review, and compares judicial review with merits review.
- Section 10.3 describes the types of merits review provided for in regulatory regimes in New Zealand.
- Section 10.4 provides a framework for assessing what sort of judicial oversight of regulatory decisions should be provided for.
- Section 10.5 assesses calls for greater access to merits review of regulatory decisions in regimes where this is limited or not provided for.
- Section 10.6 considers alternative ways of achieving the outcomes sought from merits review of regulatory decisions.
- Section 10.7 summarises the Commission’s guidance on access to review and appeal of regulatory decisions.

10.2 Types of decision review

Types of appeals and reviews of regulatory decisions include:

- judicial review;
- appeal to a tribunal or court;
- internal review; and
- ombudsmen.

56 Commerce Act 1986, s. 1A.
57 Insurance (Prudential Supervision) Act 2010, s. 18.
Each type has different processes, focuses, and outcomes.

Judicial review

Judicial review is the exercise of the High Court’s inherent jurisdiction to rule on the legality of public acts (Joseph, 2003, pp. 821-22). Over centuries, the English courts developed a doctrine of common law which established that courts had the inherent jurisdiction needed to administer the law, independently of any statutory power:

> The inherent jurisdiction of the Court arises in relation to and for the purpose of giving proper support for the functioning of the Court as a Court of justice. It is part not of the substantive but of the procedural law: and in such a case as the present it is exercisable for the purpose of controlling not only the actions of persons associated with the proceedings but the world at large. That sort of judicial power obviously could not be used for purposes of individual or group convenience nor even for the public interest in general. Instead, as one experienced office of the Court in England has said, "The juridical basis of [the inherent] jurisdiction is … the authority of the judiciary to uphold, to protect and to fulfil the judicial function of administering justice according to law in a regular, orderly and effective manner." (Taylor v Attorney-General, 1975, at 689)

The High Court’s jurisdiction derives from the instruments that established the High Court (then called the Supreme Court) in New Zealand and provided that the New Zealand High Court exercised the jurisdiction of the common law and equity courts in England, including their inherent powers of judicial review. The Judicature Amendment Act 1972 simplified the procedure for obtaining judicial review remedies, but did not extinguish or limit the common law right of review.

The three main grounds of judicial review are procedural impropriety, illegality and reasonableness. **Procedural impropriety** focuses on the compliance of the decision making process with the rules of natural justice, or with the prescribed procedural requirements. **Illegality** is concerned with whether the decision maker has correctly understood and given effect to the law that regulates its decision-making power. **Reasonableness** is concerned with the fairness or reasonableness of a decision, including the exercise of discretion. The courts used to apply a very high threshold in assessing reasonableness, only intervening where a decision was outrageous or perverse. Now the courts apply a sliding threshold and varying intensities of judicial review depending on the context. This is discussed further below.

Appeal

The courts lack any inherent appellate jurisdiction over regulatory authorities: "Appellate powers are purely statutory. There is no such thing as a common law right of appeal." (Guy v. Medical Council of New Zealand, 1995, at 93)

Not all appeals are of the same type or scope. Appellate review is a continuum of different types with a variable intensity of review. The intensity of appellate review depends on how Parliament has conferred that jurisdiction. It depends particularly on the type or form of the appeal and other procedural and evidential rules that shape the courts’ approach. (Thwaites & Knight, 2011)

The Legislation Advisory Committee (LAC) categorises appellate procedures across four broad types (2012, pp. 285-86). The types offer a structure to anchor analysis on the legal scope of appeals.

Figure 10.1 illustrates these broad appellate procedures on a continuum according to the breadth and depth of allowing further, or new, evidence to be presented to the court. To the left is the relatively broad approach, which then narrows as one moves to the right.
De novo appeal or hearing

At one extreme is a de novo appeal. In de novo appeals, the appellate body stands in the shoes of the primary decision maker and hears the matter afresh. The appellate body is not bound by the presumption that the decision appealed from is correct and therefore may approach the case afresh. This is the most intensive form of judicial supervision, allowing the appellate body to form its own view on the law, fact, and policy involved in the regulatory decision. The LAC guidelines note that de novo hearings are “more costly” than available alternatives (2012, p. 284).

Appeals by way of re-hearing

Appeals by way of re-hearing are normally heard on the record of evidence before the primary decision maker, with often an ability to re-hear or receive more evidence. The appellate body may reach its own findings on the evidence, including about developments since the initial decision. But there are some presumptions about the circumstances in which the appellate court can differ from the decision maker under review.

Pure appeals

In pure appeals (or appeals stricto sensu), the appellate body may depart from the lower body’s conclusions if consistent with the evidence available to the lower body. But the appellate body cannot hear new evidence. The LAC guidelines note that “this category of appeal is very restrictive and should not be enacted” (2012, p. 284).

Appeals on questions of law or appeal by way of case stated

At the other extreme are appeals on questions of law. The supervising court may only intervene to correct an error of law or to determine a legal question. Where an appeal is restricted to points of law, the court’s approach is very similar to the approach adopted in judicial review. Sir Kenneth Keith has written: “the distinction between appeals, especially appeals on law alone, on the one hand, and judicial review on the other can and often does disappear” (1969, p. 159).

Choices between the types of appeals

Civil procedure rules adopt appeal by way of re-hearing as the default if legislation provides for appeal but doesn’t specify the type (High Court Rules, r 20.18; District Court Rules 2009, r 14.17). The LAC guidelines states that an appeal by way of re-hearing is the most appropriate procedure in most contexts (2012, p. 286). It is more expeditious than a hearing de novo because it focuses on specific alleged errors. It is not as narrow as an appeal on a question of law only.

The LAC (2012) explains that the choice of procedure turns on the type and purpose of the appeal and the nature of the appellate body, and offers these general observations:

An appeal by way of re-hearing is the appropriate procedure in most contexts. It is more expeditious than a hearing de novo because of its focus on specific alleged errors, but not as restrictive as an appeal stricto sensu. Indeed, an appeal should focus on specific alleged errors. In general, there is no need to provide an opportunity to re-litigate the whole matter, as in a hearing de novo, unless there is
good reason not to presume that the first instance decision-maker correctly ascertained the facts. The added cost of a complete re-hearing generally counts against this procedure. An appeal should not be by way of case stated unless there is some reason why this option is preferable to an ordinary appeal limited to questions of law. (p. 286)

What is merits review?
The terms merits review and appeal are often used interchangeably. But merits review is any process that lets all of a decision be scrutinised, including process and substance. Using this framework, merits review would include *de novo* appeals, re-hearings, and pure appeals (Figure 10.2). Appeals on points of law/case stated would not be a merits review. A court need not undertake a merits review; specialist tribunals are sometimes established to do so.

**Figure 10.2** Merits review within the legal scope of appeals

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**Difference between judicial review and appeal**

**The orthodox approach**
The orthodox approach is that judicial review involves sitting in judgment on the correctness of the decision-making process, whereas appeal involves sitting in judgment on the correctness of the decision itself. A judge in the United Kingdom House of Lords described the difference this way:

> Judicial review is concerned, not with the decision, but the decision-making process. Unless that restriction on the power of the court is observed, the court will in my view, under the guise of preventing the abuse of power, be itself guilty of usurping power … Judicial review, as the words imply, is not an appeal from a decision, but a review of the manner in which the decision was made. *(Chief Constable of the North Wales Police v Evans, 1982, at 154-55)*

The courts will often strongly proclaim the distinction between judicial review and appeal. In *Brannigan v Davison* [1997] 1 NZLR 140 (PC) at 148, the Privy Council observed:

> In these proceedings the court is not exercising an appellate jurisdiction. It is exercising its supervisory, review jurisdiction. The distinction is not a piece of empty formalism.

The distinction drawn between the two forensic processes serves as a self-serving reminder and discipline that a judge does not have unfettered licence in judicial review. The courts must not trespass, they say, on the merits of the decision or the policies it implements. Those matters are for the mandated decision maker, not the courts. In *Waitakere County Council v Lovelock* (1997, at 397), the Court of Appeal reiterated that review was not an appeal on the merits and that the court “could not substitute its own opinion for that of the [decision maker]”. The proper concern on review was “with the decision-making process, not the decision itself” *(R v Sloan, 1990, at 479)*. In *Qiong v Minister of Immigration* (2005, at 30) the Court was adamant that “an attack on the merits of the decision … is not the purpose of a judicial review proceeding”. The Supreme Court ventilated similar sentiments in *Unison Networks Ltd v Commerce Commission* (2008, at 54). It observed that the courts are concerned to identify the legal limits of the power rather than assess the merits of its exercise: “They must be careful to avoid crossing the line between these
concepts”. In *Hopper v North Shore Aero Club Inc* (2007, at 16), the Court of Appeal stated: “merit review of the decision … would be appropriate in an appeal, rather than a review of the process in the more traditional judicial review sense”. There are many such statements in the judgments of the courts.

**An outdated distinction?**

Notwithstanding the courts’ professed commitment to the appeal–review distinction, the processes of appeal and review inevitably overlap and merge at the margins. This is occasionally acknowledged by the courts. Professor Joseph comments:

> At times, the courts are disarmingly frank. In *Shaw v Attorney-General*, the High Court conceded that reasonableness review was merits based, and was ‘the very antithesis of judicial review’. In *Isak v Refugee Status Appeals Authority*, the same Court conceded that unreasonableness ‘focuses on the substantive outcome rather than the processes of decision-making’. Challenges of unreasonableness necessarily envisage a ‘qualitative assessment’, entailing ‘an element of subjectivity’ in balancing public benefits and private rights. Challenges of proportionality likewise entail qualitative assessments, requiring courts ‘to review the balance struck by the primary decision-maker between the conflicting considerations’. *(2014, at 22.3.5)*

Over the past few decades, developments in judicial review have undercut the claim of a substantive distinction between review and appeal. In many judicial review cases, the review is based on the merits, with the court focusing not on how the process was made but on the actual decision.

The courts cross the appeal/review divide when they evaluate the decision maker’s policy role and discretion. They also engage in merits-based review where they proceed from remitting decisions for reconsideration to reversing decisions. Certain grounds of review enable greater scrutiny of the substance of the decision: the ground of irrationality or unreasonableness, for example, is inherently merits-based.

**Judicial review can include scrutinising the merits of a decision**

In 1985, New Zealand’s pre-eminent jurist Sir Robin Cooke (later Lord Cooke of Thorndon) said that “the time has probably come to emphasise that New Zealand administrative law is significantly indigenous” (*Budget Rent A Car Ltd v Auckland Regional Authority*, 1985 at 418). Lord Cooke is responsible for broadening the scope of judicial review in New Zealand jurisprudence, particularly the ground of “unreasonableness” (Knight, 2008).

Unreasonableness is the principal ground of challenge that inherently enables merits review. In practice, unreasonableness is subordinate to the grounds of illegality and procedural impropriety. In many cases a finding of unreasonableness will be reached only after other reviewable errors in the decision making have been unearthed on those grounds.

The seminal British case establishing unreasonableness as a ground is *Associated Provincial Picture Houses v Wednesbury Corporation* (*Wednesbury*, 1947). In that case, Lord Greene said that a public authority acts unreasonably when a decision it makes is “so absurd that no sensible person could ever dream that it lay within the powers of the authority”. *Wednesbury* unreasonableness set a high test for a decision to be set aside.

> It is true to say that, if a decision on a competent matter is so unreasonable that no reasonable authority could ever have come to it, then the courts can interfere. That, I think, is quite right; but to prove a case of that kind would require something overwhelming, and, in this case, the facts do not come anywhere near anything of that kind. (*Wednesbury*, 1947)

The Australian courts have “conclusively adopted” the high test of *Wednesbury* unreasonableness, according to the President of the Australian Administrative Appeals Tribunal, the Hon Justice Garry Downes. Justice Downes notes the limited application of unreasonableness as a ground for judicial review

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59 *Isak v Refugee Status Appeals Authority* (2010).
60 *Carter Holt Harvey Ltd v North Shore City Council* (2006).
61 *Huang v Minister of Immigration* (2008).
in Australia, citing evidence that “there are not many decided cases in which the principle has been successfully raised” (Downes, 2008).

By contrast, in New Zealand Lord Cooke led a “rejection of legal formalism in the area” (Knight, 2008, p. 100).

It is no longer sufficient for decision-makers to assert that their decision is not absurd or irrational; it is necessary for them to consider whether the circumstances in which the decision was made and its consequences mandate closer scrutiny of the logic and substantive merits of the decision. (Knight, 2008, p. 107)

First, in Thames Valley Electric Power Board v New Zealand Products and Paper Ltd (1994) the Cooke Court held that substantive unfairness was a stand-alone ground of review. This set a review threshold considerably lower than the Wednesbury threshold. Substantive unfairness, by definition, focuses on the substantive merits of the impugned decision.

There have been few decisions where challenges on the ground of substantive unfairness have succeeded. The most likely scenario for a successful challenge would be a serious of errors that cumulatively have the effect of substantive unfairness.62

Second, the courts might also lower the threshold in individual cases to engage with the substantive merits of decisions. This is known as the “variable intensity” or “sliding threshold” approach. The level of scrutiny varies depending on the circumstances of individual cases, as does the degree of deference the courts will grant to decision makers in the Executive.

Joseph notes that “bodies exercising public regulatory functions may expect more intensive judicial scrutiny than decision-makers entrusted to develop and apply policy, such as government Ministers and elected councils” (2007, p. 939). Joseph notes that “the sliding scale of review is part of the legal tapestry” (2007, p. 936).

At the extreme, courts will take a “hard look” at decisions that impinge on human rights63 (the UK courts review these decisions with “anxious scrutiny”). More intensive review invariably entails a court evaluating the merits of the decision.

Finally, other principles that the courts may consider under the head of unreasonableness – including proportionality, consistency of decision making, and the innominate ground – also entail a substantive review of the merits of a decision.

In the course of oral arguments, Justice Tipping expressed most plainly where the court will intervene:

I would hope I would always have a hard look, the question is more, isn’t it, to the standard to which you hold the decision making? … the more fundamental the right, the more reasonable the decision must be … And the Court must interfere where it must … you interfere if you think you should. (Ye v Minister of Immigration, 2008)

Despite the overlap, significant differences remain

Although review and appeal overlap, key differences exist. For example, in assessing a decision on the judicial review ground of reasonableness, the court will evaluate whether the substantive decision is reasonable, applying a review threshold appropriate to the particular context. But the court’s task in judicial review is not to determine whether the decision or the particular is the “most correct”, unlike in appeals by way of re-hearing or de novo appeals.

Another important difference between review and appeal is that in an appeal the appeal body can consider all aspects of a case. In a judicial review the court focuses just on the issues based on the grounds of the judicial review.

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The outcome of a successful challenge is also a key difference. Successful appeals involve the court substituting its decision for that of the regulator. Successful judicial reviews typically involve referring the decision back to the decision maker to re-consider, with or without express directions from the court. This has led to the claim that a successful judicial review only leads to the same decision being confirmed – a claim discussed in section 10.5 below.

**A spectrum of review and appeal**

Judicial review and appeal are both pluralistic mechanisms, “each representing variable forms of judicial methodology and intensity depending on the context and circumstances”. (Thwaites & Knight, 2011, p. 223). The court’s approach will depend upon many complex contextual factors: the particular legislative provisions, the subject matter of the decision, and the suitability of the particular questions to judicial adjudication.

Academic and practitioners’ commentary acknowledges the overlap between review and appeal. Joseph calls the appeal/review distinction an outdated dichotomy that no longer explains what the courts are doing, or should be doing, when exercising their review jurisdiction (2007, pp. 830-31). Professor Taggart wrote that “many of the dichotomies upon which administrative law has rested – appeal/review, merits/legality, process/substance, discretion/law, law/policy, and fact/law – are no longer seen as giving as much guidance as they once did”. (Taggart, 2006, p. 83). The last edition of *Judge Over Your Shoulder* acknowledges that, in practice, it is sometimes “difficult to completely sever” process from the merits (Crown Law Office, 2005, at 12).

This overlap of judicial review and appeals at the margin stands in contrast to the situation in Australia, where there is a “significant division between merits review and judicial review” (Downes, 2008) and where strict Wednesbury unreasonableness is still the standard of review.

### F10.1
In New Zealand there is significant overlap between the scope of judicial review and appeal in practice.

### F10.2
Judicial review in New Zealand is much wider in scope than in Australia, and can include greater scrutiny of the merits of decisions.

**Deference to expert regulators in highly technical fields**

The question of whether and when judges will defer to decision makers is not settled. Knight (2010) provides a useful discussion of the varied approaches taken within the New Zealand courts. The current Chief Justice has stated that she considers deference to be a “dreadful” word (Knight, 2010, p. 408).

Even so, the courts will generally defer to the decisions of expert regulators of highly complex and technical areas, such as the Commerce Commission. The courts will generally not entertain a review of the merits under the substantive unfairness or sliding scale/variable intensity principles. Courts will only entertain intervening on narrower grounds:

> Often, as in this case, a public body, with expertise in the subject-matter, is given a broadly expressed power that is designed to achieve economic objectives which are themselves expansively expressed. In such instances Parliament generally contemplates that wide policy considerations will be taken into account in the exercise of the expert body’s powers. The courts in those circumstances are unlikely to intervene unless the body exercising the power has acted in bad faith, has materially misapplied the law, or has exercised the power in a way which cannot rationally be regarded as coming within the statutory purpose. (*Unison Networks Ltd v Commerce Commission*, 2007, at 55)

The Supreme Court reiterated those cautionary remarks the following year in *Z v Dental Complaints Assessment Committee* (2008).
As a result, the overlap between judicial review and appeal does not apply to economic regulation or to other highly technical areas of regulation.

Courts will generally defer to the decisions of expert regulators of highly complex or technical areas. In these areas of regulation, there is still a clear distinction between judicial review and appeals, and judicial review is less likely to scrutinise the substantive merits of decisions.

Proposals for reform in the United Kingdom and Australia

In the course of the Commission’s engagement, attention was drawn to two recent reviews of decision review frameworks in other countries.

First, in the United Kingdom, recent proposals would limit the scope of judicial oversight in regulatory and competition appeals. A discussion document presents two options to do this. Both would introduce standards of appeal that are similar to the scope of judicial review in New Zealand. (Box 10.1)

Box 10.1 Proposed reform of regulatory and competition appeals in the United Kingdom

In June 2013 the British Government published a consultation paper seeking submissions on options for reform of the appeal regime for regulatory and competition appeals. The report focused on appeals from decisions of economic regulators and competition authorities on the basis that they are materially different from non-economic regulators.

The report identified concerns about the appeals regime in some sectors and for some types of decisions. These concerns include:

- that the current framework can impose significant time and costs on all parties, which slows down efficient regulatory decision making and can create regulatory uncertainty;
- the length and scale of some appeals, involving large volumes of evidence and legal and technical arguments; and
- the lack of consistency across sectors and across different types of decisions, which has a number of consequences, including that, in certain sectors, there appear to be strong incentives on parties to appeal decisions.

The UK Government considered reform of the appeal regimes for regulatory and competition decisions might be desirable so that:

- it is more focused on identifying material errors;
- appeal bodies’ expertise is applied in the most appropriate way and appeal routes are more consistent across sectors to provide greater certainty and better use of resources;
- it is more accessible to all affected parties;
- incentives in the system are aligned with government’s objectives for the appeals framework; and
- appeals processes are as efficient and cost effective as possible.

The UK Government was of the opinion that the grounds of appeal should be defined more clearly and narrowly and focused on clear errors by the decision maker. “Merits review” can result in different levels of scrutiny and having more well-defined grounds of appeal will provide greater clarity and certainty up front. (Her Majesty’s Government, 2013, [4.21], p. 29).

The Government proposed that the scope of appeal available to challenge these decisions should be narrowed and no longer be on all aspects of the merits. It proposed two options for limiting the scope
of appeals.

- Appeals should be heard to an (English) judicial review standard. The grounds of review would be largely limited to procedural irregularities.

- Appeals allowed on a slightly wider basis, including:
  - material error of law (an error of law that is significant enough to have an impact on the ultimate decision)
  - material error of fact (an error of fact that is significant enough to have an impact on the ultimate decisions so that it might be different)
  - material procedural irregularity (a procedural irregularity that was significant enough to have an impact on the ultimate decision so that it might be different)
  - unreasonable exercise of discretion (decision maker exercised its discretion in a way that no reasonable regulator would act)
  - unreasonable judgments or predictions.

In addition, the Government proposed additional measures to discourage unmeritorious appeals and improve the efficiency of handling cases.

Most responses to the proposals have been hostile, with the Competition Appeal Tribunal itself saying that “no case at all is made out in the Consultation for altering or reformulating the standard of review in competition appeals”.


Second, proposed changes would broaden the scope for review of decisions from the Australian Energy Regulator, while instituting less adversarial review processes (Box 10.2).

Box 10.2 Proposed reform of review of decisions from the Australian Energy Regulator

From 2008 the Australian Competition Tribunal has been able to undertake limited merits review of decisions by the Australian Energy Regulator (AER) under the National Electricity Law and National Gas Law. The review is described as “limited” because an applicant is required to establish one of four grounds of review based on regulatory errors of fact or discretion (rather than establishing any “preferable” decision). An applicant must also persuade the Tribunal there is a serious issue to be heard. The grounds are:

- the AER made an error of fact in its findings of facts, and that error of fact was material to the making of the decision;
- the AER made more than one error of fact in its findings of facts, and that those errors of fact, in combination, were material to the making of the decision;
- the exercise of the AER’s discretion was incorrect, having regard to all the circumstances; and
- the AER’s decision was unreasonable, having regard to all the circumstances.

There was a requirement to review the limited merits review regime within seven years. In October 2012 an independent expert panel published its final report on the effectiveness of the regime and recommended changes.

The panel findings are noted below.
There was a lack of evidence of major improvements in the way the AER conducted its activity as a result of the regime. Decisions were routinely appealed, and the appeals were generally successful.

Applicants have most often been successful in claims establishing that the regulator’s decisions were unreasonable or an incorrect exercise of discretion, rather than the grounds relating to errors of fact.

Not all stakeholders’ views were taken into account. Consumer and user groups were “inconvenient guests”, largely disengaged from participating in the appeals process due to the high risks and costs, and the hostile environment.

The Tribunal used an overly legalistic approach. Its focus on error correction has not supported the objectives of the regime, in part because only errors detrimental to the interests of applicants are subject to correction (while errors in their favour are unchallenged).

Consistent with this, there was evidence that the appeals resulted in allowed revenues 8% higher than the determinations of the AER.

The regime had adversely affected consumer interests in the short run through higher network charges and retail energy prices, without any evidence of countervailing consumer benefits over the longer term, consistent with the objectives of the regimes.

Regulatory certainty over the long term was undermined, as the upward pressure on energy costs generates political pressures to reform the regime.

The expert panel’s recommendations included:

- replacing the four grounds of appeal with a single, broader, ground that “that there is reason to believe that a materially preferable decision exists”;
- review which is investigative rather than adversarial in nature (“review should not be a contest between interest groups, but an exercise in seeking to discover whether or not there exists a decision that better serves the long-term interests of consumers”);
- an obligation to seek out consumer views at the review stage; and
- a new, wholly administrative body (that is, not a court, and not a judge-led tribunal) to undertake the reviews.

The Standing Council on Energy and Resources is consulting on reforms arising from the expert panel’s recommendations.


### Internal review

Internal review is where a decision made by an officer in an organisation is reviewed by another person in the organisation. Some regulatory organisations have a formal system of internal review; others have more ad hoc systems. Internal review may be established by legislation or through administrative and policy processes within the organisation.

Internal review is available under the following Acts:

- Agricultural Compounds and Veterinary Medicines Act 1997
- Animal Products Act 1999
- Animal Welfare Act 1999
In most cases the requirements to provide internal review apply to very specific decisions, rather than providing for review of regulatory decisions generally. In some cases there is a requirement that the agency’s chief executive conducts the review where the chief executive’s decision-making powers have been delegated within the agency.

The Commission has not been able to identify significant literature on the value of internal review of regulatory decisions, or any guidance in New Zealand on their application. Canadian guidance (Administrative Justice Office, 2005) notes the potential for internal review as an easily accessible, quick and cheap way of resolving errors, and points to the benefits of providing direct and immediate feedback to original decision makers. It says that internal review may be most appropriate where administrative decisions are made against clearly articulated criteria, with little discretion exercised.

No regulatory agency that responded to the Commission’s information request mentioned internal review as a method available to review their regulatory decisions.

Internal review could offer promise as a relatively inexpensive, swift way of error correction; or it could be ineffective due to the lack of clear independence. In its submission Business New Zealand commented negatively on the internal review of New Zealand Qualifications Authority decisions in regulating English language providers in the private tertiary education sector (sub. 19).

The Commission would like to further understand the risks and opportunities of internal review mechanisms in theory or in practice.

Q10.1 What evidence exists for the effectiveness of internal review of regulatory decisions?

Ombudsmen

The Ombudsman is an independent official responsible to Parliament who can investigate (upon complaint or their own motion) the decisions and actions of central and local government and Crown entities.64

The Ombudsman’s procedures are informal, flexible, and free for complainants. It also has significant powers if required, including requiring the provision of information and the ability to question employees of state agencies under oath.

Following an investigation, the Ombudsman can issue a report and make recommendations. Although its recommendations are not binding, the Ombudsman is considered an effective “constitutional watchdog” (Chen, 2010). It is a regulator and an important check on the actions of other regulators.

In a recent report Transparency International New Zealand highlighted concerns about resourcing of the Office of the Ombudsman:

The Chief Ombudsman is of the view that since about 2009, the Ombudsmen have been seriously under-resourced and a substantial backlog of complaints is awaiting investigation. … From 2008/09 to 2011/12, the number of complaints on hand at any one time increased from about 1,000 to about 1,700, a 59 per cent increase. In contrast, the Ombudsmen’s annual appropriation from Parliament

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64 The organisations subject to the Ombudsman’s jurisdiction are listed in the First Schedule to the Ombudsmen Act 1975.
increased only 6.3 per cent. In 2011/12, only 53 per cent of complainants considered the ombudsman process to be timely and overall satisfaction with their standard of service has dropped … Senior lawyers say that although the Ombudsmen’s investigations are thorough and fair, they are no longer referring clients to the Ombudsmen if there is an alternative. (2013, pp. 214-15)

The appropriation for the Office of the Ombudsman increased by 36% from 2008/09 ($6.854 million) to 2013/14 ($9.320 million). The number of complaints received increased by 50% from 2008/09 (6757 complaints) to 2012/13 (13,684 complaints).

These constraints weaken an important check on the exercise of state power, particularly for members of the public who do not have the resources or wherewithal to challenge decisions through other means. As Transparency International New Zealand notes, a weakening of the Ombudsmen will encourage recourse to more expensive processes where an aggrieved party has sufficient resources.

Transparency International New Zealand recommends that the adequacy of funding for the Office of the Ombudsman be reviewed in 2014/15. The Commission agrees.

R10.1 The Officers of Parliament Committee should review the adequacy of funding for the Office of the Ombudsman to undertake its statutory functions to a high standard.

In addition to the Ombudsman with general jurisdiction over the administration, there are also subject-specific and industry-funded Banking Ombudsman and Insurance and Savings Ombudsman schemes.

10.3 What types of appeal are available in New Zealand regulatory regimes?

In its issues paper, the Commission noted calls from legal practitioners and academics for access to greater merits review in New Zealand (2013b). Some of these views on merits review may no longer be current. Articles cited in the Commission’s issues paper by Professor David Round and David Goddard QC both date from 2006, predating the 2008 amendments to the Commerce Act which made merits review the norm for most parts of the regime. The Commission had noted a perception that, in general, New Zealand provided less access to merits review of regulatory decisions than other countries such as Australia, with a comparative reliance on judicial review as the main mechanism to challenge regulators’ decisions.

Research undertaken by the Commission does not support this perception (see Appendix C). In its submission, Business New Zealand correctly notes that “full rights of appeal are embedded in much New Zealand legislation” (sub. 19, p. 15).

Stocktake of appeal rights in New Zealand regulatory regimes

The Commission undertook a stocktake of the 94 pieces of legislation that involved regulation which were identified in the course of mapping New Zealand’s regulatory environment (see discussion of this inquiry’s scope in Chapter 1). Table 10.1 lists the 25 pieces of legislation that provide no access to appeal.

Table 10.1 Regulatory legislation that provides no access to appeals

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<th>Legislation</th>
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<tr>
<td>Atomic Energy Act 1945</td>
<td>Land Transfer (Computer Registers and Electronic Lodgement) Amendment Act 2002</td>
<td>Reserve Bank of New Zealand Act 1989</td>
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</table>

65 Other regimes were excluded from the definition of regulation used in this inquiry, such as immigration, accident compensation, social welfare or employment (see Chapter 1). Although not investigated in the course of this stocktake, it is likely that these types of regimes make more use of internal review mechanisms and appeals to tribunals.
### Legislation

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<th>Act</th>
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<td>Human Tissue Act 2008</td>
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*Source:* Productivity Commission research.

Based on the stocktake conducted, the view that access to merits review is limited is incorrect. Most appeals provided in regulatory regimes are general appeals conducted by re-hearing. First appeals restricted only to questions of law are uncommon; second appeals restricted to questions of law are much more common. Appeals on questions of law are provided for under the following statutes (out of 94 statutes examined):

- Commerce Act 2003
- Crown Pastoral Land Act 1998
- Dairy Restructuring Act 2001
- Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012
- Films, Videos, and Publications Classification Act 1993
- Financial Advisors Act 2008
- Financial Markets Authority 2011
- Financial Markets Conduct Act 2013
- Gas Act 1992
- Hazardous Substances and New Organisms Act 1996
- Securities Act 1978

It is possible to draw some similarities between most of the regulatory regimes established by these statutes. Most of these regimes deal with complex decisions that are highly technical and highly dependent on facts. The first instance decisions are made by expert bodies with particular expertise and experience, such as the Commerce Commission, Financial Markets Authority or the Environmental Protection Authority. Courts may be institutionally less competent than such specialist bodies to deal with these types of decisions.

**F10.4** In general, legislation establishing regulatory regimes does provide access to merits review of regulatory decisions.
A number of important regulatory regimes have a more limited access to merits review. The importance of these regimes in the New Zealand economy will have supported perceptions that there is limited access to merits review of regulatory decisions more generally. For example:

- small parts of the Commerce Act 1986 (that were the subject of significant comment from a number of submitters); specifically, appeals are allowed on questions of law only against determinations under s. 52P that set out how information disclosure regulation or negotiate/arbitrate regulation applies to regulated suppliers or the default price-quality path that applies to regulated suppliers. Other appeals under the Commerce Act are by way of re-hearing;

- The Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012 provides for an appeal on a question of law only against the Environmental Protection Authority’s review of a decision on an application for consent;

- the Financial Markets Authority Act 2011, where the Financial Markets Authority may state a case for the opinion of the High Court on a question of law (s. 48);

- some parts of the Gas Act; specifically, there is an appeal on a question of law only against a decision under any gas governance regulations or rules (s. 43ZC);

- most of the Insurance (Prudential Supervision) Act 2010, except for appeals allowed against powers to remove directors and officers of firms, ban certain persons from participating in the industry, and valuation of policies;

- the Overseas Investment Act 2005, with no right of appeal;

- the Reserve Bank Act, with no right of appeal;

- the Telecommunications Act 2001, which provides for appeals on a question of law only, apart from appeals related to Commission directions about costs, against conditions imposed on the construction of networks, and against the Commission’s refusal of a person’s objection to a civil infringement notice.

In areas of complex or highly technical regulation, access to merits review or the scope of appeal provided is often limited.

Appeal rights are generally not provided to challenge the decisions of ministers. As noted in Chapter 6, ministerial decision making is appropriate in decisions that involve value judgements that are not amenable to technical analysis, or that involve significant fiscal implications. Providing for merits review of ministerial decisions would subject an elected representative’s evaluation as to complex policy issues and community values to review by an unelected body. The appropriate recourse to exact accountability for these decisions is through the ballot box. Courts are generally quick to defer to the judgments of democratically accountable decision makers (*Wellington City Council v Woolworths (NZ) Ltd (No 2)*).

It will generally be inappropriate to provide for appeals of ministerial decisions.
10.4 How to think about access to judicial review and merits review

The red light theory and green light theory are the two main theories of the purpose of administrative law (Harlow & Rawlings, 2009). Figure 10.3 illustrates these two theories.

Figure 10.3 Two theories of administrative law

Red light theory
- The purpose of administrative law is to curb state power, to protect the rights of the individual.
- Strong judicial control of executive power is desirable.
- Access to the courts is an end in itself.
- A non-instrumentalist approach.

Green light theory
- The purpose of administrative law is to help the state meet its policy objectives.
- The judiciary is useful to the extent it serves these goals.
- Access to the courts is a means to an end.
- An instrumentalist approach.

The two theories can apply to review and appeal (Cane, 2004).

- Red light theorists would think about access to judicial oversight of regulators in a non-instrumental way. Such oversight is an essential part of the constitution that should be available to citizens as of right, except in the most extraordinary of circumstances. This is not to deny the likelihood of instrumental benefits from judicial oversight; only that access should not be contingent on such benefits.

- By contrast, green light theorists would think about access to judicial oversight in an instrumental way. What is the (expected) quality of outcomes from the review? Judicial oversight of regulators should be available where it is most likely to improve the quality of regulation.

It is essential to the rule of law that there are external checks to ensure Executive decision makers act lawfully. This is properly the role of the courts, and judicial review fulfils this function well. It follows that a non-instrumentalist approach should be taken to judicial review. It should be available as of right, and is an important component of New Zealand’s constitutional arrangements.

Exceptions do exist. The courts have an inherent jurisdiction to rule on the legality of public acts and no public administration is immune per se from judicial review. Even so, while the courts will always have jurisdiction they may in a particular case find that the issues raised are “non-justiciable” and abstain from ruling on them. “Non-justiciable” means that the particular issue is not suitable for judicial adjudication because the court lacks institutional competence and/or legitimacy to determine the issue. Certain types of issues are often identified as non-justiciable. For example, the courts will be reluctant to review decision making if it involves public policies based on political judgements. They are reluctant to do so because the judicial decision making method is ill-suited to dealing with complex policy issues and political judgements should be made by decision makers with a democratic mandate.

Judicial review will always be available where legislation establishes a regulatory regime and confers powers of decision on a regulator (including on a minister). Every legal power has limits; there is no such thing as
unfettered discretion.66 These limits constrain the design of decision review mechanisms in regulatory regimes: judicial review is a “given”, and there is no way to restrict or amend its application. Attempts in legislation to exclude judicial review of regulatory decisions are wholly undesirable, given the constitutional role of the courts in ensuring that executive power is exercised lawfully (LAC, 2012).

By contrast, there is no general right to ensure that decision makers are correct, which is the general objective of merits review. “Natural justice does not require that there should be a right of appeal from every decision and there is no such thing as a common law right of appeal. However, in most circumstances it will be desirable for legislation to provide a right of appeal against an administrative decision” (LAC, 2012).

It follows that designers of regulatory regimes should take an instrumentalist view about access to merits review. Taking into account the costs, risks and expected benefits, is it likely to improve the outcomes of the regulatory regime? This means that merits review should be thought of not as an external check on the regulatory regime, but as a part of the regime. For example, the test for whether a regime relating to the prudential regulation of insurers should provide for appeals of decisions should be whether the availability of the appeals would “promote the maintenance of a sound and efficient insurance sector” and “promote public confidence in the insurance sector” (which are among the stated purposes of the Insurance (Prudential Supervision) Act 2010, as set out in s. 3).

Legislation Advisory Committee (LAC) guidelines provide help on when to establish appeal rights (Box 10.3).

**F10.7** Access to judicial review should be approached in a non-instrumental way. Judicial review is an important constitutional check on the power of the Executive, and is available to citizens as of right.

**F10.8** Access to appeal (or merits review) should be available where it is likely to improve the quality of regulation, in terms of the objectives of the regulatory regime, taking into account the costs of providing it.

Legislation Advisory Committee (LAC) guidelines provide help on when to establish appeal rights (Box 10.3).

### Box 10.3 Legislation Advisory Committee guidelines on appeal and review

The LAC guidelines state that: “Whether a right of appeal should be provided turns on the nature of the decision and the decision-maker at first instance, and the need to ensure subsequent oversight”. The guidelines advise that “it is generally desirable for legislation to provide a right of appeal against the decisions of officials, tribunals and other bodies that affect important rights, interests, or legitimate expectations of citizens”.

Appeals serve a private and public purpose. The private purpose is to scrutinise and correct individual decisions of decision makers with the aim of providing redress of the particular party involved. The public purpose is to maintain a high standard of public administration and public confidence in the legal system.

The value of having an appeal must be balanced against the following factors:

- cost;
- delay;
- significance of the subject matter;

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66 Padfield v Minister of Agriculture, Fisheries and Food (1968); and Wellington City Council v Woolworths (NZ) Ltd (No 2) (1996).
Although brief, these guidelines appear to set out an approach that is suitably instrumentalist in nature. It invites those designing regulatory regimes to weigh the costs and benefits, and to consider the relative institutional capacity of the decision maker at first instance.

Despite the requirement for papers to the Cabinet Legislation Committee to assess proposals for compliance against the LAC guidelines, it is not clear how influential the guidelines are:

> Officials and ministers are currently supposed to consider whether draft bills comply with the Legislation Advisory Committee’s guidelines. But, as their name implies, these are merely guidelines; in practice they are often ignored, especially, where it matters most, by the Cabinet. (Caygill, 2010)

### Q10.2 How effective are the Legislation Advisory Committee’s guidelines on appeal and review in influencing policy-makers in the design of new regulatory regimes?

#### 10.5 Calls for greater access to merits review

Most submitters wrote favourably about merits review, and told the Commission that there should be greater access to merits review where it is not currently available. A typical submission was that of Genesis Energy. They wrote that merits review mechanisms (beyond judicial review or appeal on questions of law) “correct errors and act as a discipline on the regulator (so drives better quality processes and decisions in the first instance)” (sub. 48, appendix A, pp. 4-5). Carter Holt Harvey submitted that “[t]he right of those affected by regulation to appeal decisions to an independent authority should be identified by the Commission as a reasonable presumption” (sub. 8, p. 9). Wellington Electricity submitted that:

> Merits appeal processes are essential for ensuring robust regulatory outcomes. Regulators should be accountable for the decisions that are made and should be subject to the potential for third party appeal. (sub. 17, p. 1)

Submitters made a number of arguments in support of merits review.

- The threshold for judicial review is high, and it does not provide an effective means of challenging decisions. (subs. 10, 29, 46, 48)
- Access to merits review reduces the incentives for firms to lobby politicians or officials for special treatment or legislative change. (subs. 46)
- Merits review would ensure regulators undertake a proper process (such as give sufficient consideration to consultation). (subs. 5, 31, 46, 48)
Merits review would improve the upstream incentives on regulators to get the decision right, to a greater degree than judicial review. (subs. 5, 19, 24, 31, 46)

Merits review provides for error correction, and better decisions. (subs. 19, 24, 29, 46, 51)

Merits review would clarify the operation of new regimes, and its use would decline over time. (subs. 48)

Even so, not all submitters thought that merits review served the interests of the general public. KLR Investments (sub. 18) and Internet New Zealand (sub. 45) said that merits review was used by large firms to undermine the objectives of regulation or the public interest: “From the perspective of end-users, merits review appears to be an additional expensive and lengthy process that operators use to avoid or delay regulation” (sub. 45, p. 10).

Cost, delay, and complexity are inherent in the appeal of decisions that require specialist expertise due to their highly technical nature. This is illustrated by a recent high-profile merits review of a determination by the Commerce Commission on the input methodologies (IMs) to be applied to the regulation of natural monopolies (Box 10.4).

**Box 10.4  Appeals from the Commerce Commission determinations of the input methodologies for regulation of natural monopolies under Part 4 of the Commerce Act 1986**

Changes to the Commerce Act in 2008 required the Commerce Commission to set IMs. IMs are the methodologies, rules, processes, requirements and evaluation criteria that underpin price control regulation and information disclosure regulation. IMs are intended to promote certainty for suppliers and consumers. Such regulation applies to markets where there is little or no competition and little or no likelihood of a substantial increase in competition. Such markets currently include electricity lines businesses, Transpower, gas pipeline businesses, and major airports.

The Commerce Commission set IMs in December 2010 following an extensive process, tightly prescribed by the Commerce Act.

Over a two year period the Commission produced over 800 separate substantive documents and based its consultation on a distribution list comprising more than 440 individual addressees representing more than 200 different organisations for the IM consultation alone. Consultation on the s 52P determinations was also occurring, often in parallel. It cannot be doubted, therefore, that the Commission’s decision-making process was both careful and considered. *(Wellington International Airport Ltd & Ors v Commerce Commission, 2013, at 173)*

A number of regulated firms brought applications for judicial review that required the Commerce Commission to re-consult on some aspects of the IMs. The IMs were reissued in June and September 2012.

In September 2012 the High Court began hearing a substantive appeal (merits review) of the IMs brought by 10 regulated firms and consumers. Parliament set different rules for appeals against IM determinations than apply to other appeals under the Commerce Act.

- Appeals against IM determinations will only succeed if the court is satisfied that a different IM would be “materially better” than that set by the Commerce Commission. The meaning of materially better was an issue of contention in the appeal.

- The High Court must sit with two “lay members”. Lay members are economic or regulatory experts or academics, appointed to help the court understand the subject matter of the appeals. In this appeal, both lay members were members of the Australian Competition Tribunal.

- The appeal takes place on the basis of a “frozen record”. The court can only consider documentary information and views that were before the Commerce Commission when it made its determination. Although section 52Z of the Commerce Act describes these appeals as a “re-hearing”, the ban on new evidence means it is more properly a pure appeal.
As this case shows, providing access to merits review is not without cost. The financial costs will ultimately be borne by the customers of regulated industries, the shareholders of those firms, and the taxpayer. In many cases regulated firms will have greater financial resources to litigate than regulators. The more avenues that are provided to challenge decisions, the greater this imbalance becomes.

In the case of economic regulation, the costs arising from uncertainty and delay may also be significant. IMs are designed to promote certainty so that firms can invest in future infrastructure to serve the long-term interests of consumers.

Section 53 of the Commerce Act provides that while appeals are underway, the Commerce Commission’s determinations are in effect, to prevent regulated firms adversely affected by determinations using litigation as a delay tactic. Even so, while a successful appeal will allow firms to claw-back revenue they have been denied, this cannot compensate for the uncertainty. This uncertainty may still discourage firms from planning and undertaking capital investment that might serve the long-term interests of consumers while awaiting judicial confirmation or amendment of the IMs.
There appears to be considerable value to finality in this situation, which the LAC guidelines indicate should be considered in deciding whether to provide an appeal. But this does not appear to have been considered in the Cabinet paper or Regulatory Impacts Statement (RIS) relating to 2008 decisions on amendments to the Commerce Act.

**Is judicial review an effective means of challenging decisions?**

A number of submissions argue that the threshold for judicial review in New Zealand is high (for example, sub. 46, p. 13) or that judicial review causes regulators to correct procedural deficiencies without leading to a better outcome for applicants.

Of course, it is possible for a regulator to be ordered by a court to correct a deficient process and yet still reach the same decision again. This can be appropriate. In *Fraser v State Services Commission* (1984) the Court of Appeal noted that the impugned decision may have been justified on the evidence. Even so, it set aside the decision for breach of natural justice.

During the Commission’s inquiry it became clear that the pattern of use of judicial review varies widely across regulatory regimes. One financial institution told the Commission that seeking a review of a decision by the Reserve Bank of New Zealand would be a “nuclear option”. Vodafone’s view was that “in practice, the existing threshold means that review proceedings are most unlikely to be brought” (sub. 46, p. 13).

Other firms that the Commerce Commission regulates have no such compunction. Since the Commerce Act was significantly amended in 2008, firms in the telecommunications, airport and electricity lines sectors have used judicial review to challenge the Commission’s decisions. According to the Commerce Commission’s annual reports, there have been no successful challenges of its processes in this time.

A claimed weakness of judicial review commonly identified is that “they go through the process again and you just get the same decision”. Of course that does not necessarily mean the decision is wrong, only that the regulated party is still displeased. The Commission has not been able to identify evidence on this question in New Zealand. The Court of Appeal has also noted the lack of evidence on this point:

> Regrettably, there is little in the way of empirical evidence in the New Zealand context as to whether administrative law as a behaviour modification mechanism in government actually works. Such empirical evidence as there is in other jurisdictions tends to suggest that administrative law is likely to be able to make only a modest contribution to the promotion of external goals. (*Lab Tests Auckland Ltd v Auckland District Health Board*, 2009, at 398)

Yet an empirical study in Australia suggests regulators often change their decisions following a judicial review. The authors conclude:

> Anecdotal belief had long held that a successful judicial review action would most likely be followed by an agency remaking the same decision, though taking care to avoid the earlier legal error. That belief has now been disproved, at least in Australian judicial review in the period covered by this research project. If theories are built upon facts, then the value of judicial review in producing a favourable outcome to an applicant has been demonstrated. (*Creyke & McMillan*, 2003, p. 186)

In New Zealand, there is also a widespread belief that judicial review is futile. This belief was expressed to the Commission in the course of the inquiry engagement. Yet no evidence was presented to substantiate it.

The Commission has found no evidence to suggest that judicial review is an ineffective method of challenging regulators’ decisions, and ensuring they act in proper, lawful, and reasonable ways.

Goddard argues that, in the area of economic regulation, judges may lack sufficient understanding of the complex issues to assess in a judicial review whether the decisions of a regulator are unlawful, or whether a regulator has taken the relevant material into account in forming a decision.

It is not easy to point to hard evidence of this, but my strong sense of appearing as a counsel in a range of judicial review cases (and a review of other recent decisions) is that this is an area where Judges are less confident than usual in identifying the outer bounds of statutory power and the purpose for which
it was conferred, and as a result exercise less effective control over decisions by regulators than they do in respect of other statutory decision-makers operating in more familiar, or less technical, fields. (Goddard, 2006, p. 6)

Merits review does not solve this problem and indeed exacerbates it. Even with the help of lay members or expert witnesses, it is judges alone who can rule definitively on questions of lawfulness. It is likely that only a greater degree of economic skills, or specialisation among the bench, will help to resolve this issue. In the course of its engagement the Commission heard that New Zealand courts were reluctant to move towards judges becoming more specialised. These issues are discussed below in Section 10.6.

Q10.3 Is there a need for greater specialisation among the judiciary to hear cases relating to complex areas of regulation? What approaches might be effective to develop greater expertise among the judiciary in these areas?

Does the absence of merits review encourage special pleading to politicians or officials?

A lack of access to merits review in the courts does not necessarily mean that aggrieved parties lack other means of recourse. Vodafone, considering the regulation of telecommunications markets notes that “current practice is for MBIE to act as a ‘final arbiter’ of regulatory decisions” (sub. 46, p. 13). For example, following the final decisions of the Commerce Commission’s UBA benchmarking review in 2013, Chorus Ltd had no recourse to merits review in the courts but was able to try to appeal to the Government directly and by motivating public opinion. MBIE brought forward by a number of years a scheduled review of the Telecommunications Act 2001 specifically to consider the Commerce Commission’s benchmarking decisions.

Appeal to ministers is more common and far more formal in Australia and some other countries than in New Zealand. In general, ministerial intervention in the decisions of independent regulators is undesirable. Where it does take place, it should occur through transparent channels.

In the situation described above, Chorus also has a contractual relationship with the Government to undertake the roll-out of ultra-fast broadband. This means that the Government has an additional interest in Chorus being able to fulfil its obligations.

Parties aggrieved by regulatory decisions are likely to pursue a range of strategies, including lobbying politicians and officials, regardless of the presence of merits review. Even so, the absence of merits review is likely to reduce the ability of politicians and officials to resist such pleading and direct them to the available formal appeal processes. A lack of merits review may provide politicians and officials with greater motive and opportunity to interfere in regulatory decisions than where there are formal processes to test the correctness of regulatory decisions.

F10.10 An absence of merits review increases the likelihood that aggrieved parties will seek recourse outside the legal system. In particular, it will encourage special pleading to politicians.

A greater understanding of the ability of aggrieved parties to test the reasonableness of decision through judicial review processes would improve the ability of politicians and officials to resist such special pleading. In late November 2013 a range of political parties made clear that there would be no parliamentary majority for legislating to overturn the Commerce Commission’s decision. Judicial review proceedings were filed in the High Court three days later.

Would merits review get regulators to make lawful and reasonable decisions, or follow a better process?

A misunderstanding about the scope and focus of judicial review was evident in some submissions. Some submitters argued that merits review would cause regulators to improve their decision-making processes in
the first instance. Some submitters also seem to believe that judicial review is concerned exclusively with the process of making a decision and ignores the substantive aspects of the decision making process and outcome. This is incorrect.

For example:

- the Insurance Council of New Zealand said that merits review would be “likely to induce a more considered and meaningful consultation process than occurs currently by the RBNZ, FMA and other regulators” (sub. 5, p. 5);

- Mortlock Consultants argued that merits review would allow a regulator’s decision to be challenged “on the grounds that is unreasonable or inconsistent with the statutory objectives, or that the regulator did not pay adequate attention to the concerns raised in the consultation process in relation to the matter.” (sub. 31, p. 10); and

- Genesis Energy supported merits review because “reasonable submissions are dismissed without good reasons” by the Electricity Authority (sub. 48, pp. 4-5).

These matters are all within the scope of judicial review. Goddard notes that “[j]udicial review is well equipped to … ensure that regulators follow a proper process consistent with the statutory framework under which they operate and the requirements of natural justice” (2006, p. 3). Often the courts set aside decisions of the Executive for procedural deficiencies, unlawfulness, or unreasonableness. A recent example of this is Board of Trustees of Phillipstown School v Minister of Education (2013), where a failure to provide a sufficiently detailed breakdown of the cost involved in safely rebuilding an earthquake-damaged school was sufficient for the court to conclude meaningful consultation had not taken place, and so set aside the Minister’s decision to close a school.

Would merits review sharpen the incentives on regulators to get it right?

Review of administrative decisions by courts appears to change the behaviour of regulators.67 The widespread application of judicial review and the relatively broad scrutiny possible under a claim of unreasonableness provides a strong incentive for regulators to “get the decision right”. The reputational risk from having decisions set aside motivates decision makers, following a proper process, to make good decisions that will be defensible in the face of judicial review.

A number of submitters argued that the broader scope of merits review provided even stronger incentives than judicial review. No evidence was forthcoming in the submissions as to why this would happen. The Commission has considered what empirical evidence might be available to test the question. Examining the rates of decisions being overturned on judicial review or appeal would not seem to provide a sound basis to test this assertion. If merits review did provide stronger ex ante incentives to make a good decision, then it might be expected that the access to merits review would lead to fewer judicial challenges. Indeed it might also be expected to lead to fewer successful challenges than in regimes with no access to merits review. But any comparison would be largely meaningless because of differences in the underlying capability of regulators, and in the means and motivation of regulated parties to challenge decisions.

The starting point is that, to the extent good decisions flow from good processes, judicial review already provides all the incentives that merits review might provide. As the Reserve Bank argued, “a good process leads to good regulatory outcomes, and regulated entities already have a remedy against inadequate processes” (sub. 9, p. 6).

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67 See for example the Judicial Review project in Australia discussed in Creyke & McMillan (2003).
Earlier the Commission found significant overlap between the scope of judicial review and appeals in practice. The scope of judicial review that will be considered by a judge in any given case varies on the facts and circumstances (see discussion in Section 10.2). Applicants naturally seek a broad scope of judicial review, working merits arguments under the head of unreasonableness. Judges vary in their willingness to entertain these arguments, but scope exists for the substantive merits to be considered in the course of a judicial review.

Importantly, the scope of potential judicial review that a regulator might be subject to is uncertain at the point the decision is made. Applicants will understandably seek to bring a substantive examination of the merits within the scope of a judicial review. And at times judges can and do undertake such an examination.

The degree to which a court will defer to a decision maker is uncertain. In *Lab Tests Auckland Ltd. v Auckland District Health Board*, Justice Hammond noted the “lack of an agreed classification or taxonomy, accompanied by properly developed substantive principles as to when a court will intervene by way of judicial review” (2009, at 380). Joseph has described the variable thresholds of review as the “selective raising and lowering of the review threshold” (2001, at 936). As noted above, courts are likely to defer to specialist regulators in highly complex fields. Yet most regulators take decisions that are subject to an uncertain degree of potential judicial review, and with a realistic prospect of a substantive examination of the merits of a decision.

Clearly, the trend away from the strong Wednesbury deference is continuing. The threat of judicial review with a wide scope that scrutinises the merits of a decision is not qualitatively different from the threat of merits review itself. So the incentives provided on the decision maker *ex ante* are of similar strength.

The uncertainty about the scope of review that might be applied is unlikely to dull the incentive. Regulators are concerned with their reputation. They want to take decisions that will be upheld.

Some submitters argued that the accountability to make good decisions would be lessened by the knowledge that a subsequent party would be the effective decision maker. The Electricity Authority noted, “the regulatory process risks becoming an entrée to the court process with parties restricting themselves to stating their points to get them on record as opposed to engaging fully and meaningfully to best meet the objectives of the regulator” (sub. 50, p. 5). Once a regulator knows that they are no longer actually the decision maker, then the regulator’s decision making could become only an information-gathering phase – the precursor to the real decision by the courts.

Are courts able to make “better” decisions than regulators?

Chorus submitted that “merits review recognises that regulatory decision makers will not always get it right” (sub. 51, p. 19). Regulators sometimes do make mistakes, as do courts.

Those may be errors on the part of the court, or they may be legitimate rulings on the part of the court which nevertheless, from an instrumentalist perspective, serve to undermine Parliament’s objectives in establishing a regulatory regime. Box 10.5 summarises a notable example explored in the Commission’s recent 2nd interim report on boosting productivity in the services sector. (2014)

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**Box 10.5**  
**Interpretation of section 36 of the Commerce Act 1986 by the New Zealand courts**

In its 2nd interim report on boosting productivity in the services sector, the Commission discussed s 36 of the Commerce Act 1986. Section 36 of the Commerce Act aims to prevent the taking advantage of substantial market power for an anticompetitive purpose. Taking advantage for such a purpose is also known as “monopolisation”.

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Anti-monopolisation provisions aim to prevent dominant firms in a market from harming competition and forestalling the benefits to consumers which flow from competition – efficiency and innovation. They are intended to allow large firms to compete, and indeed to do so vigorously, providing that in so doing they do not harm the competitive process.

New Zealand’s jurisprudence on s 36 developed through two Privy Council cases and a Supreme Court judgment in 2010 (the so-called 0867 case). In each case, the court found against the Commerce Commission’s contention that s 36 had been breached. The courts relied almost exclusively on the counterfactual test for determining whether the firm in question had “taken advantage” of its market power. The Supreme Court in 0867 noted:

Anyone asserting a breach of s 36 must establish there has been the necessary actual use (taking advantage) of market power. To do so it must be shown, on the balance of probabilities, that the firm in question would not have acted as it did in a workably competitive market, that is, if it had not been dominant. (Commerce Commission v Telecom Corporation of New Zealand Ltd, 2010, at 34)

The Commission agrees with the analysis that New Zealand jurisprudence on s 36, in relying almost solely on a counterfactual test, is unique among comparable countries. The intention in drafting s 36 had been to align New Zealand’s law with Australia’s. But the application of s 36 now differs from Australia’s approach (not without its own controversies), where jurisprudence and legislative amendments provide a range of tests for whether dominant firms are behaving to the detriment of competition in a market.

The Productivity Commission’s main concern is that the counterfactual test appears to be an inefficient rule that runs a high risk of false negatives (finding anticompetitive actions to be lawful) and some risk of false positives (finding legitimate actions to be unlawful). These are likely to result in costly errors for the economy.

Source: NZPC, 2014b; and Commerce Commission v Telecom Corporation of New Zealand Ltd (2010).

When the courts appear to interpret the law in a surprising way or in a way that appears to undermine the objectives of the regulatory regime, the legislative framework requires scrutiny.

R10.2 Where courts interpret legislation in ways that significantly alter a regulator’s understanding of their mandate, the department responsible for the regime should review that aspect of the legislation. Its review should ascertain whether the courts’ interpretation undermines Parliament’s objectives in establishing the regulatory regime, and whether legislative amendment is desirable.

Submitters argued that merits review of complex, technical regulatory decisions is desirable because judicial review is not “an enquiry into the underlying evidence, or whether another substantive decision should be preferred based on this evidence” (sub. 46 p. 12).

Vector argued that “due to the often factual and merit-based elements of [decisions about economic regulation], judicial review can be an inadequate mechanism to ensure high quality regulatory decisions and successful regulatory outcomes” (sub. 29, p. 14). However, in its 2008 review of the Commerce Act, the Ministry of Economic Development did not consider courts the appropriate body for appeals of economic regulation decisions: “There is a risk that the review of decisions about IMs are not suited for judicial decision-making since they relate to fact, rather than interpretation and application of the law” (MED RIS 2008, p. 49). For the Ministry, this led them to prefer using specialist tribunals rather than the courts to undertake merits review of these decisions. This option is discussed in more detail below.
New Zealand’s judiciary is widely regarded as independent, competent, and respected. A recent report by Transparency International New Zealand found the quality of the judiciary to be one of the strongest pillars in its framework of New Zealand’s “national integrity system” (2013).

Even so, in the course of its engagements, the Commission heard concerns expressed about the institutional capability of the courts to grapple with highly complex areas of regulation. In its submission, Powerco noted that “High Court judges can find [the specialist technical nature of many regulatory arrangements] difficult to comprehend fully, even with the assistance of specialist advisers” (sub. 14, p. 2).

Perhaps understandably, these sort of comments were expressed more strongly in the Commission’s engagement meetings than in the written submissions. These comments were not aimed at individual judges or the judiciary as a body, but the entirety of the court process. Comments included the degree of capability of senior barristers to accurately convey complex technical issues to the court, the lack of specialist technical support available to the court compared to the decision maker at first instance, and the procedural rules involved in appeals. The overwhelming sentiment expressed was one of sympathy towards the judges involved in hearing such appeals.

Even where it is likely that the court will correct an error, that may not lead inevitably to more preferable outcomes in terms of the objectives of regulation. As Yarrow et al note:

Whilst this argument might have at least some force if errors to be corrected were selected at random, that does not correspond to the factual situation. Interested parties can choose their grounds of appeal, and this leads to bias in which particular errors are corrected. Thus, by way of illustration of the general point, if errors leading to a higher determination of revenue are approximately balanced by errors leading to a lower determination of revenue, then the correction of errors on only one side of the divide would actually create bias in what had previously been a near-unbiased assessment. (2012b, p. 31)

Where there is an imbalance between regulated firms and the consumers/beneficiaries of regulation in their ability to challenge decisions, this paradox may be magnified.

**F10.13** Providing access to merits review may not always promote the objectives of a regulatory regime.

Having merits review available where it is likely to support the objectives of the regulatory regime requires designers of those regimes to consider critically whether:

- the appellate body has sufficient institutional capability, compared with the decision maker at first instance, to improve the outcomes of decisions in terms of the objectives of the regulatory regime (including, but not limited to, whether correcting an error is more likely than creating one);

- the total costs in providing access to merits review, including monetary costs, delays and uncertainty, justify the expected outcomes in terms of the objectives of the regulatory regime; and

- mechanisms are available that might support or mitigate these two considerations.

These considerations are consistent with the pragmatic approach recommended by the LAC guidelines. Designers need to consider whether providing access to merits review will create incentives for market participants to seek to improve regulatory outcomes through the courts, at disproportionate costs to the public.

**F10.14** Designers of new regulatory regimes need to consider whether to provide access to merits review. In areas of highly complex, technical regulation, designers need to critically assess whether the appellate body has the institutional capability, compared to the decision maker at first instance, to improve the quality of decisions in terms of Parliament’s objectives for the regulatory regime. They also need to take into account the costs and uncertainty created by providing access to merits review.
Will the incidence of appeals decline over time?

Finally, the Commission was told in engagement meetings that the number of merits review would decline over time as key areas of contention were clarified on appeal and precedents established to guide future resets. These arguments were made mainly in the context of the Commerce Commission’s determination of IMs. For example, in correspondence to the Commission, MBIE said that:

> With the recent release of the High Court’s merits review judgment, we are now well through this transitional bedding-in phase and anticipate a more settled period as we approach the end of the first complete regulatory cycle.

Inherent in this argument is an assumption that the legislative framework will remain relatively stable over a significant period of time.

Data and case summaries prepared in the course of the *Review of the Limited Merits Review regime* about appeals from decisions of the Australian Energy Regulator do not indicate that the frequency or complexity of appeals is declining (Figure 10.4).

**Figure 10.4** Number of appeals from the Australian Energy Regulator involving Weighted Average Cost of Capital (WACC)

![Graph showing number of appeals from 2007 to 2012](image)

*Source:* Yarrow et al., 2012a.

In the Commission’s view this argument that appeals are likely to decline over time underestimates the complexity of economic regulation generally and IM determinations in particular, where there will always be scope for new challenges. The argument also underestimates the strong incentive on regulated firms to try to seek more favourable determinations through the appeals process when there are large amounts of money at stake, and to seek to distinguish previous appeal decisions from the facts that give rise to new appeals.

> There is no reason to believe that the incidence or complexity of appeals in areas of highly complex or technical regulation will inevitably decline over time.

10.6 Do alternatives exist that might improve the likelihood of good merits review decisions?

In its submission, Mighty River Power said that “the nature and form of merits review requires careful attention to avoid protracted and costly legal engagements” (sub. 30, p. 10). A number of mechanisms might improve the institutional capability of appellate bodies to hear appeals on areas of highly complex, technical regulation.
Specialist court/tribunal

In its submission Vodafone argued in favour of a specialist tribunal to handle merits review of economic regulation. Recognising that a permanent standing tribunal would “involve significant costs, and may only rarely have a full workload … it makes sense for it to be constituted when required using, as far as possible, resources that are already available within the New Zealand courts system” (sub. 46, p. 15). Such a model has also previously been advocated by Goddard:

We cannot justify a permanent specialist review body – but that is not what is required. We can in my view put together, on an ad hoc basis, a review body that would collectively bring to bear the relevant expertise, and would be well equipped to carry out merits reviews of decisions of the Commerce Commission, Electricity Commission, Securities Commission and possibly other bodies. The Commerce Act provides a model: a Judge, sitting with one or more lay members. (2006, p. 16)

Such a tribunal was considered following the 2008 review of the Commerce Act. Cabinet advice at the time noted that while such a tribunal or panel might allow for more tailored expertise and deliver faster decisions than the High Court, it also carried with it a high risk of further appeals, a heightened perception of political involvement (particularly in selecting Tribunal members), and increased difficulty in managing conflicts of interest (Minister of Commerce & Minister of Energy, 2008, p.8).

As the Ministry of Justice advised in the Cabinet paper following the 2008 review:

The Ministry considers that review decisions about input methodologies are not suited for judicial decision-making since they relate to fact, rather than interpretation and application of the law. There may also be difficulties in assigning judges with specialist knowledge in this area. (Minister of Commerce & Minister of Energy, 2008, p. 9)

The concerns about perceived political involvement in selecting panel members and conflicts of interest may be overstated given the regard with which lay members appear to be held. Additional safeguards in appointing panel members could prevent political abuse. Such tribunals appear attractive given that they might more easily lend themselves to a more inquisitorial process, and the body could be provided with greater in-house specialist expertise to help it than is provided for in a traditional court structure. Care would need to be taken to protect the independence of such a tribunal, including ensuring it was resourced sufficiently to hear merits reviews.

Such a tribunal would be subject to judicial review in discharge of its functions, but in so doing a court will generally only intervene for material error of law, bad faith, breach of natural justice, or Wednesbury unreasonableness (Unison Network Ltd v Commerce Commission, 2007, at 55; and Z v Dental Complaints Assessment Committee, 2008, at 139).

Different procedural rules

There were a number of suggestions of how different procedural rules could enhance the merits review of highly complex and technical regulatory regimes.

A more inquisitorial approach

The first suggestion would be to allow a more inquisitorial approach. The New Zealand Airports Association noted,

It is also important to ensure that the appeal forum has the appropriate expertise and procedural flexibility to handle the challenges that come from a factual appeal against very technical and detailed decisions. For example, it may be appropriate for a decision-maker on appeal (whether the Court or an expert panel) to be empowered to adopt an inquisitorial role where this will assist with the efficient and just determination of the issues on appeal. (sub. 33, pp. 15-16)

For example, where there are restrictions on the provision of new evidence, it still may be desirable to allow the court to examine parties’ expert witnesses to help the court gain a thorough understanding of the issues and arguments. This process should not extend to letting parties cross-examine each other’s expert witnesses, to avoid undermining the inquisitorial approach.
In the course of the inquiry engagement the Commission was told about the benefits of “hot-tubbing” in relation to the Commerce Act. Hot-tubbing provides for different parties’ experts (usually economists) to gather before or during a trial, with the aim of trying to reach agreement between the experts, or to better clarify areas of disagreement. Such processes would seem to help a court understand highly complex and technical issues.

Is a frozen record helpful?
As noted above, appeals against Commerce Commission determinations relating to IMs take place on the basis of the information that was before the Commerce Commission when it made its decisions: a closed or frozen record. In the recent IM appeal, the court noted that “as matters transpire, the [closed record] provision gives rise to little controversy in these appeals” (Wellington International Airport Ltd & Ors v Commerce Commission, 2013 at 176).

The stated justification for this restriction is to prevent gaming by parties. It would be undesirable for regulated firms (or the Commerce Commission) to withhold material from consideration only to deploy it later during an appeal.

In its inquiry into local government regulation, the Commission was sceptical about the widely held view that the availability of de novo appeals to the Environment Court encouraged participants in local authority processes under the Resource Management Act 1991 to “keep their powder dry” by holding back information until the appeal stage. The Commission noted that parties would not pay to create expert information until they knew it would be required, and that the success of mediation processes indicated that parties took a constructive approach (NZPC, 2013a, pp. 159-63).

In the case of economic regulation the stakes are higher. New Zealand Airports submitted that the frozen record means that at times the court is discussing what might happen in a hypothetical future, when there is existing information about what did happen not available to it (sub. 33). But the purpose of economic regulation is to regulate prices and quality over a defined period of time in markets where there is no realistic prospect of competition. This involves making predictions about the future based on imperfect information. It would be undesirable for emerging facts to influence a firm’s incentives, when the objective of the regime is to promote certainty over the regulated period. This is particularly so where firms will only be incentivised to appeal when the emerging facts are favourable to their arguments.

On the other hand, the frozen record may create a different set of problems. While it exists to prevent gaming, it may drive other perverse behaviour – an obsession with getting things on the record, not so they can be considered by the regulator, but so they are available to the court on appeal. In its submission the Commerce Commission noted that in the case of its 2010 decision around IMs, it received a submission a few days before the statutory deadline for its final determination (sub. 44). Such submissions are clearly intended to be available on appeal rather than to influence the primary decision. Inevitably the Commerce Commission feels compelled to also get its response to such submissions on the frozen record. The substantial appeals about IMs were delayed by significant litigation about the composition of the frozen record. The frozen record appears to front-load the cost and effort involved in creating the material that will be considered on appeal, rather than substantially making the process simpler or cheaper for the Commission or other parties.

It may be that, in a more inquisitorial process, an appellate body could exercise more discretion over the admissibility of new evidence in a way which could reduce delay and costs involved in the merits review. In engagement meetings the Commission was told that the Australian Competition Tribunal would often discount newly introduced evidence, if it thought that the evidence ought to have been provided to inform the initial decision. Broad discretion over cost awards could also discourage gaming.
Providing courts or tribunals discretion over the admissibility of new evidence is likely to be more efficient than providing for appeals based on a frozen record.

Different thresholds of appeal

Appeals against IM determinations must demonstrate that an alternative is “materially better”. Such thresholds may seek to deter marginal appeals, but they create additional scope for litigation.

While on balance it may be desirable to deter marginal appeals, such thresholds should not be intended to compensate for deficiencies in the institutional capability of the appellate body. If there is doubt about the ability of the body to correctly identify a preferable or better decision than the regulator, then there is no reason to suppose it is in a better position to correctly identify a significantly preferable or materially better decision.

Lay members and specialisation

As the Commission noted in its issues paper, the Commerce Act 1986, Human Rights Act 1993, and Land Valuation Proceedings Act 1948 provide for lay members to be appointed as members of the High Court, which provide specialist expertise in cases relating to those Acts. High Courts judges have the discretion to appoint lay members to particular cases. But once a lay member has been appointed to a case, that member becomes a member of the court for the purposes of that case.

In the course of the inquiry engagement, there was a uniformly positive view expressed about the role played by lay members in hearing Commerce Act cases. There are currently 15 lay members appointed by the Governor-General on the advice of ministers in recognition of their particular expertise in industry, commerce, economics, law or accountancy. Of the 15 lay members, 8 are New Zealanders and 7 are Australians, including three members of the Australian Competition Tribunal.

The regard in which they are held illustrates that the concerns discussed earlier around appointments to a specialist tribunal may be overstated. It also shows the value that those involved in Commerce Act litigation place on specialist expertise.

Some guidance from the Treasury suggests the presumption in designing regulatory regimes should be that appeals are heard by relevant experts:

> Appeal bodies should generally be comprised of experts in the relevant subject area. The more specialised or technical the subject area the more important it will be for the appeal body to include the relevant subject or technical experts. The more likely it is the appeal will involve legal issues the greater will be the need to have at least one person on the appeal body with some legal expertise. There are a range of choices as to the nature of the appeal and whether it is limited in some way, and the applicable appeal procedure (usually a choice of a re-hearing of some matters vs an entirely new hearing of the matter). (New Zealand Treasury, 2013a, p. 69)

The issue of judicial specialisation was discussed in a Law Commission report Review of the Judicature Act 1908, discussed in Box 10.6.

Box 10.6 The Law Commission on the Commercial List and specialisation in the High Court

The 2012 Law Commission report on Review of the Judicature Act 1908 discusses “what should be done about the existing Commercial List of the High Court” as well as “how far, if at all, should some form of judicial specialisation be effected in the High Court of New Zealand?” (pp. 99-116)

The report is careful to note the importance of the High Court’s general jurisdiction, and particularly its constitutional role in exercising judicial review.

The Commercial List was established as a pilot in 1987, and formalised in 1991, to provide a list of judges to deal with pre-trial matters in commercial litigation, to assist in the timely and effective progress of commercial litigation.
Trying to achieve consistent high performance is very hard when the pool of specialist people is small and the breadth of their work is large. There are advantages in having a pool of people doing particular types of review frequently so that they can develop expertise.

As at 1 August 2013, New Zealand had only 36 High Court judges, with 1 acting judge and 8 associate judges. Given the small size of the judiciary, a significant degree of specialisation appears unfeasible. Without reliable data it is hard to assess whether sufficient work exists to justify an administrative panel to provide a degree of specialisation in administrative law cases in New Zealand.

**Alternative dispute resolution**

In its report on housing affordability (2012), the Commission noted that less formal alternative dispute resolution processes were likely to be less expensive, more accessible and faster than court processes. But the Commission cautioned that their outcomes may have less authority and so provide weaker incentives on decision makers (in that case, local government bodies).

Alternative dispute resolution mechanisms are a feature of a number of regulatory regimes, including:

- Animal Products Act 1999, s. 118
- Education Act 1989, s. 10
- Employment Relations Act 2000, ss. 144-155
- Gas Act 1992, s. 53D
- Health and Disability Commissioner Act 1994, s. 61
- Human Rights Act 1993, s. 77
- Privacy Act 1993, ss. 74 and 76
Even so, most of these dispute resolution processes deal with disputes between the public and regulated parties (such as between consumers and retirement villages, or consumers and gas distributors), or to resolve disputes about levies on regulated firms (under the Animal Products Act and Wine Act).

Only the Education Act provides for a disputes resolution process to challenge the decision of a regulator: specifically, a determination by the Secretary of Education that a young person with special education needs should be required to attend a particular state school, special school, special class, or special clinic.

By their nature, regulators’ decisions are unlikely to be suited to negotiated outcomes. This could compromise the independence of the regulator and encourage special pleading. Even so, the Commission has previously commented positively on the dispute resolution provisions available under the Resource Management Act 1991 (schedule 1, clause 8AA), and suggested similar procedures could be applied to the Local Government Act 2002 (in the context of disputes about developer charges).

**Q10.4** What benefits and risks are there in providing for alternative dispute resolution mechanisms as a way of reviewing regulatory decisions?

**Foreign expertise in reviewing decisions**

New Zealand’s small size and associated difficulties in sourcing specialist expertise means that foreign expertise can improve the capability of appellate bodies in areas of complex regulation. The Australian lay members are perceived as bringing valuable expertise in Commerce Act cases.

Recourse to Australian or joint trans-Tasman appellate tribunals may be desirable in some areas of regulation, given the desirability of harmonising regimes to promote trade and investment.

Box 10.7 describes how review and appeal of regulatory decisions might work in the proposed Australia New Zealand Therapeutic Products Agency (ANZTPA).

**Box 10.7 Proposed review of decisions by an Australia New Zealand Therapeutic Products Agency**

The proposed ANZTPA has been in development since the signing of a treaty between the governments of Australia and New Zealand in 2003. It would be the first truly joint regulator, with oversight of most medicines and therapeutic products in both countries.

It is anticipated that review of decisions by ANZTPA would be provided for through a range of mechanisms, including:

- internal review within ANZTPA;
- merits review to one of two tribunals, established in each country and exercising identical jurisdiction (with members drawn from a common pool of persons appointed by the Ministerial Council);
- judicial review as provided for in each country; and
- appeals on questions of law to the superior court of each country – in New Zealand to the High Court.

A 2013 discussion document described how the review of decisions by ANZTPA would work:

There will be the ability for an applicant or person affected by a decision of ANZTPA to seek a
Many regulatory regimes will be unsuited to decision review by a foreign or international tribunal. The joint report between the Australian and New Zealand Productivity Commissions in 2012 noted the challenges with regulatory harmonisation generally:

Implementing agreements to reduce behind-the-border barriers—typically regulatory in nature—is more complicated than reducing tariffs. Work programs have taken many years in some cases. For example, the first consultation paper on establishing a joint therapeutic products agency was released in 2000, yet the new agency is not due to be operational until 2016. In other areas—such as a mooted merger of stock exchanges and the integration of banking supervision and competition policy regimes—deeper integration has not been achieved. (APC & NZPC, 2012, pp. 5-6)

Even so, New Zealand should continue to seek opportunities to provide for input from foreign experts in areas of complex and highly technical regulation.

Foreign expertise can play a valuable role in bringing expertise to merits review of highly complex and technical regulatory regimes.

10.7 What is the Commission’s guidance on review and appeal in regulatory regimes?

Merits review should be available where it is likely to contribute positively to the objectives of regulation, taking into account the issues noted by the LAC:

- cost;
- delay;
- significance of the subject matter;
- competence and expertise of the decision maker at first instance; and
- need for finality.

If regulatory decisions are plotted along a scale of complexity, then trivial and mundane decisions are less likely to require access to merits review; and extremely complex decisions may be less likely to benefit from access to merits review. It is the vast bulk of decisions in the middle of that spectrum that are most likely to be improved by access to merits review (Figure 10.5).

The Reserve Bank of New Zealand makes this point in its submission. It argues that its proposed powers under the Non-bank Deposit Takers Bill to determine whether an individual is a fit and proper person to be a director or senior officer of a non-bank deposit taker are amenable to merits review. By contrast, prudential regulation is “inhomogeneously technical and judges do not usually have that technical or industry expertise” (sub. 9, pp. 5-6). The Electricity Authority also argued that “electricity industry disputes are often complex and technical, requiring specialised electrical engineering or economic knowledge or both” (sub. 50, p. 5).

The Commission has not formed a view on the whether merits review should be provided in these or any other specific regulatory regimes, or what the form and process of any merits review should be. But in areas
of highly complex and technical regulation, designers of regulatory regimes should critically assess whether courts have sufficient expertise or institutional capability, relative to the decision maker at first instance, to be confident that merits review would likely improve the desired regulatory outcomes.

This assessment should include considering what mechanisms could be used to support the capability of the appellate body. Minter Ellison Rudd Watts thought that:

> [t]here can be benefits in having an expert body developing expertise over a range of similar decisions, particularly in a highly technical field. There can also be benefits in a more streamlined process, for example, if the courts conducted a more inquisitorial process to speed up the production of evidence. These changes could be achieved within the existing court system or by creating a dedicated appeals body. (sub. 28, pp. 33-34)

**Figure 10.5** When is merits review likely to be appropriate?

Determining whether appeals should be provided for is highly circumstantial. It will necessarily entail forming a robust view about the capability – or in the case of a new regulator, the likely capability – of the decision maker at first instance, and the capability and expertise of the appellate body.

Making such an assessment is fraught. Regulated firms often have a natural incentive to criticise a regulator. A firm faces minimal costs by advocating for the availability of merits review. Where there are large sums of money are at stake for firms, then choosing to appeal, even at great expense, may be a relatively small investment for the prospect (from their perspective) of a better result. Providing access to merits review will not always be appropriate.

The corollary of not providing appeals is that it heightens the importance of effective processes to review the performance of regulators and regulatory regimes, so that monitors can independently assess the quality of regulatory decisions. This is discussed in greater detail in Chapter 14, which focuses on accountability and performance monitoring.
11 Regulator practice

Key points

• Successful implementation of a regulatory regime depends on the regulator’s strategies, tools and methods.

• Regulators around the world, including in New Zealand, have drawn heavily on theory in designing compliance and enforcement strategies, tools and methods. In particular, regulators have tended to adopt responsive regulation approaches or risk-based approaches.
  - In responsive regulation approaches regulators select their compliance tool based on the attitude of regulated firms towards compliance. For firms willing to do the right thing, the regulator may select a low-cost tool (such as education); for firms unwilling to comply, the regulator may select high-powered tools (such as prosecutions).
  - In risk-based approaches regulators focus on identifying and assessing the risk of harm from non-compliance and target their resources towards reducing the greatest harms.

• Official guidance in New Zealand endorses both risk-based and responsive approaches.

• Both responsive and risk-based approaches are evident in the strategies of New Zealand regulators, although agencies differ on how far they prioritise reducing harm or maximising compliance, and to what extent the two objectives are integrated or treated separately.

• In practice, implementation of either approach has involved considerable challenges, including that:
  - regulators can face barriers to using high-powered tools, such as prosecutions; and
  - a risk-based approach does not necessarily solve the issue of what risks to prioritise, how to deploy regulator resources, or what enforcement tool to use.

• As a result of these challenges, regulatory scholars Robert Baldwin and Julia Black have developed the concept of really responsive regulation – a more nuanced institutional approach, which sees regulators being attentive and responsive to a broad range of factors in undertaking their regulatory practices.

• There is evidence that some New Zealand regulators are demonstrating elements of the really responsive approach. However, evidence also suggests that New Zealand regulators are not paying enough attention to how their regimes perform over time.

• Regulating is a deeply challenging task. More effective, and consistently effective, practice in New Zealand will require greater sharing of experience and practice between regulators and more detailed and targeted guidance about regulatory practice. The Commission therefore recommends that:
  - regulator networks or forums be formally recognised through partial government funding, tied to a business case and performance measures;
  - Cabinet’s Expectations for Regulatory Stewardship is revised to clarify that regulators should seek to raise their own, and the wider sector’s, performance by sharing experience; and
  - regulators are provided with more sophisticated guidance to reflect developments in the theory of regulatory practice.
11.1 Introduction

A central concern in the design of a regulatory regime is ensuring its effective implementation and administration, so that the intent of the regime is met. However, the approach taken to monitoring, enforcement and operational compliance activity is typically left to the expert discretion of the regulator. Successful implementation of regulatory regimes will depend on the regulator’s strategies, tools and methods.

This chapter is about effective regulator practice. Many of the influences that shape what regulators do in practice are covered elsewhere in the report. For example, Chapter 5 investigates the importance of the choice of institutional form and the governance of the regulator, Chapter 7 focuses on the influence of organisational culture and leadership, Chapter 12 discusses workforce capability, Chapter 13 examines the funding arrangements, and Chapter 14 sets out the accountability and performance frameworks of regulators.

This chapter starts by examining the theories that have been influential in determining the strategies that regulators use to detect and manage harm, intervene, and enforce compliance. The chapter also highlights the issues and challenges that regulators face in putting theory into practice. The operational practices of regulators in New Zealand and some of the particular challenges in the New Zealand context are examined. The chapter concludes with suggestions for further development of guidance to help regulators think about their regulatory practices in a deliberate, reflective and adaptive way.

The chapter is set out as follows:

- Section 11.2 outlines developments in the theory of regulatory practice – the role of the regulator in the regulatory regime, the different attributes and motivations of regulated parties, the strategies the regulator should use to achieve the objectives of the regulatory regime (this section also outlines the challenges, identified in the literature, in putting theory into practice);
- Section 11.4 examines the operational practices of regulators in New Zealand, the challenges they face, the extent to which New Zealand regulators have adopted regulatory approaches and strategies consistent with current theory, and the guidance available to help them; and
- Section 11.5 suggests areas for further guidance and help for regulators in adopting effective regulatory practices.

11.2 Developments in the theory of regulatory practice

Developments in the theoretical literature on regulatory practice have been influential in contemporary thinking about the role of the regulator and the strategies they should use to achieve the objectives of regulation. This literature has increasingly highlighted and sought solutions to the issues and challenges that regulators face in putting theory into practice.

**Compliance versus deterrence**

In the early literature the two main models for achieving regulatory objectives were the compliance model and the deterrence model. The compliance model used the tools of persuasion and building trust and relied on an ongoing working relationship between the regulator and regulated parties. The deterrence model described an arm’s length regulatory strategy in which regulated parties were required to meet regulatory requirements or face punitive sanctions (Reiss, 1984).

The key difference between these two models is the assumed motivations of regulatees. The compliance model assumes that most people want to do the right thing in complying with regulations, but strategies by the regulator are still needed to help people comply. The deterrence model assumes that people weigh up the costs and benefits of breaching a regulation. The higher the likelihood of detection and the higher the punishment, the higher the cost of non-compliance and the more likely the costs of non-compliance will outweigh the benefits. The regulator uses its detection and enforcement strategies to influence the regulated parties’ costs and benefits of compliance (Becker, 1968; Stigler, 1970).
Responsive regulation

In the 1990s it became increasingly recognised that regulators needed a range of tools so that they could respond contingently to the attitude and conduct of regulated parties – cooperatively to cooperative regulatees and punitively to recalcitrant regulatees. Ian Ayres and John Braithwaite’s Responsive Regulation (1992) has been an important influence in the thinking about effective regulatory compliance over the last two decades (Etienne, 2013).

Scholtz’s “tit-for-tat” strategy was an early model of responsive regulation (Scholtz, 1984). The game theoretic model assumes a rational economic actor, motivated solely by profit maximisation, in an ongoing regulatory relationship with a regulator. The regulatee reaps benefits over the long term by foregoing short-term opportunities to default in favour of consistent cooperation with the regulator. The regulator can optimise the long-term cooperation of regulated parties by setting a minimal level of compliance, and using cooperative strategies with regulatees that do comply and punitive strategies against those that do not comply. The regulator will return promptly to a cooperative approach once a regulatee that is not complying signals they are willing to comply.

Ayres and Braithwaite (1992) undertook empirical research into a wide range of industries, exploring the dynamic interactions between regulators and regulated firms. Their findings supported “tit-for-tat” strategies for effective regulatory compliance. They developed an “enforcement pyramid” of regulatory tools, with a broad base of cooperative measures and increasingly punitive measures for non-compliance. The operating strategy of the regulator is to start at the base of the pyramid, seek compliance through persuasion and escalate up the pyramid when compliance is not forthcoming. Importantly, efforts of the regulatee to comply are met with regulatory de-escalation down the pyramid (Box 11.1).

<table>
<thead>
<tr>
<th>Attitude to Compliance</th>
<th>Compliance Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have decided not to comply</td>
<td>Use full force of the law (e.g. prosecutions, imprisonment, maximum fines, banning activities)</td>
</tr>
<tr>
<td>Don’t want to comply</td>
<td>Deter by detection (e.g. fines, warning letters, abatement notices)</td>
</tr>
<tr>
<td>Try to, but don’t always succeed</td>
<td>Assist to comply (e.g. guidance material, education programmes)</td>
</tr>
<tr>
<td>Willing to do the right thing</td>
<td>Make it easy (e.g. one-stop-shops, online forms)</td>
</tr>
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</table>

Box 11.1 An application of an enforcement pyramid

At the base of the pyramid, compliance is encouraged by appealing to an individual’s social responsibility and leveraging cooperative approaches. This level recognises that most people want to do the right thing by complying with regulations. For these people, the ideal strategy is to make compliance as easy as possible such as implementing online application processes or having convenient opening hours for lodging paperwork.

Further up the pyramid are people who are willing to comply with regulations, but, for whatever reason, do not always succeed. These people need help to comply by, for example, providing guidance material or education programmes. Still further up the pyramid are those who do not want to comply. For these people, the strategy escalates to a deterrent threat (warning letters, fines, publicity around successful prosecutions). These actions appeal to an individual’s rational self-interest. Finally, at the top of the pyramid are a small number of individuals who decide not to comply. These people should face the full force of the law (Ayres & Braithwaite, 1992).
Ayres and Braithwaite (1992) summarise the important insights to consider when examining the efficiency and effectiveness of compliance regimes.

- A complex set of economic, psychological and sociological factors underpins regulatory compliance decisions. Individuals and firms have different motivations based on values, social responsibility, economic rationality and the desire or need to follow the law. These motivations play out in different contexts and situations.

- Some individuals and firms will comply with the law if it is economically rational for them to do so. Most individuals and firms will comply with the law most of the time simply because it is the law.

- A strategy based totally on persuasion will be exploited when actors are motivated by economic rationality.

- A strategy based totally on punishment will undermine the goodwill of actors when they are motivated by a sense of responsibility.

- Punishment is expensive; persuasion is cheap. A strategy based mostly on punishment wastes resources on litigation that would be better spent on monitoring and persuasion.

- A strategy based mostly on punishment fosters organised resistance by business and industry to regulation.

- Voluntary compliance is most likely when a regulator displays and applies an explicit enforcement pyramid with a hierarchy of graduated responses to non-compliance, moving to more coercive measures only when less coercive means fail.

### Challenges in implementing a responsive approach

According to Etienne (2013), responsive regulation places heavy reliance on the regulator – “not just any regulator but a skilled and resourceful one, presumably capable and willing to push regulatees into compliance by making good use of discretion and judgement” (p. 14). However, Baldwin and Black (2008) have pointed to real difficulties in practically applying the responsive approach. For example, the responsive model assumes that regulators will be able to move smoothly up and down the enforcement pyramid, picking the appropriate compliance strategy to suit the attitude of the individual or firm, but enforcers may be excessively tied to compliance approaches for a number of reasons, including their own organisational resources, tools, cultures and practices and the constraints of the broader institutional environment … it may lack the necessary information to judge the need to escalate its response and it may be disinclined to escalate unless it has sufficient evidence to make a case for the highest level of response (eg to prosecute or disqualify). There may also be legal problems in applying a responsive approach. (p. 64)

The particular issue that regulators face in using the top of the responsive/enforcement pyramid – prosecuting a breach through the courts – is outlined in more detail in Box 11.2.

### Box 11.2 Barriers to taking prosecutions

A number of institutional/structural factors may dissuade regulators from moving to the top end of the pyramid and taking prosecutions. The key factors are:

- the evidentiary requirements for prosecutions;
- reputational risks in taking prosecutions;
- the time and resources involved in pursuing prosecutions;
- the public interest in prosecutions; and
- timeliness.
Mascini (2013), in a special issue of the journal *Regulation and Governance* devoted to the appraisal of 20 years of responsive regulation, concludes that institutional impediments have posed enormous challenges to implementing the enforcement pyramid, making it almost impossible for the responsive regulator to use the responsive approach to apply suitable enforcement:

Communication problems between regulators and regulatees, as well as institutional impediments, pose difficult challenges to the implementation of the enforcement pyramid. Miscommunication can result from ambiguous, infrequent, and interrupted contacts between regulators and regulatees, from the lack of organizational or legal infrastructure or because of political or economic pressure rendering it impossible to apply the enforcement style deemed most suitable. (p. 53)

**Risk-based regulation**

While the responsive model of regulation focuses on the compliance and enforcement strategy of the regulator, risk-based regulation focuses on identifying and assessing the risk of harm, and on channelling resources to modify or reduce harm.
Sparrow’s regulator is a “saboteur” of harm (Sparrow, 2000; 2010). The regulator develops ways to tackle particular problems rather than being driven by legislative prescriptions or by following operational manuals. The regulator targets key risks and defines them precisely, implements a plan to deal with them, measures performance, and adjusts the strategy on the basis of the assessment outcome.

Risk-based regulation has been characterised as a cycle, with a strong focus on monitoring performance and evaluating outcomes (Figure 11.1).

Risk-based regulation has found favour with governments and business, and has been dominant in regulatory reform initiatives, because it offers a framework that relates the activities of the regulator directly to the objectives of the regulatory regime (Hampton, 2005). Further,

[...] in its idealized form, risk-based regulation offers an evidenced-based means of targeting the use of resources and of prioritizing attention to the highest risks in accordance with a transparent, systematic, and defensible framework. (Black & Baldwin, 2010, p. 181)

Figure 11.1  Characterisation of a risk-based approach

Operating context

- Identify risks
- Assess & prioritise risks
- Analyse behaviours (causes, options for treatment)
- Determine intervention strategies
- Plan & implement strategies
- Monitor performance against plan
- Evaluate outcomes

Source:  Adapted from Organisation for Economic Co-operation and Development (OECD), 2004a.

However, adopting a risk-based regulatory approach presents significant issues for the regulator that challenges the notion that it provides “an evidence-based means of targeting resources” or a defensible framework for undertaking enforcement activity.

**Challenges for the risk-based regulator**

Adopting a risk-based approach to regulation requires the regulator to:

- deal with uncertainty about risk;
- operate in a political and public environment where there may be very different perceptions of risk and a poor understanding of what it means for the regulator to take a risk-based approach;
- make risk assessments and decide how to allocate its resources; and
- decide what approach it will take to enforcement once a risk assessment has been made.

**Evidence and the nature of the risk**

In many cases, what the regulator faces is uncertainty about the nature of the risk and the potential for the harm that may be caused. Low-frequency but high-consequence events in particular are hard to assess. In addition, focusing on large risks can overlook smaller risks that can accumulate into a significant threat. And because risk-based approaches tend to focus on known or familiar risks, regulators can fail to detect new and emerging risks and risk-creators that may be “off the radar” (Black & Baldwin, 2010; 2012).
Public and political perception of risk and risk-based regulation

Public perceptions of risk (sometimes amplified by the media) can place pressure on regulators to increase monitoring above the level suggested by an objective risk assessment. In other cases, the public perception of risk can be lower than identified by the regulator, leading to the perception that the regulator is being over zealous. Ex ante and ex post perceptions of risk can be very different. Politicians and the public may have a limited understanding that some risks will be prioritised and some risks might not be monitored. There can be a perception that the regulator is not doing its job, or that if the risk is not monitored then it should not be regulated. There may be a lack of understanding of the distinction between the inherent risks arising from the nature of the regulated activity and how risk is being managed by the regulated party, leading to charges that the regime is unfair or inequitable in its treatment of regulatees (Black & Baldwin, 2010).

Allocation of resources

Black and Baldwin (2010) argue that while risk assessments can identify the most high-risk activities or firms, they cannot be used to allocate the regulator’s resources. Regulators who focus on highest-risk events can lose sight of the need to achieve the greatest risk reduction for the given level of enforcement expenditure:

Even on a relatively simple matter such as the identification of the largest risks, risk-based regulation per se tells us only a limited amount about the costs of securing risk reductions or whether objectives are best furthered by targeting analyses at individual risk creators, particular types of risk, particular industrial sectors, certain systemic risks, or some other focus. (p. 193)

Indeed, there may be greater net benefit from spending a limited enforcement budget on reducing numerous smaller risks.

Approach to enforcement

A simple assessment of risk does not, of itself, tell the regulator where to allocate its resources. It also does not provide a guide to the type of enforcement action that should be undertaken:

A firm may, for instance, be given a high risk score because of the inherent risks it poses and because its management’s slack attitudes are reflected in a failure to manage risks well. This risk score may indicate a degree of urgency with which some regulatory intervention has to be made, but the firm’s high risk score does not indicate, in itself, whether the best way to reduce the risks posed by the firm is to use a command-and-control regime applied in, say, a deterrence fashion, or whether an incentive-based, educative, escalating sanctions, or disclosure strategy would prove more effective. The kind of intervention required may at best be loosely linked to the level of risk the firm presents. (Black and Baldwin, 2010, pp. 189-90)

At first blush it appears that the responsive enforcement pyramid might provide guidance to the risk-based regulator about the types of enforcement and compliance tools to apply. Gunningham (2010) suggests that

... a pyramidal response might be applied to enterprises that had first been targeted on the basis of a risk assessment. (p. 129)

Black and Baldwin (2012) disagree. They argue that

[a] disconnect … exists between the risk-based categorization of sites and activities, which … is meant to drive resource allocation, and the predominantly behaviour-based approach of the enforcement manuals, and indeed the preponderance of the literature on compliance and enforcement. There is, furthermore, a strategic gap between the risk-based assessment process and the enforcement process, with comparatively little development of strategies that might occupy the operational middle ground between these two stages of assessment and formal enforcement action. (p. 133)

Responsive and risk-based regulatory approaches – summing up

The theoretical landscape has been dominated for almost two decades by Ayres and Braithwaite’s responsive regulatory pyramid, which focuses on the behaviour of regulated parties and a range of enforcement tools for achieving compliance. The last decade has seen the emergence of risk-based regulation which focuses on identifying and assessing risk, and on allocating resources to modify or reduce the risk of harm.
The literature has increasingly recognised that both approaches present considerable practical challenges for regulators. Indeed, after 20 years of responsive regulation it appears that it is enormously challenging – indeed nearly impossible – in practice, for the responsive regulator to apply enforcement according to the responsive approach. The outlook for risk-based regulation is similarly discouraging. The promise that risk-based regulation would better align compliance activity with the objectives of regulatory regimes, and offer an evidenced-based means of targeting the use of resources, founders on the challenges posed by uncertain probabilities and outcomes, differing public and political perceptions about risk, and the realisation that allocating resources to risk reduction is not a simple task.

How a regulator meets the objectives of its regulatory regime requires that prioritisation decisions be made about deploying regulatory resources – what risks will be targeted and how. As a practical reality, it needs to be acknowledged that neither elimination of risk nor total compliance is achievable. Indeed, “zero risk is unattainable and undesirable” (Better Regulation Commission, 2006). Allocating resources to reduce risk and achieve compliance are prioritisation questions that the regulator must solve in a dynamic regulatory environment where there may be complex incentives and institutional constraints operating on both regulators and regulated parties. The following section describes a framework that has been designed to help regulators with these implementation challenges.

Twenty years of responsive regulation in practice has demonstrated that institutional impediments have posed enormous challenges to the real-world implementation of the enforcement pyramid.

Putting risk-based regulation into practice poses considerable challenges for regulators. Adopting a risk-based approach to regulation requires the regulator to:

- deal with uncertainty about risk;
- operate in a political and public environment where there may be very different perceptions of risk and a poor understanding of what it means for the regulator to take a risk-based approach;
- make risk assessments and decide how to allocate its resources; and
- decide what approach it will take to enforcement once a risk assessment has been made.

A risk-based regulatory approach does not necessarily solve the issue of what risks to prioritise, how to deploy regulator resources, or what enforcement strategy to use.

Really responsive regulation (and really responsive risk-based regulation)

The need for a really responsive approach to regulation came out of the growing recognition of the challenges regulators faced in putting the enforcement pyramid into practice (Baldwin & Black, 2008). However, following the requirement that regulators in the United Kingdom develop and use risk-based frameworks for organising their regulatory activities (Department for Business, Enterprise and Regulatory

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68 A notable feature of recent theoretical work is its grounding in actual practice. This is a feature of the work of researchers Julia Black and Robert Baldwin (London School of Economics and Political Science), but also of the work of other researchers such as Henry Rothstein and John Downer (King's College, London and Stanford University respectively). Rothstein and Downer, for example, studied the risk-based policy making of the UK Department for the Environment, Food and Rural Affairs by embedding a researcher within the department for 8 months to observe and interview staff (Rothstein & Downer, 2012).
Reform, 2007), Black and Baldwin (2010) considered whether the really responsive approach would also help regulators put risk-based regulation into practice:

This widespread endorsement of risk-based regulation prompts us to consider how risk-based regulators can attune the logics of risk analyses to the complex problems and the dynamics of real-life regulatory scenarios. (p. 182)

Black and Baldwin (2010) were further prompted to examine the implementation challenges of risk-based regulation following the Global Financial Crisis, which highlighted the difficulties for regulators working in a globally interconnected market and an international institutional environment:

A further prompting to re-examine the implementation challenges of risk-based regulation comes in the wake of the 2007–2009 credit crisis and stems from the widespread perception that risk-based regulation, at least in the UK, signally failed to protect consumers and the public from the catastrophic failure of the banking system. This decline in the reputation of the UK’s risk-based approach to financial regulation, together with the experiences of other regulators who have adopted risk-based approaches, presses us to examine whether there is a need to apply risk-based regulation in a newly reflective manner and to conceive of it in a more nuanced way. (p. 182)

Really responsive regulation recognises that a number of factors influence the behaviour of regulators and regulated parties and ultimately the effectiveness of regulation. To be really responsive, a more sophisticated institutional analysis is required. Regulators need to focus on not just the compliance behaviour of regulated parties but also on wider aspects of regulatee attitudes and cultures and on the dynamics of the environment in which regulated parties operate. Further, the regulator must be aware of and responsive to its own behaviours, attitudes and culture and to the wider institutional environment in which it operates (Figure 11.2). Box 11.3 elaborates on the five aspects of really responsive regulation.

Figure 11.2  The really responsive regulator

The really responsive regulator is attentive to

- The behaviour, attitudes and cultures of regulatory actors
- The institutional setting of the regulatory regime
- The different logics of regulatory tools and strategies
- The regime’s performance over time
- Changes in each of the factors
Putting really responsive regulation into practice – three examples

What does being really responsive look like? And how can a really responsive approach help overcome the practical problems that regulators face in implementing the enforcement pyramid or help a regulator select the right enforcement strategy once a risk assessment has been undertaken? Can the really responsive approach capture the complex institutional settings that shape the behaviour of regulators and regulated parties? This section works through three examples: taking prosecutions, selecting an enforcement strategy for low-risk activities, and working within a unique constitutional and statutory environment.

Example 1: Taking prosecutions

One of the issues regulators face is the ability to use the top end of the responsive/enforcement pyramid. Box 11.2 outlines the factors that can dissuade regulators from taking prosecutions. These include the evidentiary requirements, the time and resources needed to take a prosecution, the time it can take to achieve an outcome, and uncertainty about the outcome and so the potential risk to the regulator’s reputation. Further, the ability of a regulator to promote compliance depends, in part, on the regulator being willing to use punitive powers to punish and deter breaches. A sub-optimal use of that power can undermine the regulatory regime. In addition, the regulator must be aware of the public interest in prosecuting breaches that are considered serious, pre-meditated or violent.

How can a regulator be responsive to these institutional and structural factors? A set of questions the really responsive regulator should ask about its approach to prosecutions is suggested in Box 11.4.
Example 2: Selecting an enforcement strategy for low-risk activities

One of the challenges of risk-based regulation is choosing what enforcement action to take. A simple risk assessment will not, of itself, provide the answer. The appropriate enforcement action will depend on the nature of the risk, such as whether it is stable or unstable or likely to change or accumulate over time. The appropriate enforcement action will also depend on the characteristics of the regulatee. The regulatee may be either well motivated or unmotivated to comply, or may have high or low capacity to comply. Indeed, the ability of the regulatee to manage or mitigate the risk can lower the inherent riskiness of the activity, leading to a lower overall “net” risk.

Black and Baldwin (2012) use their really responsive approach to develop a Good Regulatory Intervention Design (GRID) framework to help the risk-based regulator choose the best enforcement approach based on the nature of the risk and the nature of the regulatee for low risk activities (Figure 11.3). The authors have chosen to focus on the approach to low risks because low risks can accumulate over time. They note that...
environmental risks, in particular, can accumulate to create significant environmental damage. The authors recognise that in practice many regulators are tempted to adopt a “one size fits all” approach (to select one strategy and apply it to all lower risk sites or activities). Regulators may also be tempted to simply match the cost of the enforcement intervention to the level of risk. This is consistent with the main thrust of most risk-based approaches (direct resources to the highest risks), but it does not direct enforcement resources to the attitude of the regulatee and their capacity to comply and so modify the risk.

Figure 11.3  Framework for dealing with low-risk activities

Source: Black and Baldwin, 2012.
Figure 11.3 provides a framework for regulators to sort their regulatory activities in three different ways. The first way of sorting regulatory activities – shown on the left margin – is by the nature of the regulatee. Regulatees may be more or less willing to comply and more or less capable of complying. Regulatees with different levels of motivation and capability will respond to different regulatory activities. For example, a willing regulatee with high capability to comply may respond to a mailout of information on regulatory obligations, while a less willing or capable regulatee may require further interaction.

Second, regulatory activities can be sorted by the nature of the activity or site that is being regulated (the top margin). Regulated activities or sites can be “inherently” lower risk or “net” lower risk. The difference between “inherent” and “net” risk is the extent to which interventions can modify the risk. Regulated activities or sites can also be at a stable level of risk over time. Alternatively, the level of risk could accumulate steadily over time or increase dramatically through a step-change.

Third, different regulatory tools can be allocated according to the nature of the risk and the nature of the regulatee. The three basic types of regulatory tools described on the right margin are screening tools, monitoring tools, and engagement and incentive mechanisms.

The boxes in the centre of the figure are for regulators to fill in according to their assessment of the risk, the characteristics of the regulatee and the types of tools the regulator has available. For example, a regulator could allocate its educational activities – such as information brochures – to well-motivated, highly capable regulatees in regulatory areas of low and stable risk. These activities would be classified as “engagement and incentive mechanisms”. To illustrate this, the relevant box in Figure 11.3 has been filled out.

Figure 11.3 enables regulators to do one further piece of assessment. The regulator assesses the “regulatory intensity” depending on the type of regulatee and risk. “Regulatory intensity” is short-hand for the amount of time and effort the regulator needs to spend on a particular type of regulatee and risk. The figure provides a typical assessment of levels of regulatory intensity – the shade turns from light for low intensity through to dark for high intensity. The level of intensity grows higher as the regulatees’ willingness and ability to comply diminishes, and as the risk becomes less stable and more amenable to regulator effort.

To provide an example, the framework developed by Black and Baldwin (2012) for dealing with low-risk activities can be applied to pest management activities under the Biosecurity Act 1993. The Greater Wellington Regional Council’s pest activities are described in its Regional Pest Management Strategy (Wellington Regional Council, 2009) (Box 11.5).

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### Box 11.5 A strategy to manage pests

Pest invasions can be relatively stable or quickly accumulating depending on the stage of the invasion. As the Council notes, many pest invasions accumulate slowly as the pest establishes itself, followed by “a steep rise as the pest finds suitable habitats, and then a flattening off as these habitats reach carrying capacity” (p. 36). The Council’s strategy reflects this by keeping early and relatively stable pest invasions under surveillance and focusing pest control by council staff or contractors on pests that have found habitats.

Council pest activities also vary depending on the level of capability and motivation of landowners or land occupants. For example, the Council encourages capable and highly motivated landowners and occupants to form community groups that undertake local pest management projects.

Finally, activities can be sorted into screening, monitoring and engagement/incentive tools. Screening tools take the form of regional surveys to determine what pests have taken hold and what stage of invasion these pests have achieved. Monitoring tools include site inspections by staff or contractors. Engagement and incentive mechanisms take a range of forms, from public engagement via stalls at horticultural shows, to direct control of pests on site by staff or regulations banning certain pests or mandating certain control activities by landowners or occupants. At the extreme end, council inspectors have the power to enter and inspect any place for the purpose of confirming the presence of pests.
The GRID framework developed by Black and Baldwin (2012) for low-risk activities is attentive to the five concerns of the really responsive regulator in that it:

- integrates risk and behaviour by recognising that a regulatee’s willingness and capacity to comply with regulation is a key aspect in risk assessment (for example, it recognises that a well-motivated and capable regulatee can lower the overall net risk of the harmful activity; that is, the framework takes into account the behaviour and attitude of regulatory actors);

- recognises that the capacity of firms to comply is, in part, a function of the regime, and that one way to increase regulatee capacity to comply is to simplify the regime (that is, the framework is sensitive to the institutional setting of the regime);

- provides the risk-based regulator with a means for choosing a logical and defensible enforcement action rather than having one strategy for low risks or by simply assuming low risk equals low priority equals low resource allocation (that is, there is a logic to the enforcement tools);

- incorporates an explicit consideration of potential changes in the nature of the risk and changes in the capacity or motivation of regulatees to comply; it recognises that the need for regulatory intensity increases in the progression from inherent and stable low risks that require the least intensive interventions to net low risks that are unstable and which call for more attention (that is, there is sensitivity to change over time); and

- offers an opportunity for reassessment of the intervention strategy at regular intervals (that is, the framework allows for an assessment of the performance of the regulator in its choice of intervention strategy).

Example 3: Working within a unique constitutional and statutory environment

The really responsive framework emphasises the institutional settings in which the regulator operates. As explained in Chapter 2, a distinctive institutional setting in New Zealand is acknowledging Māori interests in the overall regulatory management system, and specific statutory requirements on some regulators in administering particular regulatory regimes. Chapter 9 illustrates how the Environmental Protection Authority fulfils its regulatory objectives within a framework that incorporates the principles of the Treaty of Waitangi.

The constitutional, statutory and legal requirements set the parameters under which the regulator undertakes its activities. The Treaty principles influence the decision-making approach of the regulator and a number of internal processes have been developed to fulfil the regulator’s statutory obligations with respect to the principles. The constitutional and statutory requirements influence the approach of the regulator to ensure that regulated parties (in this case, applicants for consent for nationally significant proposals under the RMA) understand the requirements around consulting and engaging with iwi. Because Māori and other stakeholders can make submissions on the proposals of applicants, this necessarily influences the approach that applicants need to take in preparing an application and working through the application process.

The regulator needs to be able to assess it performance and adapt its strategy over time. Performance measures include how efficiently and effectively the process works to generate the regulatory outcome, whether the regulator is meeting its statutory obligations with respect to the Treaty of Waitangi, and whether improvements can be made.

Finally, the relationship between the Treaty partners and how the principles of the Treaty are interpreted by the courts continues to evolve. The really responsive regulator needs to be sensitive to these changes over time.
11.3 Summing up

The really responsive approach to regulation sees the regulator being attentive and responsive to a broad range of factors in undertaking its regulatory practices. Factors that the regulator needs to be attentive and responsive to include the institutional settings it operates in and the market environment that the regulatees operate in; its own behaviours, attitudes and cultures and also those of regulated parties, the logics of regulatory tools and strategies (and how they interact), how the regime performs over time, and changes in all of these factors.

A sophisticated institutional approach offers a potential way forward in dealing with the challenges that regulators face in implementing their regulatory regimes. The Commission is interested in hearing from submitters on whether recent developments in the theoretical literature described in this section have application in the New Zealand context, both for the design of new regulatory regimes and their implementation.

Q11.1 Do recent developments in the theoretical literature, suggesting that in designing and implementing regulatory regimes, there needs to be a focus on:

- the behaviour, attitudes and cultures of regulatory actors, including those of the regulator;
- the dynamics of the regulated environment in which regulated parties and regulator operate, and the institutional setting of the regulatory regime;
- the logics of the regulatory tools and strategies used;
- the performance of the regime over time, and
- changes in each of the above factors;

offer a way forward for improving both the design and operation of New Zealand’s regulatory regimes?

The Commission suggests how recent developments in the theoretical literature might be incorporated into practical guidance for regulators at the end of this chapter. But first, the next section examines the operational practices of regulators in New Zealand and some of the challenges they face.

11.4 The practices and challenges of New Zealand regulators

This section explores practices that regulators in New Zealand use and the challenges they face. It draws on official advice produced for New Zealand compliance agencies; the Commission’s “request for information” from New Zealand regulatory agencies; an examination of selected agencies’ enforcement strategies; submissions to this inquiry; and surveys of business, chief executives and regulatory staff.

First… the practices

The key findings are:

- official guidance endorses both risk-based and responsive approaches;
- most regulators appear to prioritise their compliance and enforcement efforts, but the factors/criteria used to prioritise vary significantly;
- both risk-based and responsive regulatory approaches are evident in agency strategies; and
- some elements of really responsive regulation were also evident.
Official guidance endorses both risk-based and responsive approaches

The available official guidance on regulatory practice puts a strong emphasis on risk-based approaches, but also endorses responsive regulatory strategies.

The two main sources of official guidance on regulatory practice are Cabinet’s *Initial Expectations for Regulatory Stewardship* and the Department of Internal Affairs’ *Achieving Compliance* guide.

**Cabinet Initial Expectations**

*Initial Expectations* was agreed in March 2013 and outlines “at a high level how departments should be thinking about designing and implementing regulatory regimes and their stewardship responsibilities in administering those regimes” (Office of the Ministers of Finance and Regulatory Reform, 2013b). The intention is to set clear standards for chief executives about regulatory management, with the aim that regulatory regimes “deliver a stream of net benefits to New Zealand over time … and … be managed with that idea in mind” (ibid).

In *Initial Expectations*, Cabinet expects that “departments, in exercising their stewardship role over government regulation, will maintain a transparent, risk-based compliance and enforcement strategy, including providing accessible, timely information and support to help regulated entities understand and meet their regulatory requirements” (ibid, emphasis added).

**Achieving Compliance**

*Achieving Compliance* is a guide for compliance agencies in New Zealand, developed by the Department of Internal Affairs for the Compliance Common Capability Programme (CCCP). The guide has been cited as “best practice” by the Ministry of Transport and Pike River Royal Commission (Ministry of Transport, 2012; Royal Commission into the Pike River Mine Tragedy, 2012) and by Maritime New Zealand in their compliance strategy (MNZ n.d.(a)).

*Achieving Compliance* also endorses risk-based approaches:

...risk management is central to a successful and cost-effective compliance strategy. An intelligence-led, risk-based approach guides a compliance agency in choosing its compliance tools in individual cases or for particular segments of the regulated sector. It enables the agency to maximise its effectiveness, subject to the resources available to it. (DIA, 2011, p. 25)

A systematic risk-management framework helps decision makers make informed choices and respond to compliance risks in appropriate and proportionate ways. It therefore helps the agency develop a cost-effective compliance strategy, where limited resources are allocated appropriately to ensure the best possible compliance outcomes. (ibid, p. 56)

However, while the guide recommends using risk assessments to decide “which compliance tool will be appropriate for a particular case of non-compliance”, it also endorses a responsive regulatory approach, citing the Ayres/Braithwaite enforcement pyramid as a “valuable conceptual tool for regulatory agencies in achieving or improving compliance” (DIA, 2011, p. 31).

**Most agencies prioritise their compliance and enforcement efforts**

The Commission asked 32 regulatory agencies to describe their compliance monitoring strategies for each Act they administered. Agencies were asked: Do you monitor all regulated entities to the same degree? If not, which statements describe your compliance monitoring strategy for these areas?

a) Monitoring effort is based on the perceived likelihood of non-compliance by organisations and individuals.

b) Monitoring effort is based on the perceived harm from non-compliance by the organisation or individual.
c) Monitor in response to complaints or “intelligence”.

d) Other (please describe).

Figure 11.4 captures the responses of the 24 agencies that responded to this question.

Figure 11.4 Monitoring approach taken by regulators

Non-compliance likelihood AND perceived harm from non-compliance AND other factor
Perceived harm from non-compliance AND response to complaints and intelligence
Non-compliance likelihood AND perceived harm from non-compliance
Likelihood of non-compliance
Perceived harm from non-compliance
Approach varies depending on circumstances or regime
Non-compliance likelihood AND other factor
Response to complaints and intelligence
Non-compliance likelihood AND perceived harm from non-compliance AND response to complaints and...

Source: Information collected by the Productivity Commission.

Only three – the Takeovers Panel, the Reserve Bank of New Zealand and the Ministry of Transport (with regards to the Airport Authorities Act) – said that they monitored all regulated entities to the same degree. The rest employed a range of monitoring approaches, with the most common response being combined enforcement strategies (that is, the likelihood to comply and the risk from non-compliance and complaints or intelligence) and complaints/intelligence-based monitoring.

Few of the regulators that responded to the Commission’s request for information applied the same level of compliance monitoring to all regulated entities. Most prioritised their efforts in some way, and in many cases regulators applied more than one criterion in judging where and when to monitor.

Published compliance and enforcement strategies

In addition to the request for information, the Commission examined the published compliance and enforcement strategies of five regulators – the Commerce Commission, the Civil Aviation Authority (CAA), the Department of Internal Affairs (DIA), the Financial Markets Authority (FMA) and Maritime New Zealand (MNZ) – to understand the criteria and approaches they applied (Table 11.1).
The Civil Aviation Authority
Risk reduction is the main enforcement goal for the Civil Aviation Authority (CAA): “A key driver for the CAA’s decisions on the type and level of its involvement with participants is the nature of their aviation activity and the impact on third parties of safety failure. In this regard the principle of public interest being paramount is a key consideration” (CAA, 2012a). Every industry participant is rated according to the level of aviation safety risk they pose, and CAA resources are allocated towards activities where the consequences of regulatory failure are highest.

However, in carrying out its regulatory activities, the CAA also takes into account the attitudes of participants and their willingness to comply with or correct behaviour. The key criteria considered are:

- “the life cycle of an aviation participant at the CAA’s role at each stage (entry, continued operation or exit);”
- the nature of the activity (its inherent level of risk at a system level);
- the CAA’s assessment of the specific aviation safety risk presented by activities of the individual participant; and
- the attitudes and behaviour of aviation participants towards compliance, safety and reporting” (CAA, 2012a).

Similarly, enforcement actions are taken based on the principles of public interest, proportionality (the level of action reflects the degree of culpability and harm caused, willingness to learn, and compliance history) and consistency (that is, the same response to similar cases).

The Commerce Commission
The Commerce Commission applies risk-based criteria in deciding whether to take or continue enforcement actions, that is:

- **extent of detriment**: examples include the extent of physical harm, increased costs, property loss or impaired choice created; whether the vulnerable are targeted; and adverse impacts on competition or emerging markets;
- **seriousness of conduct**: examples include the extent to which the conduct is reckless or deliberate, repeat behaviour, a serious departure from expected lawful commercial behaviour, and its reversibility; and
- **public interest**: examples include the extent to which action is required to maintain public confidence, clarify the law; and the existence of mitigating or aggravating features.

In choosing how to respond, the Commerce Commission seeks to prioritise limited resources “on matters where the greatest harm exists or may occur”. Breaches involving significant harm, reckless and repeated behaviour and public confidence are likely to prompt a “high-level enforcement response” (such as civil or criminal proceedings, cease and desist orders). Less severe breaches may prompt warnings or compliance advice letters. In taking action, the Commerce Commission also seeks to “incentivise compliance with the law” and therefore reaches for low-cost and less-intrusive tools (such as education, advocacy, engagement, and outreach) “wherever we believe that we can share our knowledge to prevent non-compliance with the law” (Commerce Commission, 2013a, Commerce Commission n.d.).
### Department of Internal Affairs

Compliance maximisation is a key goal. The Department of Internal Affairs (DIA) expects “everyone to comply with the law” and believes “most individuals and organisations are willing to comply”. DIA therefore sees their role as being to “identify and focus our regulatory efforts on removing barriers to full and sustained compliance. This means that the approach we take to compliant individuals or organisations will differ from the solutions we choose for those who are wilfully negligent or deliberately negligent”.

Harm reduction is a complementary, but separate activity: “as well as focusing on compliance, we promote examples of excellence and highlight areas where non-compliance or negligence is creating harm or has the potential to create harm...This means we use our insight, knowledge and understanding to identify risks, and determine interventions to most effectively deal with those issues” (DIA, 2012).

### The Financial Markets Authority

The Financial Markets Authority (FMA) takes a “risk-based approach” to monitoring and surveillance, with resources and enforcement action prioritised “to those participants and practices that present the greatest risk to fair, efficient and transparent financial markets” (FMA n.d.(a)). The Authority uses market intelligence and research to identify “potential problems, assess the likelihood that poor practice or non-compliance will occur, and consider its impact on consumers or the market”.

However, the FMA’s regulatory framework and compliance philosophy also incorporate aspects of responsive regulation. The compliance philosophy emphasises working “with industry to help them comply with our expectations, so there is an improvement in overall behaviour and performance across financial markets” and establishing “a framework that encourages participants to quickly report and correct errors or regulatory breaches” (FMA n.d. (b)).

### Maritime New Zealand

Maritime New Zealand (MNZ)’s enforcement approach targets harm, “the magnitude of the consequence that would eventuate should an event occur” and “the likelihood of that event occurring”. MNZ concentrates “our activities where we see a pattern of problems or issues. These patterns might occur in particular parts of the maritime sector, with types of vessels, types of equipment, or practices, or in particular geographic areas. They might also occur with particular operators”. To identify these patterns, MNZ draws on intelligence, including audits, inspections, investigations and their “knowledge of oil spills and security issues” (MNZ n.d.(a)). At the same time, MNZ will take into account the nature of the conduct and attitude to compliance of the individual or firm in question. Compliance tools are selected using the following criteria:

- **extent of harm or risk of harm**: for example, the scale of actual or potential harm to health and safety, security and the environment;
- **conduct**: “the behaviours, intent and capability of the person whose actions are being considered”;
- **public interest**: for example, “responsibility to victims, the need to clarify the law, and whether the matter at hand reflects a widespread problem that can be usefully addressed by highlighting the need for compliance”; and
- **attitude to compliance**: “the general attitude (or level of willingness) of individuals or groups to be compliant” (MNZ n.d. (b)).
Both risk-based and responsive regulatory approaches are present

According to their published compliance and enforcement strategies, all five regulators considered both the harm caused by compliance breaches and the attitude/behaviour of those causing breaches when allocating resources and taking action. However, agencies differed in the extent to which they prioritised harm reduction or compliance maximisation, and the extent to which the two objectives were integrated or treated separately.

Broadly characterised, DIA’s strategy puts the most emphasis on responsive regulation, with an underlying objective of full compliance with the law. The FMA’s strategy is arguably the most risk based, with a clear acknowledgement in its enforcement policy that the Authority “will not enforce every breach that comes to our attention”, especially those breaches that are minor and do not involve a public interest issue (FMA n.d. (c)). The strategies of the CAA and MNZ integrate harm reduction and compliance maximisation most closely, while the DIA strategy appears to see compliance and harm reduction as separate but complementary activities.

F11.6

The strategies of the regulatory agencies examined by the Commission consider both the severity of the harm caused by compliance breaches and the attitude/behaviour of those causing breaches when allocating resources and taking action. However, they differ in how far they prioritise reducing harm or maximising compliance, and the extent to which the two objectives are integrated or treated separately.

Some elements of really responsive regulation are also evident

Attentiveness to some of the really responsive regulation factors (Box 11.3) was also clear in a number of agency strategies:

- **Behaviour and attitude of actors**: The CAA, Commerce Commission and MNZ explicitly integrated the attitude of the firm or individual into their risk or harm-based decisions about when and how to intervene.

- **Institutional setting**: DIA and MNZ acknowledge in their compliance strategies that some firms and individuals may face difficulties complying:

  We support individuals and organisations needing help to comply. We provide a lot of information and guidance and make compliance as simple as possible. We tolerate unintentional errors and mistakes. We understand mistakes happen and can help rectify them when they are brought to our attention openly and early. (DIA, 2012, p. 10)

  We aim to make compliance as easy as possible for those that are capable and want to comply [and] assist those who are trying to comply but not succeeding. (MNZ n.d. (a))

- **Logic of regulatory tools**: MNZ does not apply one intervention for low-risk breaches, nor do they necessarily conclude that low-risk breaches are a lower priority for action. The CAA is mindful that strong enforcement action can deter reporting of incidents, recognising that good information is necessary for the aviation system to learn from mistakes:

  Recognising the importance of full disclosure and reporting for the ability of the aviation system to learn from mistakes, the Civil Aviation Authority “prefers not to take enforcement action against those who fully report details of accidents and incidents” but may do so where reporting is “patently incomplete or reveals reckless or repetitive at-risk behaviour”. (CAA, 2012a; 2012b)

  Our approach will be tailored to the circumstances. We will select the intervention/s that we think will have the most impact on achieving our outcomes, taking into account risk, attitude and capability, plus the likely consequences of an incident or harm occurring … In some compliance agencies, interventions form a sequence or hierarchy – starting with low-level activity, and moving to more severe measures. MNZ does not operate in this way, focusing instead on selecting the right tool for the right job. (MNZ n.d. (a))
The compliance and enforcement strategies examined by the Commission paid less attention to the dynamic factors of the really responsive regulation framework – that is, attentiveness to the regime’s performance over time, and to changes in factors such as regulatory behaviour and market settings. The exception was the FMA, which seeks “to proactively monitor a range of market participants and business models. In this way, we can identify new risks, and any compliance themes or areas of poor practice across the market or market sector” (FMA (n.d.(a))). It is worth noting that, in its submission, the CAA explicitly referred to the need for attentiveness to the five factors of really responsive regulation when designing, developing and applying regulatory systems, if a regime is to be enduring (CAA, sub. 6).

Now the challenges...

The Commission found that New Zealand regulators face challenges in implementing good regulatory practice similar to those identified in the academic literature. The New Zealand experience demonstrates challenges relating to:

- difficulties assessing and targeting risk;
- conflicting compliance approaches;
- insufficient or inappropriate enforcement tools;
- the costs and timeliness of prosecutions; and
- the ability of regulators to learn from experience and respond to changes in the regulated environment.

Difficulties assessing and targeting risk

Experience with regulatory failures in New Zealand suggests that some agencies have struggled to effectively identify and target risks. Chief among examples is the Pike River mine tragedy, where the relevant regulator had an explicitly risk-based strategy. As the Royal Commission noted,

> although mining had the third highest injury rate, in contrast to the construction, agriculture, forestry, manufacturing and fishing industries, it was not seen as a priority area. This seems to be because of a focus on industries with 100,000 or more full-time equivalent workers. This approach was too blunt….

Interestingly, the highest risk sectors were identified primarily according to personal injury data – the consequences of individual accidents – but high-hazard industries are at risk of catastrophic process safety accidents, which are, by their nature, low frequency high consequence events. As the Pike River mine tragedy demonstrates, a focus on personal injury rates alone is not adequate to identify the ultimate workplace hazards. Until recently, there was no sign that catastrophic risk featured in the department’s strategic thinking. (Pike River Royal Commission, 2012, p. 295)

Inquiry participants pointed to three main barriers to identifying and targeting risk effectively: insufficient capability, inadequate information sources, and differing political and public definitions of risk.

Capability

Aviation New Zealand commented that few regulators consistently undertook “high quality risk analysis and utilization of the risk management standard”, which was “critical in building consensus”. They attributed the lack of consistent good practice in part to “an absence of high quality analysts who understand the information” (sub. 36, pp. 28-29). In the case of regulated parties, the CAA observed that smaller organisations can struggle to keep up:

> Having good ability to recognise risk, sector confidence and trust, sector knowledge, intelligence systems, and good training for staff are all factors in the adoption of risk-based approaches in
New Zealand. Particular challenges related to the speed and competence with which smaller and sole operators will implement SMS [Safety Management Systems]. (sub. 6, p. 50)

Information
The Council of Trade Unions noted that a significant barrier in adopting risk-based approaches (at least in the area of occupational health and safety) “is sufficient data and information of the right quality and the right form to make the decisions necessary for risk-based approaches. In some cases there are privacy and confidentiality issues that must be addressed. Well-designed information systems are also necessary” (sub. 25, p. 24). Aviation New Zealand concurred, noting that “we are a small country and thus our data sets are not rich” (sub. 36, p. 29). ANZ Bank observed that, in some cases, regulated parties may be better able to identify legitimate risks than the regulator (sub. 24, p. 6).

Public and political understanding of risk
According to the Meat Industry Association, a key barrier to introducing and maintaining risk-based compliance systems is public and political understanding of risk:

Understanding of risk is generally lacking, including at a political level, and is a major challenge to risk-based regulatory approaches … In New Zealand, with regards to biosecurity there is a public expectation that 100% inspection at the border will result in 100% security. In fact 100% border inspection may increase the risk, as it could mean spreading resources inappropriately and providing a false sense of security. (MIA, sub. 40, p. 7)

The Reserve Bank made it clear that

[i]n respect of the prudential supervision of financial institutions, regulatory failure is not synonymous with the failure of a financial institution. Financial regulation does not have a goal of zero failure of financial institutions, and the failure of a financial institution is not a regulatory failure. The supervision of financial institutions by the Reserve Bank is aimed at maintaining a sound and efficient financial system, and avoiding significant damage to the financial system that could result from the failure of a financial institution. (RBNZ, sub. 9, pp. 11-12)

A lack of industry or sector understanding of a risk-based approach – which entails targeting resources on some activities and explicitly not others – can undermine the credibility of the regime. The New Zealand Food and Grocery Council (NZFGC) suggests that non-enforcement under a risk-based approach raises issues about the appropriateness of regulation:

The issue in risk basing compliance raises the issue of non-enforcement and therefore appropriateness of regulation (if a regulation is not intended to be enforced, why have it and are there better ways of giving effect to the desired outcome or changing behaviours) (sub. 35, p. 8)

And where regulators manage to successfully implement compliance strategies, they risk sowing the seeds of their own undoing, by creating public and political complacency about risk:

[T]here is potential in a high-risk high-reliability industry that has had very few safety failures (such as aviation) of failure to maintain regulator relevance and public understanding of the sector and its risks. A consequence of this is loss of interest in the activities of the regulator, and progressive disinvestment and loss of priority for the agency. (CAA, sub. 6, p. 52)

Good compliance monitoring and enforcement can be expensive but the results are often not visible and tangible compared to when something goes wrong – so over time it can be devalued and underfunded compared to front end rule-making and decision-making processes. Investigation into ways to account for the intangible results of good monitoring and enforcement may help keep this politically fresh. (Environmental Protection Authority, sub. 20, p. 3)

Conflicting compliance approaches
Aviation New Zealand noted that there were fundamental conflicts between the aviation safety compliance regime (which relies in part on disclosure by industry participants to reveal risks) and health and safety regulation (which is more prosecutorial in approach):

Aviation’s safety system is predicated around information disclosure which facilitates and enables continuous learning. However in the HSE [health and safety in employment] environment there is a belief that it’s best not to self incriminate. The CAA has an understanding and appreciation of the
importance of learning from accidents – the same cannot be said for agencies involved in HSE matters where investigations are conducted to determine whether to prosecute or not. If this prosecution culture crosses over into aviation then there will be a rapid deterioration in reporting. Even a loss of confidence in the robustness with which safety information is treated can lead to a loss of confidence in regulatory systems and processes and a reduction in reporting. (pp. 7-8)

**Insufficient or inappropriate enforcement tools**

Air New Zealand (sub. 47) emphasises the importance of the regulator having the appropriate regulatory tools available:

Good operation of regulators cannot overcome the inherent flaws in poor regulatory design. In these cases the outcomes intended by Parliament will never be achieved because the regulators have never been provided with the tools to effectively achieve these outcomes. (p. 5)

The NZFGC noted limitations in the range of enforcement tools available under the Food Act: “The comparison between the Food Act and the Food Bill is instructive – the Food Act provides for limited discretion and tools, the Food Bill for much greater discretion and a wider range of enforcement tools” (sub. 35, p. 8).

**The cost and timeliness of prosecutions**

Enforcement actions in the courts are expensive, and these costs increase with the severity of the breach in question. A 2011 review of public prosecution services (which many regulators use, either entirely or in part, to undertake prosecutions) found that average costs had increased between 2005 and 2010, with the average cost of an action in the High Court being about four times the cost of an action in the District Court (Spencer, 2011).

For enforcement actions involving complex issues, the costs can be high. For example, the Commerce Commission often incurs well over $1 million each year in costs investigating and pursuing cases of coordinated behaviour, such as cartels (see Table 11.2). This is only one type of regulatory breach that the Commission investigates.

Table 11.2  Commerce Commission expenditure on coordinated behaviour cases: 2008/2009 to 2010/11

<table>
<thead>
<tr>
<th>Year</th>
<th>Expenditure on output class</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008/9 Actual</td>
<td>$3.679m</td>
</tr>
<tr>
<td>2009/10 Actual</td>
<td>$3.364m</td>
</tr>
<tr>
<td>2010/11 Actual</td>
<td>$1.759m</td>
</tr>
</tbody>
</table>

Source: Commerce Commission, 2011.

The timeliness of getting an outcome in the courts was an issue for the Commerce Commission in the Credit SaILS case. Because of the length of time it would take to secure a successful prosecution through the courts, the Commerce Commission elected to settle with the five companies who agreed to establish a settlement fund for investors, many of whom were elderly. The Commerce Commission’s decision was taken in the interests of consumers (consistent with the purpose of the Fair Trading Act 1986) and public interest considerations.

Box 11.6  Commerce Commission closes out successful Credit SaILS investigation

Credit SaILS were sophisticated debt securities marketed and sold to the New Zealand public in 2006, with the prospect of 8.5% interest income and capital protection. $91.5 million was raised through the offer. Credit SaILS failed in 2008 and the notes were virtually worthless on maturity.

In December 2012 the Commerce Commission reached a settlement with five companies involved in the failed investment product. The companies were Forsyth Barr Limited, Forsyth Barr Group Limited, Crédit Agricole Corporate and Investment Bank, Credit Sail Limited and Calyon Hong Kong Limited. The Commerce Commission alleged that the parties had engaged in misleading and deceptive conduct when marketing the products, and that this breached the Fair Trading Act. The companies did not agree with the Commerce Commission, and denied that they had breached the Act. However, as
part of the settlement, the companies agreed to create a settlement fund of $60 million to be distributed to investors who lost money.

Commerce Commission Chairman Dr Mark Berry said that completing the payment process was a fantastic outcome for the investors: “Most of the investors in this fund were elderly and it was important for the [Commerce] Commission to settle this in the most advantageous way for these people. Hopefully, having the money returned to them will have a big impact on the quality of their lives”.

Source: Commerce Commission, 2013b.

This example illustrates that good outcomes can be achieved by being mindful of the purpose of the regulation and an understanding of the incentives on the market participants involved. However, Bell Gully suggests that regulators may be reluctant to negotiate a settlement as a means of resolving a regulatory disagreement once procedures have been initiated. This is because the costs of the regulator’s investigation have already been incurred. Bell Gully has concerns about statements in enforcement policies that indicate that the prospect of settlement is reduced once a regulator has determined to pursue an enforcement case (Bell Gully, sub. 38).

Learning from experience and responding to change

A number of surveys provided perceptions about a regulator’s attentiveness to its performance and perceptions about a regulator’s ability to learn from experience. The Commission’s survey of 1,526 businesses revealed that only 15% of businesses perceived that regulators “always” or “mostly” review their performance and seek opportunities to improve, although 48% thought that this happened “sometimes” (Figure 11.5).

Figure 11.5 Business perceptions of whether “regulators review their own performance and seek opportunities to improve over time”

Source: Colmar Brunton, 2013.

A second but more equivocal source of evidence is the Commission’s survey of regulator chief executives (Figure 11.6). Respondents were fairly evenly split on whether they agreed with the statement that “there are effective feedback loops between frontline regulatory staff and policy functions”, which is one important avenue for identifying opportunities to improve over time. Six respondents agreed or strongly agreed that there were effective feedback loops, but seven respondents disagreed or strongly disagreed (eight respondents neither agreed nor disagreed and two did not know).

Figure 11.6 Chief executive agreement with the statement “There are effective feedback loops between frontline regulatory staff and policy functions”

The most detailed source of evidence is the recent Victoria University (VUW IRC) survey of Public Service Association (PSA) members. PSA members were asked how they perceive “their organisation’s ability to learn from their mistakes and successes”. On average, workers disagreed with the statement that “this organisation is good at learning from its mistakes and successes”. But central government regulatory workers showed the highest level of disagreement, and this was significantly different compared to the responses of regulatory workers working in local government and district health boards, and to the responses of non-regulatory workers.

Figure 11.7 Central government regulatory worker agreement with the statement “This organisation is good at learning from its mistakes and successes”

![Graph showing the percentage of workers agreeing with the statement across different categories.]

Source: VUW IRC & PSA, 2014.

The responses from PSA members to other questions tend to reinforce the finding that regulators (and in some cases government agencies more generally) face difficulties in relation to continuous performance improvement (Table 11.3).

Table 11.3 PSA worker perceptions of their organisations

<table>
<thead>
<tr>
<th>Topic</th>
<th>Perceptions across all workers</th>
<th>Perceptions across central government regulatory workers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Challenging poor practices</td>
<td>On average, surveyed workers seem to disagree that management systems allow them to challenge poor practices.</td>
<td>Central regulatory workers perceive that their management systems are less likely to allow them to challenge poor practices compared to non-regulatory workers.</td>
</tr>
<tr>
<td>Communication</td>
<td>On average, surveyed workers seem to disagree that there is good communication between workers in their organisations.</td>
<td>Central regulatory workers are less likely to perceive that there is good communication across all sections of the organisation compared to non-regulatory workers.</td>
</tr>
<tr>
<td>Sharing knowledge and information</td>
<td>On average, surveyed workers seem to disagree that knowledge and information are shared throughout their organisations.</td>
<td>Central regulatory workers are less likely to perceive that knowledge and information are shared throughout their organisations compared to non-regulatory workers.</td>
</tr>
<tr>
<td>Innovation</td>
<td>On average, surveyed workers disagree with the statement that their organisation is innovative.</td>
<td>Central regulatory workers are less likely to perceive their organisations as being innovative compared to non-regulatory workers.</td>
</tr>
</tbody>
</table>

Source: VUW IRC & PSA, 2014.

The PSA survey also reveals that few central government regulatory workers believe that the management systems in their organisations are flexible enough to allow them to respond quickly to changes (Figure 11.8).
Figure 11.8  Regulatory workers in central government who agree with the statement “the management systems in this organisation are flexible enough to allow us to respond quickly to changes”

<table>
<thead>
<tr>
<th></th>
<th>14%</th>
<th>29%</th>
<th>34%</th>
<th>21%</th>
<th>2%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly disagree</td>
<td>Tend to disagree</td>
<td>Neutral</td>
<td>Tend to agree</td>
<td>Strongly agree</td>
<td>non-response</td>
</tr>
</tbody>
</table>

Source: VUW IRC & PSA, 2014.

And few regulatory workers in central government believe that the management systems in their organisations evolve rapidly in response to shifts in business priorities (Figure 11.9).

Figure 11.9  Regulatory workers in central government who agree with the statement “the management systems in this organisation evolve rapidly in response to shifts in business priorities”

<table>
<thead>
<tr>
<th></th>
<th>15%</th>
<th>31%</th>
<th>32%</th>
<th>21%</th>
<th>2%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly disagree</td>
<td>Tend to disagree</td>
<td>Neutral</td>
<td>Tend to agree</td>
<td>Strongly agree</td>
<td></td>
</tr>
</tbody>
</table>

Source: VUW IRC & PSA, 2014.

While the PSA survey presents a picture of inflexibility and a lack of speed among central government regulators in responding to changes in priorities, there is some evidence that regulators are attentive to and scan for changes in risks in the regulated environment. For example, the Reserve Bank publishes a six-monthly Financial Stability Report that includes a systemic risk assessment. The Ministry for Primary Industries monitors changes to New Zealand’s biosecurity risks.

The CAA commented about the changing nature of risk (sub. 6). As safety-related technology has improved, risk is becoming increasingly behavioural. This has led the CAA to put a greater focus on human factors, behavioural change and more subtle surveillance cues.

Many of the issues and challenges identified in the literature play out in New Zealand, including:

- difficulties assessing and targeting risk;
- conflicting compliance approaches;
- insufficient or inappropriate enforcement tools;
- the costs and timeliness of prosecutions; and
- the ability of regulators to learn from experience and respond to change.

In summary, regulators often struggle with putting risk-based approaches to regulation into practice, and there are challenges in applying enforcement tools.
The perception that regulators do not take opportunities to improve performance, do not learn from mistakes and successes, and are inflexible in the face of changes in priorities, suggests that New Zealand regulators are insufficiently attentive to two of the five key factors of really responsive regulation – performance over time and response to changes in the regulated environment.

An examination of regulatory practice in New Zealand has revealed a range of approaches and amply illustrated the challenges of putting theory into practice. The next section suggests areas for further guidance, and assistance for regulators in adopting effective regulatory practices.

11.5 More effective regulatory practice

Being an effective regulator is hard. Both the academic debates over the pitfalls of risk-based and responsive approaches, and the practical challenges that agencies here and overseas have faced in implementing regimes, demonstrate this point.

A number of New Zealand regulators have clearly thought deeply about their compliance and enforcement strategies, incorporating insights from the developing academic literature and attempted to integrate elements of risk-based and responsive approaches into their strategies. These efforts are commendable, and reflect well on the leaders and staff of those organisations. However, to support effective practice across the regulatory system, better central guidance and assistance will be needed. The two particular areas where changes in the regulatory management system could help promote more effective practice are:

- formal recognition of communities of regulator practice in the regulatory management system; and
- development of more detailed and targeted guidance on regulator practice.

Formal recognition of communities of practice

Regulatory practice in New Zealand could be improved by supporting networks, where regulators can discuss common challenges, share experiences and learn from each other. Such networks currently exist, but they are not formally recognised as part of the regulatory management system and they rely on the goodwill and dedication of individuals.

Under the current public sector management framework, responsibility for ensuring that regulators have the systems and capability in place to effectively or efficiently carry out their regulatory obligations lies with chief executives of the public sector departments that administer the regimes and (where relevant) the boards of Crown entities or other agencies that implement the regimes. Recent changes to the State Sector Act have made this responsibility on departmental chief executives clearer.

Clear obligations on departmental chief executives and Crown entity boards for performance and maintaining organisational capability are appropriate. They provide incentives for the continued delivery of services to New Zealanders. However, the strong vertical lines of accountability provide few incentives for agencies to coordinate and share experience, capability, processes or practices. Gill (2013), the Better Public Services Advisory Group (2011) and the Review of the Centre Advisory Group (State Services Commission, 2001), among others, have noted this.

In other areas of government activity (such as use of information and communication technology, and procurement, finance and property management) efforts have been taken to provide horizontal coordination by appointing selected departmental chief executives as “functional leaders” for these areas. The intent behind the appointment of “functional leaders” is to

- drive efficiencies (though economies of scale, leveraging buying power in whole-of-government contracts, setting common standards and approaches, and reducing duplication);
- develop expertise and capability (centres of expertise, coordinated professional development, deploying capability to where and when it is most needed); and
improve services and service delivery (through sharing and coordinating activities and facilities, joined up service delivery). (SSC, 2013b)

As noted in this chapter and other chapters in the report, many regulators face a set of common issues and challenges and there is scope to improve capability across the board.

One option would be to appoint a departmental chief executive as the functional leader for regulatory practice. This would have the merit of clearly allocating responsibility for activities such as developing expertise and guidance, developing standards, and sharing experience or practice. Depending on the approach taken, it could also provide strong incentives for a wide range of regulators to participate in shared and coordinated activity – “functional leaders” can, with Cabinet agreement, be given the power to impose mandatory requirements on other departments. Also, the Ministers of Finance and State Services can direct Crown entities “to support a whole of government approach by complying with specified requirements”. The leadership role could be given to the Treasury (as the department with responsibility for the government’s regulatory management system), the State Services Commission or one of the departments with a significant and broad role in implementing regulation (possible candidates include the Ministry of Business, Innovation and Employment or DIA).

However, while there are some potential benefits from appointing a functional leader for regulatory practice, there are also costs and limitations.

- Unlike ICT, procurement, finance and property management, regulatory practice is not a generic and common input to other public services. As such, it may not be as easy for a central “leader” to drive performance improvements.

- A considerable share of the expertise in implementing regulatory regimes lies in Crown entities. However, under current policy, only departmental chief executives can be appointed as “functional leaders”.

- Most importantly, establishing new leadership arrangements for regulatory practice would cut across existing networks and would be likely to create disruption, at least in the short term.

Given these points, the Commission considered that a more effective and lower-cost approach would be to formally recognise existing networks in the regulatory management system and strengthen incentives for regulators not currently participating to either join existing networks, or establish equivalent fora.

**Existing networks**

The main forum on regulatory practice is the CCCP, a voluntary group of central and local government agencies aimed at developing a “professional compliance community in New Zealand”. Since its establishment in 2008, the CCCP has:

- commissioned a guide for regulatory agencies on regulatory practice (DIA, 2011),

- developed three national qualifications on compliance and is working with The Skills Organisation on qualifications for the National Qualifications Framework as part of the Targeted Review of Qualifications (Chapter 12); and

- established a Regulatory and Learning Council to create and share material to support learning and development opportunities.

The CCCP is currently managed out of MNZ, with DIA contributing both financial and in-kind support for specific activities. In line with its voluntary nature, the CCCP’s project management is “club funded” by 10 agencies. This funding has a time limit and will expire at the end of the current financial year.

While supportive of the CCCP, the Commission is neither recommending that membership of the CCCP be mandatory nor that the Crown fully fund all CCCP activities directly. The Commission reasons that:

69 Crown Entities Act 2004 (s. 107).
• requiring agencies to meet at least some of the costs of membership encourages them to pay attention to the activities of the network and hold its leaders to account;

• mandatory membership of one network would weaken incentives on the CCCP to deliver value for members; and

• while the CCCP has demonstrated leadership and expertise, alternative networks and arrangements may provide superior value to some regulators.

In addition, a number of regulators who responded to the Commission’s information request reported that they undertook benchmarking against domestic and foreign agencies, including through membership of international networks.

**What formal recognition would entail**

The ability of regulator networks to promote better practice and information sharing is constrained by limited time and limited resources, and by a lack of incentives on individual agencies to participate. Formal recognition would seek to offset these barriers for example through:

• partial government funding for a period (for example, 3-5 years) for established or new regulator networks or forums, tied to a business case and performance measures;

• revisions to Cabinet’s *Expectations for Regulatory Stewardship*, to clarify that regulatory agencies should seek to raise their own and the sector’s performance by sharing experiences and participating in communities of practice; and

• active monitoring by Treasury and portfolio departments (for Crown entities) of regulator participation in communities of practice and other activities to share experiences.

A 3-5 year funding contract could be used to update guidance on regulatory practice (see below), and support a wider range of activities to improve practice. Some possible topics of work are outlined below. At the end of the funding period, officials would consider whether a new contract or alternative institutional arrangements were needed.

The point of the exercise is not to require membership of groups and networks *per se*, but to find cost-effective ways of helping regulators – many of whom are small, and face scale issues – to improve their practice by learning from each other. In monitoring regulator participation, the Treasury and portfolio departments should focus on this outcome, not processes.

**R11.1**

Formal recognition of regulator forums or networks could offset the barriers to sharing good practices through:

• partial government funding (for example, 3-5 years) for regulator networks, tied to a business case and performance measures;

• revisions to Cabinet’s *Expectations for Regulatory Stewardship*, to clarify that regulatory agencies should seek to raise their own and the sector’s performance by sharing experiences and participating in communities of practice; and

• active monitoring by the Treasury and portfolio departments (for Crown entities) of regulator participation in communities of practice and other activities to share experiences.

**Improved guidance**

Discussion about regulatory practice often focuses on simplified portrayals of the decisions and trade-offs required. The Commission encountered simplistic use of the Braithwaite enforcement pyramid (outlined in Box 11.1) and the risk-based regulation cycle (Figure 11.1). The problem is not just confined to compliance
practitioners. Nor is it confined to New Zealand. Mascini (2013) argues that responsive regulation has been reduced to the pyramid, stripped of the normative content of Ayres and Braithwaite’s seminal work:

> All in all, because responsive regulation has very largely been reduced to the enforcement pyramid, the literature has neglected the normative issues surrounding the regulation of capitalist economies that were central to Ayres and Braithwaite. (p. 48)

Similarly, Black and Baldwin (2010) argue that the mechanical/quantitative means of solving regulatory problems as envisaged for example by the Hampton Review (2005), presents a “too easy vision of risk-based regulation” (p. 183).

While simple portrayals are useful entry points to the concepts of responsive or risk-based regulatory approaches, they present a misleading picture. Guidance on regulatory practice needs to provide a more sophisticated analysis in line with recent developments in the theoretical literature.

A key task for a regulator network to secure funding, as proposed above, should be to build upon existing guidance on regulator practice, so as to:

- reflect developments in the theory of regulatory practice; and
- provide more targeted and detailed guidance.

The main source of guidance on compliance and enforcement is the DIA /CCCP’s publication *Achieving Compliance*. This was a step forward for regulatory practice in New Zealand, bringing together key regulatory concepts, lessons and principles in a format that a wide range of users could access. The guide was seen as “a foundation and starting point for capturing and sharing knowledge”, and the intent in developing it was

> to provide easy access to information about specific topics or matters of interest; as well as, in total, providing a comprehensive view of options for designing effective compliance organisations and strategies… This guide will support compliance agencies to develop and constantly improve the way they work by capturing and sharing information that enables this to occur. (DIA, 2011, p. 3)

*Achieving Compliance* was also aimed at a cross-section of the regulator community:

> It is intended to be of interest to the most experienced and skilled leaders who have the capability and resources available to them to be at the cutting edge of operational compliance work through to those managers and staff who have limited experience of compliance work, or time to devote to it, but find that it is part of their portfolio of responsibilities. (ibid)

While the broad focus of *Achieving Compliance* was appropriate for a “starting point”, what is needed now is more detailed and sophisticated information that reflects the:

- practical challenges in implementing and integrating risk-based and responsive compliance and enforcement strategies; and
- different information needs at different levels of a regulatory agency – for example, managers may need help to set and review regulatory strategies or improve organisational processes, while enforcement staff may need help to assess the risk posed by an incident.

Judging by the issues and barriers outlined in Section 11.4 above, possible areas of focus could include guidance on defining and targeting risk; selecting intervention tools that appropriately reflect both risk and compliance attitudes: and establishing strong internal feedback loops for intelligence gathering and assessment of how well enforcement strategies are working.

Of course, the real value in any guidance material is how it is used. To encourage the production of guidance that is of practical use to regulators, one performance measure of the proposed 3-5 year funding contract should be take-up and use of the guidance material produced.
To encourage the production of guidance material of practical use to regulators, one performance measure of the 3-5 year funding contract should be take-up and use of the guidance material produced.

The CCCP will consider its future direction and resourcing requirements in the first half of 2014 (sub. 12a). It could use the opportunity presented by the review of its activities to consider applying for funding to improve the existing guidance material.

11.6 Summing up

This chapter began with the observation that the approach taken to monitoring, enforcement and operational compliance activity is typically left to the expert discretion of the regulator. If the quality and sophistication of regulatory practice is to be improved in New Zealand across the board, regulators must be able to call upon the leadership of those at the forefront of good practice, be able to share challenges and practices, and have access to leading practice guidance material. The Commission has recommended formal recognition of communities of practice and more sophisticated and targeted guidance material. The Commission’s recommendations are designed to build on the hard work and dedication of those individuals who have seen the practice of being a regulator as important and who have sought to improve the capability of regulatory agencies and those that work within them. The next chapter examines workforce capability.
12 Workforce capability

Key points

- Regulators need staff that combine generic and specific competencies, including specific technical expertise, personal competencies such as communication skills, and an understanding of the compliance role and the regulator’s role. The precise mix of competencies needed is likely to vary between regulators and even within a regulator at different times. It is management’s responsibility to identify the required mix and to ensure staff have the required competencies.

- Gaps in competencies can undermine the credibility of regulation and the achievement of regulatory outcomes. It is estimated that between 10,000 –14,000 people work in regulatory roles in New Zealand. There is limited data about their competencies or any gaps in competencies.

- The Commission’s survey of businesses reveals that only 23% of the firms surveyed agreed or strongly agreed with the proposition that “regulatory staff are skilled and knowledgeable” and only 25% agreed or strongly agreed that “regulators understand the issues facing your organisation”.

- New Zealand’s approach to developing the competencies of the people who work in regulatory roles is constructive, but with room for improvement. This approach is evolving within a broader review of New Zealand’s qualifications framework that provides a recognised need for change.

- The Victoria University of Wellington survey of Public Service Association (PSA) workers found that, compared with local government and district health board regulatory workers and non-regulatory workers, central government regulatory workers tend to:
  - disagree that they are given a real opportunity to improve their skills through training;
  - be less likely to perceive that they have sufficient job-related training;
  - show lower levels of agreement that their supervisors have helped them acquire additional job-related training or that they receive ongoing training that helps them do their jobs better;
  - be less satisfied with the number and quality of training and development programmes available; and
  - disagree that training and educational activities enable them to perform their jobs more effectively.

- A number of recommendations are made to build on the process of change already underway in developing the capability of the regulatory workforce in New Zealand. These recommendations are designed to:
  - reinforce capability development as a core management responsibility;
  - promote clarity about the roles and contributions of those seeking to improve workforce capability; and
  - put greater focus on workforce capability in reviews of regulator performance.

12.1 Introduction

This chapter focuses on a key aspect of the capability of regulatory agencies in New Zealand – the capability of the regulatory workforce. Other aspects of organisational capability – for example, adequate funding and effective leadership and culture – are discussed elsewhere in the report. This chapter focuses
on the competencies of people who work in regulatory agencies, their contributions to organisational capability and to regulatory outcomes, and how these can be improved.

This chapter uses the terms “competence” and “competencies” to describe the abilities, knowledge, expertise and skills required of regulatory staff. The combined competencies of regulatory staff across the regulatory sector are the sector’s “workforce capability”. The Commission found there was considerable debate in the sector about what competencies were required of regulatory staff, where the gaps were and how to improve workforce capability. There appears to be disagreement about many issues, including:

- whether the biggest need is to improve basic skills of front line staff, such as report writing, or whether senior managers have the most pressing competency gaps;
- whether training and the development of national qualifications should focus on generic or specific competencies;
- the best combination of formal and informal approaches to training;
- the return on investment from training, which is often hard to measure, and therefore hard to use as a tool for managers who are trying to decide how much to spend on training or where to direct the training budget;
- whether there should be extra incentives for staff to become qualified, extending even to making qualifications mandatory in some cases.

Underpinning some of the debate may be a lack of clarity about the objectives of some regulatory regimes (Chapter 4), or the compliance approach that the regulator has adopted (Chapter 11) which can then be reflected in an equivalent lack of clarity about the competencies that regulatory staff need.

While these issues are unlikely to be resolved quickly, the existence of this debate is a positive feature as it signals a recognised need for change. This chapter contributes to the discussion by:

- explaining why it is important that the workforce possesses both generic and specific competencies (Section 12.2);
- setting out the available information about the workforce (Section 12.3);
- describing how the approach to training and development is being transformed as part of a broader review of New Zealand’s qualifications framework (Section 12.4);
- suggesting ways to make the most of the recognised need for change (Section 12.5).

### 12.2 Competency requirements

This section describes the types of competencies that people working in regulatory roles need to have.

**Generic competencies**

A recent study found that almost all of New Zealand’s regulators carry out one or more of the following activities (National Compliance Qualifications Project, 2009, p. 22):

- gathering intelligence;
- licensing and certification processes, to ensure entities have the capacity to comply with regulations, usually before they are permitted to operate in a sector;
- education and persuasion, to inform people about regulations and encourage them to comply with them;
- audit, monitoring and surveillance, to assess compliance with regulations;
- investigations, to determine the facts of a matter, whether rules have been broken or not;
sanctioning non-compliance, to encourage future compliance.

To undertake these activities, people who work in regulatory roles need competencies – such as how to conduct an inquiry into an incident, gather information to make a case, conduct interviews, produce reports, and present evidence in court.

Communication skills are often important. Sparrow (2000) argues that process management and problem solving are also important. Similarly, the Compliance Common Capability Programme (CCCP) suggests that “modern compliance thinking suggests this is about problem solving and risk management” (sub. 2, p. 9).

Maritime New Zealand suggests that, in addition,

> the core capabilities required for regulators include an understanding of the machinery of government, application of law, objective decision making, analytical thinking, knowledge of investigation and a clear focus on the regulatory objective. (sub. 15, p. 3)

These competencies are particularly important for front line staff. Senior managers, who are responsible for ensuring that their organisations acquit their responsibilities effectively and for identifying improvement opportunities, require other competencies.

Effective regulatory managers understand why their organisation exists and the intervention logic through which it contributes to the economy. They are able to:

- work effectively within their governance framework by, for example, managing relationships with ministers and senior public servants;
- identify the mix of competencies that the organisation needs, and to develop recruitment, training and retention policies that deliver those competencies;
- establish organisational structures that capture synergies between different groups within the organisation, perhaps based on common objectives, competency sets, or client groups; and
- understand, and lead if necessary, processes for reporting and evaluating how well regulations and the organisation are performing.

They may need to apply these competencies, in situations where organisational objectives or organisational structures are changing.

**Specific competencies**

In addition to generic competencies, people who work in regulatory roles need to understand the area and the problem they are regulating. Increasingly, this requires people with multi-disciplinary skills. Determining whether there is misleading conduct as defined by the Commerce Act 1986 requires specialised expertise that differs from what is required to determine whether a building is structurally sound or food is safe. Regulators with area-specific knowledge are less likely to impose inconsistent and impractical demands (Meat Industry Association, sub. 40, p. 12), and are more able to build credibility (New Zealand Council of Trade Unions, sub. 25, p. 24). The New Zealand Food and Grocery Council indicated that it strongly supports much greater experience by public servants of business issues and suggests that such experience form the base for, or be given, weight in, future recruitment activity in areas regulating industry activity. (sub. 35, p. 7)

**Generic and specific competencies are both needed**

Neither generic nor industry-specific regulatory competencies are sufficient on their own. The Ministry of Transport observes, having an “amalgam of very different skill sets can be what matters for regulatory success” (sub. 39, p. 6). Similarly, the Civil Aviation Authority suggested that while regulators can recruit technical expertise, such people still need to be trained as regulators (sub. 6, p. 39).

Box 12.1 illustrates how, even in a specialised area (regulation of medical devices), a combination of generic and specific skills is needed.
The approach to regulation affects competency requirements

The best combination of competencies may vary depending on the type of regulatory standard that a regulator applies. Chapter 4 identified four main regulatory standards, each with its own strengths and weaknesses, and suited to different circumstances:

- principle-based regulation;
- performance/outcome-based regulation;
- input-based/prescriptive regulation; and
- process or system-based regulation.

For example, performance/outcome-based regulation is suited to situations in which firms are better placed than regulators to determine the best way to comply with regulation, and when innovation can discover less costly ways of complying. Input-based/prescriptive regulation is more effective when regulated entities do not have the ability or need to be innovative in complying and when the level of harm from non-compliance is unacceptable.

The appropriate mix of competencies for regulatory staff varies between these situations. Those who are inclined to focus on enforcing strict compliance with rules are likely to be most effective in administering prescriptive regulation. On the other hand, effective administration of performance/outcome-based regulation is likely to draw more heavily on, for example, good communication and judgement skills. Except in those few cases where the regulated outcome can be tightly defined and measured, regulators applying outcome-based standards need to make judgements about whether regulated entities can achieve the desired regulatory outcomes, without prescribing how they should do this. An example is in Box 12.2.
The appropriate combination of competencies is likely to vary between regulators and regulatory regimes, and may change within a regulator or regime, if the approach to regulation evolves over time.

Summarising the views of submitters and the preceding discussion, Figure 12.1 captures the competencies required of regulatory staff. Each piece of the jigsaw is likely to contain both generic and specific competencies. The relative size of each piece of the jigsaw will vary depending on the nature of the regulation and the role the staff member has within the regulatory agency. For example, managers need greater competency in understanding the role of the regulatory regime, while front line staff need a greater understanding and competency relating to the compliance role. Even so, sector leaders and people engaged in training regulatory staff were of the view that all of the pieces of the jigsaw should be required competencies of regulatory staff (to varying degrees) and, when taken as a whole, these pieces represented the competencies that together defined a capable workforce.

**Box 12.2 A prescriptive approach versus a performance approach to inspecting fire sprinklers**

A prescriptive approach to fire sprinkler regulations would typically specify the type and placement of sprinklers in a building. The inspector would take a tick-box approach to ensure the right number of sprinklers per square metre were placed in precise locations.

A performance approach to fire sprinkler regulations would lead the inspector to ask: “Will the number and placement of the fire sprinklers in this building do the required job in the event of a fire?” While the sprinklers might not be in exactly the recommended format (for example, due to internal partitions, other piping in the ceiling), the building might still meet the requirements.

The competencies required of fire sprinkler inspectors in each case is quite different. Under prescriptive regulation, the inspector must know the rules; under the performance-based regulation, the inspector must know the circumstances in which fire sprinklers will be effective (which implies some technical knowledge and the ability to exercise judgement based on that knowledge).

The CCCP - a collective of local and central government agencies with regulatory functions - considers that people capability is variable across New Zealand’s regulatory sector. This, combined with the broader problem of variable organisational capability, can:

Why competencies matter

It is easiest to explain why competencies matter for achieving regulatory outcomes by considering what happens when the combination or level of competencies within an organisation is deficient.
• create integrity and reputation risks for the regulatory compliance sector and individual agencies;

• mean activities are not always performed to an acceptable standard, resulting in poor compliance outcomes/regulatory failure;

• create inefficiencies through poor use of resources, as work is not performed efficiently and effectively;

• add to the cost of compliance, because of the high cost of system failures compared with effective performance;

• contribute to harm, including serious harm to people, the environment and the economy;

• indicate missed opportunities to share innovative ideas and best practice solutions; and

• lead to inconsistent approaches to carrying out regulatory compliance functions that create public confusion about the purpose of regulatory compliance and the role of regulation (sub. 12, p. 4).

Maritime New Zealand identified problems with the current system:

There is no unified system of training and educating people in regulatory practices, which results in varied and patchy delivery and in some cases a lack of clarity about the role and function of the regulator (or even regulatory capture). People recruited from industry specific sectors, such as the specialist maritime environment, are often not trained in such core competencies. With limited induction they are deployed as regulatory inspectors and find it challenging to deliver to expectations. In some instances their specialist knowledge is crucial but their ability to engage with industry in an impartial, objective and distanced yet constructive manner can be challenging. (sub. 15, p. 3)

While major regulatory failures usually have complex and multi-dimensional causes, inadequate workforce capability can be a contributing factor (Box 12.3).

Box 12.3  Findings of the Royal Commission Report on the Pike River Coal Mine Tragedy

Following structural changes within government, the mining inspectors who were responsible for all 1000 or so coal and metalliferous mines, tunnels and quarries fell within a department responsible for inspecting almost all New Zealand workplaces. They became part of the body of approximately 140 warranted health and safety inspectors, who were mainly generalist inspectors but could access technical expertise.

The inspectors were not required to have expertise in the mining method used by the mines they inspected. This meant that neither mechanical inspectors nor those with expertise in workplace fatigue were inspecting underground coal mines. The department did not have enough expertise to inspect the range of major hazards in underground coal mines, including geological, geotechnical, strata, spontaneous combustion, poor ventilation, methane and electrical.

Mining inspectors were required to meet prescribed qualification and experience criteria that are not specific to underground coal mining. They were required to hold a first class mine manager’s certificate of competence and initial training was provided in such topics as legislation, compliance assessment and prosecution. This did not focus on underground coal mines and was not taught by people with mining expertise. Ventilation training was “based on ventilation principles in normal workplaces like factories or warehouses”. The compliance training did not focus on complex mine systems.

There was no requirement for ongoing professional development. There were training deficiencies in hazard identification, auditing, workplace culture, management practices, emergency response, inspections and investigations. A review undertaken for the Commission stated that “the mines inspectors felt particularly disadvantaged, seeing themselves as specialists within a generalist inspectorate which did not see the need to equip them with mining specific skills they needed”.

Regulators need staff who, as a group, combine generic and specific competencies, including specific technical expertise, personal competencies such as communication skills, and an understanding of the compliance role and the role of the regulator. Gaps in these competencies can undermine the credibility of regulation and the achievement of regulatory outcomes. The precise mix of competencies needed is likely to vary between regulators and even within a regulator at different times. It is management’s responsibility to identify the required mix of competencies and ensure staff have, or can develop, these competencies.

What firms think about the competence of regulators

The Commission’s survey of businesses revealed that only 23% of the firms surveyed agreed or strongly agreed with the proposition that “regulatory staff are skilled and knowledgeable” (Figure 12.2) and only 25% agreed or strongly agreed that “regulators understand the issues facing your organisation” (Figure 12.3). The results for the rural sector are particularly worrying: 40% of the businesses from the agriculture, forestry and fishing sector surveyed, and 38% of all rural businesses surveyed, disagreed or strongly disagreed with the statement that “regulatory staff are skilled and knowledgeable”.

Figure 12.2  Regulatory staff are skilled and knowledgeable

<table>
<thead>
<tr>
<th>2%</th>
<th>21%</th>
<th>37%</th>
<th>19%</th>
<th>8%</th>
<th>13%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>Agree</td>
<td>Neither agree nor disagree</td>
<td>Disagree</td>
<td>Strongly disagree</td>
<td>Don’t know</td>
</tr>
</tbody>
</table>

Source: Colmar Brunton, 2013.

Figure 12.3  Regulators understand the issues facing your organisation

<table>
<thead>
<tr>
<th>2%</th>
<th>21%</th>
<th>30%</th>
<th>28%</th>
<th>9%</th>
<th>8%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>Agree</td>
<td>Neither agree nor disagree</td>
<td>Disagree</td>
<td>Strongly disagree</td>
<td>Don’t know</td>
</tr>
</tbody>
</table>

Source: Colmar Brunton, 2013.

The Commission’s survey found a more encouraging situation in relation to communication. In the last 2 years, 40% of the surveyed businesses spent significant time and resources on finding out about regulatory requirements and 25% applied for consents and approvals. Of those surveyed, 43% said that interactions with regulatory compliance officers were friendly and non-combative (Figure 12.4) and 37% of those surveyed agreed with the statement that “regulators communicated well with your organisation”.

Figure 12.4  Interactions with regulatory compliance officers (such as inspectors) were friendly and not combative

<table>
<thead>
<tr>
<th>3%</th>
<th>40%</th>
<th>33%</th>
<th>10%</th>
<th>2%</th>
<th>12%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>Agree</td>
<td>Neither agree nor disagree</td>
<td>Disagree</td>
<td>Strongly disagree</td>
<td>Don’t know</td>
</tr>
</tbody>
</table>

Source: Colmar Brunton, 2013.
12.3 Characteristics of the work force

Size

Estimates of the size of the regulatory work force differ, but indicate that it is large.

- The National Compliance Qualifications Project (NCQP) estimated, drawing on Census data, that there were about 14,000 workers in the compliance sector in 2006. This includes large agencies, such as the police and the Inland Revenue Department. The NCQP suggested that with turnover of about 11%, 1,320 jobs are taken up by new position holders per year (2009, p. 19). It also found that the overwhelming majority (about 87%) of employees were practitioners or senior practitioners, whose tasks might include conducting compliance activities, ensuring agencies are meeting required legislative standards, and investigating and preparing prosecutions (NCQP, 2009, p. 31).

- The State Services Commission’s human resource capability survey reports that in 2012 there were 2,350 information professionals and 8,698 inspectors and regulatory officers – which are the two survey categories that relate directly to compliance work (Kimberley, 2012, p. 8).

- The 27 agencies that responded to the Commission’s request for information have a total of 4,630 full-time equivalent staff “directly involved in the implementation of regulation”. About half of these people work in the Ministry of Business, Innovation and Employment (MBIE), which includes immigration staff and, at the time the information was gathered, included people who have now moved to Worksafe.

Where do regulatory staff work?

Table 12.1 illustrates the distribution of the workforce between regulators. MBIE dominates the staff count, because it has primary responsibility for overseeing 16 regulatory regimes. Most regulators have more than 50 staff, although there are 10 regulators in the “other” category that have 70 full-time equivalent staff in total. Maintaining a combination of specific and generic skills is likely to be a challenge for small regulators.

<table>
<thead>
<tr>
<th>Number of staff directly involved in the implementation of regulation (full-time equivalents)</th>
<th>Agencies</th>
</tr>
</thead>
</table>
| 0-4 | New Zealand Walking Access Commission  
Commission for Financial Literacy and Retirement Income  
Ministry of Transport  
Broadcasting Standards Authority |
| 5-9 | Energy Efficiency and Conservation Authority  
Takeovers Panel  
Gas Industry Company Limited |
| 10-19 | New Zealand Historic Places Trust  
Office of the Privacy Commissioner  
Office of Film & Literature Classification |
| 20-49 | Reserve Bank of New Zealand  
Electricity Authority |
| 50-99 | Health and Disability Commissioner  
Maritime New Zealand  
Environmental Protection Authority |
Number of staff directly involved in the implementation of regulation (full-time equivalents)

<table>
<thead>
<tr>
<th>Agencies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Markets Authority</td>
</tr>
<tr>
<td>New Zealand Qualifications Authority</td>
</tr>
<tr>
<td>Department of Internal Affairs</td>
</tr>
<tr>
<td>New Zealand Commerce Commission</td>
</tr>
<tr>
<td>Civil Aviation Authority</td>
</tr>
<tr>
<td>Statistics New Zealand</td>
</tr>
<tr>
<td>Land Information New Zealand</td>
</tr>
<tr>
<td>Ministry of Business, Innovation and Employment</td>
</tr>
</tbody>
</table>

Source: Productivity Commission information request to New Zealand regulators.

Notes:
1. Two agencies were unable to provide numbers of staff in regulatory roles: Department of Conservation and Ministry of Education.

Profiles of employees

Compared with the general workforce, the regulatory services sector has:

- a slightly higher proportion of employees of European origin;
- a relatively older aged workforce; and
- a larger proportion of male employees (Kimberley, 2012, drawing on Statistics New Zealand).

Where are regulatory staff recruited from?

In Australia, about 50% of regulators surveyed by the Australian Productivity Commission (APC) reported hiring staff with skills or experience in law enforcement and about 40% reported hiring staff with skills in education and training. Where many staff have a law enforcement background, this tends to be associated with a stricter and less flexible approach to compliance (APC, 2013, pp. 190-91). While the Commission has not found similar data for New Zealand, it has heard that it is common for regulators, particularly in the customs and biosecurity control areas, to recruit people from the police, and that people with law enforcement backgrounds often become trainers. The MPI provided an estimate: of the 206 FTEs in the Compliance Directorate, in the Inspectorate/Investigation component about 45 of the 170 staff have a police background. At the L 4/5 level of management (Regional Managers/District Compliance Managers), 8 of the 19 management positions are former police.

The APC also found that about 50% of surveyed Australian regulators have hired people who have worked in a business in the area that the agency regulates. This may also be common in New Zealand. Maritime New Zealand pointed out that “many regulators employ individuals from the industries they regulate” (sub. 15, p. 3). Business NZ, on the other hand, considers that there need to be more regulators with private sector experience:

We believe the public sector as a whole requires a greater number of employees with significant private sector experience so they can bring their own insights into regulatory decision making and pick up on potential unintended consequences. A halfway house for this might be the increased use of secondments between the private and public sector, whereby private sector experts from certain entities are brought in to assist on issues from a market perspective. (sub. 19, p. 12)

Some regulators see themselves as operating in a global market for talent. This is particularly the case in the finance sector, where the Reserve Bank of New Zealand (sub. 9, p. 7) and the Financial Market Authority (sub. 53, p. 7) referred respectively to their vulnerability to losing specialist staff and difficulty in attracting people from overseas. It is also the case in the aviation sector, where the Civil Aviation Authority and Aviation New Zealand noted that the aviation regulator must sometimes match private sector or
international salaries (sub. 6, p. 39; sub. 36, p. 29). IPENZ also noted that, particularly in technical areas, the Government is competing in a global marketplace (sub. 21, p. 8). The Ministry of Transport pointed out that it can be hard to maintain technical skills and knowledge in areas such as road safety or aviation design, particularly where there are skill shortages in the relevant industry and market salaries are high (sub. 39, p. 6).

Being part of a broader job market creates challenges for regulators, to train people from different backgrounds and to offer career pathways and rewards that attract and retain qualified staff. A regulator with high staff turnover will find it hard to maintain the balance of competencies and knowledge that it needs.

Qualifications

Being qualified is not the same as being competent. People without qualifications may have learnt from experience how to perform competently, and people with qualifications may perform poorly if they lack other competencies. Even so, qualifications are an indicator of the capability of the workforce.

People working in the compliance sector can access a wide variety of qualifications, ranging from masters-level degrees to lower-level certificates. In 2009, the NCQP found that these included:

- a range of national qualifications, some of which directly address practitioner needs;
- specialist qualifications, such as law and taxation degrees; and
- 27 New Zealand national qualifications that have some form of compliance-related purpose.

In addition to these qualifications, 38 generic and 130 agency-specific, compliance-related public sector unit standards were identified as potentially useful for creating further qualifications – either to be used directly in new qualifications or as reference material to support the writing of new standards (NCQP, 2009, p. 10).

Kimberley (2012) lists 22 national certificates, certificates or diplomas available to the compliance sector, and notes that the NCQP identified additional qualifications that could be relevant for compliance roles.

Completion rates of some compliance and regulatory control qualifications were very low over the 6 years to 2012:

Two of these qualifications have only been completed one time over the past six years, with three others ranging from 6 to 14. This shows a lack of current demand by the industry in these qualifications as they stand. (Kimberley, 2012, p. 29)

More popular were the Level 2 Animal Control Qualifications (averaging 15 completions each year), the Level 3 parking enforcement qualification (peaking at 29 completions in 2009, although dropping to 6 in 2011), and the Level 3 Foundation qualification (152 completions by November 2012) (Kimberley, 2012, pp. 29-30). More recent data provided by The Skills Organisation indicates that 65 trainees from central and local government (excluding New Zealand Police trainees) completed qualifications within the public sector compliance field between August 2012 and January 2014 (The Skills Organisation, 2014a, p. 6).

There is little information about the proportions of regulatory staff with qualifications. A survey by the NCQP, of the prerequisites for employees at different levels in 16 agencies, found that the most important prerequisite for senior practitioners is evidence of experience in the compliance sector, although a qualification in a compliance discipline is also valued for some roles. The practitioner occupational level contains the broadest range of possible prerequisites, with certification or specific training featuring most strongly (NCQP, 2009, p. 37). However, there is no general requirement for people working in regulatory compliance roles to be trained or qualified to an industry-wide standard (CCCP, sub. 12, p. 2).

F12.2 There is limited information about qualifications held by the workforce in the compliance sector. The proportion currently enrolled in training for qualifications appears to be small.
Views about the adequacy of staff competencies and training

People who work in regulatory roles and their chief executives seem to have different views about the adequacy of staff competencies and training. The Commission’s survey of 23 chief executives found that only 5 agreed with the statement that there are “significant capability or skill gaps among regulatory staff”, while 10 disagreed with the statement, 7 neither agreed nor disagreed and 1 didn’t know. On the other hand, the Victoria University of Wellington survey of Public Service Association (PSA) workers found that, compared with local government and district health board regulatory workers and non-regulatory workers, central government regulatory workers:

- tend to disagree that they are given a real opportunity to improve their skills through training;
- are less likely to perceive that they have sufficient job-related training;
- show lower levels of agreement that their supervisors have helped them get extra job-related training or that they receive ongoing training that helps them do their jobs better;
- are less satisfied with the number and quality of training and development programmes available;
- tend to disagree that training and educational activities they have received enable them to perform their jobs more effectively.

The CCCP considered that there is less focus on professional identity among regulators than there is among equivalent professions:

Even those who work in the regulatory compliance sector do not necessarily appreciate that they are part of a sizeable (12,000+ member) community of professionals. Equivalent industries (real estate agents, building practitioners, accountants, lawyers) are recognised professions with associations or networks to support the industry. The regulatory compliance sector does not have that same level of professional identity and support. (sub. 2, p. 3)

12.4 Current approach to improving competencies

The approach to developing competencies in the compliance sector is evolving in the context of a broader review of New Zealand’s qualifications framework. The review found that the national qualifications system as a whole was hard for learners, employers and industry to understand. The review recommended a package of seven changes. The Board of the New Zealand Qualifications Authority has approved the package (Box 12.4).

Box 12.4 A package of seven changes

The seven agreed changes are:

- establish a unified New Zealand Qualifications Framework (NZQF);
- require the use of existing quality-assured qualifications, and change the design rules for National and New Zealand qualifications to allow for more inclusion of local components;
- require mandatory specific reviews of qualifications to determine whether they are still fit-for-purpose;
- strengthen and standardise qualification outcome statement requirements;
- introduce a mandatory pre-development assessment stage for qualification developers;
- strengthen industry involvement in qualification development; and
- provide clear information about whether a qualification is active, inactive or closed.
The “package of seven changes” has triggered movement towards a comprehensive framework of qualifications for regulatory staff, and has highlighted the roles of the sector’s industry training organisation (ITOs) and sector representational groups in developing the framework, the service providers that deliver training, and government subsidisation of some training. Other significant initiatives to boost competencies, which are separate from the package, include legislative change, collaboration between agencies and guidance material.

Towards a comprehensive framework of compliance qualifications

As noted earlier, regulatory staff can access many different qualifications. The NCQP noted in 2009 that because most regulators carry out similar activities, there is a case for developing qualifications based on core competencies. This would lead to common standards being articulated across the compliance sector, creating a more cohesive and integrated workforce and helping agencies work more effectively together (NCQP, 2009, p. 24). The sector, through the CCCP (see below) began work on developing a set of national qualifications. However, these qualifications were overtaken by the Targeted Review of Qualifications (TROQ) that began in early 2011, in line with the third element of the package outlined in Box 12.4.

The Skills Organisation (which is the designated ITO for the sector and whose role is described in more detail below) has been leading the change process, creating representative groups to review and rationalise current qualifications, to move from the task-oriented focus of previous qualifications to a focus on learning outcomes that learners need to demonstrate to achieve a standard. (Box 12.5 provides an example of learning outcomes.)

The first stage of the TROQ review has been completed and the NZQA has granted The Skills Organisation approval to develop new qualifications by the end of 2014. The qualifications will be at different levels, so one challenge is to define the standards required at each level and to establish pathways for moving from one level to the next level. The transition arrangements for candidates, including credits for existing qualifications, will be determined during qualification development (The Skills Organisation, 2014a). Once these qualifications are developed, they will be re-submitted to the NZQA for accreditation.

Industry Training Organisations

The three main roles of an ITO are to:

- design national qualifications and run moderation systems to ensure fair, valid and consistent assessment against national standards;
- arrange the delivery of industry training that enables trainees to attain qualification standards; and
provide leadership to their industries on skill and training matters, identify current and future skill needs, and work with employers and employees to meet those needs.

To fulfil these roles, the Government expects that ITOs will:

- work with industry to ensure that vocational learning meets industry needs;
- enable working New Zealanders to complete nationally recognised qualifications;
- create clear pathways towards advanced trade qualifications at levels four and above; and
- build and maintain strong support from the industries they serve. (Nana et al, 2011, p. 2).

The 14 ITOs have each been allocated a number of industries. The Skills Organisation – formed in late 2012 – has a legislated mandate to facilitate workplace-based education for central and local government, including regulators, and for other industries. Funded by Government, The Skills Organisation helps central and local government organisations develop their workforce, and has access to government-funded industry training providers (The Skills Organisation, 2014a, p. 3). Managing the national training system for its allocated industries involves:

- developing and maintaining national qualifications and unit standards;
- managing industry training arrangements;
- designing and managing national quality assurance mechanisms for assessment;
- developing implementation and assessment resources; and
- directing government funding to the industries engaging in national qualifications training.

The Skills Organisation offers two types of assessment for its national qualification programmes: workplace assessment and assessment of prior learning. Workplace assessment enables employees to gain credits for a unit standard, based on evidence that is collected and recorded in the workplace. Assessment is carried out by assessors, who are registered, trained and moderated by The Skills Organisation. Assessment of prior learning involves a formal evaluation of previously unrecognised skills and knowledge, achieved outside the formal education and training system, against the requirements of unit standards and qualifications (The Skills Organisation website). This provides a pathway for people who have learnt “on the job” to transform their experience into qualifications.

Box 12.6 provides an example of the work of The Skills Organisation.

**Box 12.6 Competence requirements for financial advisers**

When legislation was introduced to regulate financial advisers, The Skills Organisation worked with the Financial Markets Authority (FMA; then the Securities Commission) to help it to understand the NZQA framework and the associated risks and safeguards. The Skills Organisation worked with the group that set the minimum standards of competence for authorised financial advisers, to understand the existing unit standards. Where gaps were found between these standards and the new competence requirements, The Skills Organisation facilitated a discussion between the industry and the regulator to agree on the content of the new unit standard. The qualification was then set by the regulator (as a minimum standard for authorisation).

As some financial advisers held other qualifications, The Skills Organisation helped to develop exemptions. At the request of the regulator, two groups of unit standards were reserved for assessment through a common assessment. The Skills Organisation worked with the industry to create the assessments and ensure the system met the needs of the regulator. It also encouraged training providers to meet the training needs, and it quality assured their assessments.

Achievement of the groups of unit standards and of whole qualifications is reported on a set schedule.
The Common Compliance Capability Programme

The CCCP is a collective of local and central government agencies, which as noted earlier recognised an opportunity to improve the quality, effectiveness and efficiency of compliance work across central and local government agencies by building the capability of organisations and people. Eight member agencies have committed base funding to support the programme through to June 2014.

The programme has two main initiatives: a guide for compliance agencies in New Zealand, and developing a set of national compliance qualifications.

- **Achieving Compliance: a Guide for Compliance Agencies in New Zealand:** Published in June 2011, this brings together good practice organisational and operational design, strategy and practice for operational regulation and compliance work. The target audience includes senior managers, operational managers and compliance officers in central and local government agencies.

- **National compliance qualifications:** The CCCP had developed draft national qualifications, but is now working with The Skills Organisation (and the Police, the Open Polytechnic, and UNITEC) to develop new qualifications through the TROQ process.

The CCCP considers that formal qualifications need to be supported by fit-for-purpose learning programmes and other initiatives for sharing knowledge, such as collaborative workgroups, seminars, forums and briefings. It is trialling “regulatory practice forums” (discussion groups on relevant topics) for operational staff and plans to map current learning and development initiatives across the sector, and to indicate potential priorities for development/support. Some agencies are combining resources to deliver a Basic Investigations Skills learning programme, which will be made available to other agencies.

The CCCP is developing a Regulatory Practice Skills Framework, which, when completed, will attempt to look across all the roles involved in regulatory work and determine the skills that the regulatory workforce needs. This will help with creating learning and assessment materials. The CCCP describes the framework as a warehouse – a place to store information about the skills, knowledge and attitudes required to develop capability in regulatory work. Some of this skill information will be used to create specific learning resources and assessment tools to help people develop the capability they need to carry out regulatory work.

The CCCP’s framework is intended to fit with the national qualifications framework in two ways. First, it is intended to be used to create learning programmes that can be used as a pathway for achieving national qualifications. Second, it covers other areas that are important but that would not be covered by a national qualification – perhaps because the skill area only applies to a small number of people, or is very specific and specialised, or is emerging, or because a particular organisation requires a higher standard than the national qualification expresses (personal communication, 29 January 2014).

Training providers

Training is available from a variety of providers. The Skills Organisation contracts the services of five accredited providers for public sector compliance and compliance and regulatory control qualifications. It also works with several regulators that have their own internal assessor for compliance qualifications. The CCCP also has a list of 11 recommended providers for compliance qualifications (The Skills Organisation, 2014a, p. 2), some of which may offer training in courses not accredited by the NZQA. (Box 11.8 describes some of the training provided by one of these providers.)
Employers can also send staff to universities and polytechnics, for professional training that is outside the national qualifications framework. Some larger regulators provide in-house training, particularly in general compliance and enforcement skills and in skills specific to their area of regulation. For example, the Waikato Regional Council told the Commission that it had decided some years ago that it needed to provide its own in-house training to meet its specific needs.

Professional organisations may also provide training (Box 12.8).

Box 12.8  Professional organisations’ involvement in training regulators

The New Zealand Institute of Environmental Health represents those engaged in the environment and health protection. One objective is to arrange opportunities and facilities for members to meet and exchange knowledge and information.

The Building Officials Institute of New Zealand has represented Building Control Officials in New Zealand since 1967. Its goal is to improve their competency. Through its Diploma and Continuous Professional Development based courses, the Institute provides training for the Diploma in Building Control Surveying and further qualifications, to enable those in the profession to maintain, upgrade and update their skills throughout their working life.

The New Zealand Institute of Animal Control Officers is an incorporated society consisting of practising animal control officers from throughout New Zealand. It organises annual training conferences.

The objectives of the New Zealand Parking Association (Inc.) include ensuring that enforcement officers are trained to the highest possible standard nationwide, and to collect and disseminate information that will keep member authorities and individuals well informed.

Funding
Part of the cost of training is “in kind” (for example, replacement labour to cover people who are away, and the time of supervisors acting as mentors or as on-the-job tutors), and is usually borne by employers (Nana et al, p. 9). For courses accredited by the NZQA, The Skills Organisation receives funding from the Tertiary Education Commission (TEC), some of which is used to reduce the course costs paid by the employer (or trainee) after subtracting an allowance for The Skills Organisation’s costs. Funding is provided on the basis of whole qualifications, rather than for individual units.

The standard duration of accredited courses is between 10 and 25 months. The TEC provides funding, of between about $1,400 and $3,900 per course, for each participant who completes a course. This is paid to The Skills Organisation, which retains 30% to pay for its costs. Fees that training providers charge each course participant mostly vary between $2,000 and $3,800. The provider then recoups this from TEC funding that is passed through to it by The Skills Organisation, and from the fees paid by the course participant or by their employer (The Skills Organisation, 2014a).

Legislative change
The CCCP considers that recent changes to legislation should provide a stronger foundation for effective system-wide effort to capability development (sub. 12, p. 2). For example, the purpose statement of the State Sector Act 1998 includes a requirement to promote and uphold a state sector that, among other things, is supported by effective workforce and personnel arrangements, meets good-employer obligations, and is driven by a culture of excellence and efficiency (s. 1A).

The PSA also considered that recent changes “offered some potential”, but felt that they would not adequately address fragmentation between agencies: “More needs to be done and strong leadership from the centre will be required” (sub. 26, p. 2).

Collaboration between agencies
Regulators can join forces with other agencies with similar or complementary competency requirements. For example, the Border Sector Governance Group and the Wildlife Enforcement Group are formal alliances between agencies seeking common outcomes. Other agencies have memoranda of understanding about how they work together. Less formal arrangements include networking and information sharing opportunities fostered through professional organisations (NCQP, 2009, pp. 26-27).

Sometimes the collaboration is international. For example, the Australasian Environmental Law Enforcement and Regulators Network (AELERT) is a collective of environmental regulatory agencies from Australian and New Zealand Governments at local, state, and federal levels. AELERT provides platforms for environmental regulators to work together and exchange information and knowledge. For example, “thematic cluster groups” undertake projects based on needs identified by members, who also participate in online forums and have access to a resource library (www.aelert.com.au).

Guidance material
Guidance material about how to implement good processes and administer regulations can improve the consistency and quality of regulation. The APC considers:

Staff should have ready access to a policy and procedures manual to provide guidance on matters such as: regulatory objectives; the application of a risk management framework; conduct of investigations; available enforcement actions and when they should be used; the appropriate use of discretion; record keeping; dispute resolution; and review processes. With appropriate oversight and transparency arrangements in place to ensure they are adhered to, such guidance documents can improve the quality and consistency of processes and decisions, to the benefit of both regulators and business. (APC, 2013, p. 192)

The foreword to the CCCP’s compliance guide suggests that its purpose is to

… support compliance agencies to develop and constantly improve the way they work by capturing and sharing information that enables this to occur. (CCCP, 2011, p. 1)
An international comparison

The approach to competency development for regulators in the United Kingdom has some interesting points of comparison with New Zealand (Box 12.9). A government agency (the Better Regulation Delivery Office or BRDO) has a leading role in developing generic and technical competency frameworks and learning tools, with advisory support from a group of regulators and government departments. There appears to be considerable reliance on self-assessment of development needs and on web-based learning.

Box 12.9 The approach to competency development in the United Kingdom

Professional development and culture change by regulators are supported by the introduction of a common approach to competency, which is intended to be a single, definitive and comprehensive means of addressing professional competency. The approach is being led by the BRDO in partnership with the Regulatory Excellence Forum (comprising 22 departments and regulators), and is closely linked with the relevant qualifications frameworks supported by the professional bodies. Key features of the approach include:

- core, generic regulatory skills and leadership skills sections (assessing risks; planning, organising and prioritising; promoting compliance; advising and influencing; conducting interventions; enforcing legislation; working effectively with business, citizens and other stakeholders; using and managing knowledge effectively; IT literacy and numeracy);
- technical knowledge sections, specific to areas of regulation (11 frameworks have been developed in areas such as environmental health and trading standards, agriculture, fair trading, port health and product safety), and four more frameworks are in progress (gambling, intellectual property, noise, and underage sales);
- a self-assessment tool that lets regulators identify and prioritise their development needs;
- a portal website that directs regulators to relevant online sources to help them meet these needs; and
- a development process for regulators and managers.

The portal website describes the relative advantages of many types of learning methods, including coaching, directed learning, e-learning, formal training courses, industry events, mentoring, networking and project work. The website also sets out for each area core learning resources, training courses, further reading and other information.

Source: BRDO, 2013.

12.5 Summing up

Considerable activity is aimed at developing generic and specific competencies, within the context of the national review of the qualification system. Even so, the approach is evolving and informed opinion judges that further progress is needed.

The PSA considered that

[the profile of public sector training appears to have fallen away somewhat and the link between agencies and the industry training organisation is perhaps not as strong as envisaged. It appears that the training framework is not currently providing what is needed. (sub. 26, p. 2)]

According to the CCCP, current arrangements remain inadequate. It argued:

There is no requirement for people working in regulatory compliance roles to be trained or qualified to any kind of accepted sector wide standard, even though these people often work in high risk environments, and/or have statutory powers and carry out activities that deeply affect people and businesses.
The sector as a whole lacks mechanisms for: growing capability, enabling people to move easily between regulatory compliance functions within and between organisations, and sharing and optimising investment in training.

There is a considerable body of shared knowledge, practice, policy and process relating to regulatory compliance. Each agency invests (or can’t afford to invest) in its own training regarding this. Consequently, there is duplication of effort, potential waste, inconsistent standards of people development and missed opportunities for cross-sector knowledge sharing.

Standards of performance vary across similar regulatory activities. In some cases people are not prepared or supported to carry out their roles adequately.

In terms of resourcing, many agencies do their best on limited budgets. When financial resources get strained, training is often the first area to be cut or deferred. Fundamentally, people capability development is not always supported as a necessary and important long term investment to ensure good organisational performance.

Some training providers describe their experience of working in the sector as risky, as the sector swings between requiring their services to up-skill staff, then cutting budgets for external training and making do with in-house resources. Consequently, the sector is not serviced with comprehensive external training provision. (sub. 2, p. 2)

The Commission was also told that there is not an adequate process for keeping regulators up to date with the continual changes to the legal framework within which regulators work.

Overall, it appears that:

- New Zealand has a constructive and wide-ranging approach to developing the competencies of the people who work in regulatory roles;
- the approach is evolving in the context of the national reform agenda; and
- sector participants consider there is room to improve.

F12.3 The approach to developing the competencies of the people who work in regulatory roles is constructive and wide-ranging. However, the approach is evolving and sector participants consider there is room to improve.

12.6 Making the most of the recognised need for change

The broad national qualifications programme and its translation into specific programmes for the compliance sector provide a promising environment for further change. This section describes some ways to capitalise on this opportunity.

Capability development is a core management responsibility

Most of the recommendations in this section require action by the Government or by The Skills Organisation as the ITO. However, while they can provide a framework, it is the responsibility of managers to work within this framework to develop the competencies of their employees.

The APC recently argued that regulators should address gaps in staff skills and capacities by acting in four areas in particular. They should:

- focus on recruiting and retaining staff with the appropriate industry knowledge and mix of enforcement, investigative and communication skills;
- provide appropriate training and written guidance for staff, and monitor regulator practices for consistency with this guidance;
- facilitate opportunities for staff to improve their understanding of business practices and the nature and size of the compliance costs their engagement imposes on business; and
implement cooperative arrangements with other regulators that facilitate the sharing of knowledge and resources (APC, 2013a, p. 196).

The Commission considers that these are also core responsibilities of those who lead New Zealand’s regulators. Having an appropriate recruitment policy is a particularly important way to build up generic and specific competencies. As noted earlier, Business NZ considers more staff with a business background should be recruited. Vector suggested that the Commission include a recommendation improving internal capability by requiring or expecting regulators (potentially by way of performance criteria) to employ some staff with commercial expertise and/or an industry background. (sub. 29, p. 34)

In addition to having a sound recruitment policy, managers need to capture any potential benefits from improvements to the qualifications and training framework by taking advantage of what is on offer, and grasping the opportunities that it provides to strengthen the competencies of their employees.

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<td>• implement cooperative arrangements with other regulators that facilitate the sharing of knowledge and resources.</td>
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Clarify roles and responsibilities

Section 11.4 identified many different participants in the training area, including the NZQA, The Skills Organisation, regulatory agencies, a large number of training providers, and the CCCP. There seem to be potential overlaps between the roles of The Skills Organisation and the CCCP.

As described earlier, The Skills Organisation’s three roles are to:

• design national qualifications and run moderation systems to ensure fair, valid and consistent assessment against national standards;

• arrange for the delivery of industry training that enables trainees to attain qualification standards; and

• provide leadership to their industries on skill and training matters, identify current and future skill needs, and work with employers and employees to meet those needs.

The CCCP has been involved in similar areas, as it both designed national qualifications (before The Skills Organisation was established) and has accredited training providers. Rather than designing qualifications, it is now channelling its involvement through the working group set up by The Skills Organisation. Even so, it is also developing its own regulatory skills framework, which it expects will complement the national qualifications framework, and plans to map current learning and development initiatives across the sector.

The CCCP is considering its future shape, direction and resourcing in the first half of 2014 (sub. 12a). The CCCP considers that it should be given more permanency, a formal mandate with strengthened governance arrangements, and a “modest” level of resources. It suggests that its roles could be set out in terms of reference or in a charter, and could include:

• support for the development of people competency – including cooperative capability development initiatives and credentials (workshops, seminars, training courses, qualifications);
support for the development of organisational capability (practice leadership groups, guides, case studies, information-sharing forums); and

engagement with whole-of-government processes (such as the PIF process) to support ongoing assessment and improvement of regulatory practice as part of established processes for doing this.

The Skills Organisation has changed the landscape for the CCCP, and the CCCP’s current review of its role indicates recognition of the need to adjust. Its proposals, if accepted, would increase its influence considerably. If the CCCP is to be given a formal mandate and resources, the Government will need to consider proposals emerging from the CCCP’s review, and may find it easier to do so if the CCCP:

- identifies gaps in the current organisational framework and explains why it is in the best position to fill some of them;
- sets out its specific roles as either a provider of training services or an adviser; and
- explains the issues about which it would provide advice, and how it would ensure that its advice is broadly based from across the regulatory sector.

The CCCP would then be in a position to explain how much funding it would need and how its performance would be measured.

The CCCP could consider relevant overseas experience during its review. For example, the membership of the Regulatory Excellence Forum (REF) in the United Kingdom, which includes government departments, is similar to what the CCCP considers would be appropriate (Box 12.10). The REF’s role is limited to providing advice, while the CCCP appears to leave open the possibility that it would provide training services. The “areas of interest” in which the REF provides advice appear relevant to the CCCP’s aim of improving the quality, effectiveness and efficiency of compliance work across central and local government agencies. The membership and terms of reference of the REF are reviewed yearly, rather than having permanency.

**Box 12.10  The Regulatory Excellence Forum**

The REF exists to simplify and improve the complex regulatory system. Membership is open to organisations with a national interest in regulatory delivery. It currently has 20 members, drawn mainly from regulators, professional and industry associations and government departments. Meeting up to four times each year, its role is to advise the BRDO. Particular areas of interest include:

- identifying and exploring where there is commonality and alignment between regulators’ approaches that affect delivery of regulatory services at the national and local level;
- identifying, evaluating and disseminating good practice between national and local regulators;
- suggesting priority areas impacting on the regulatory environment for discussion/problem solving;
- identifying barriers and challenges to suggested improvements and areas of shared concern, and formulating collective solutions to tackle these;
- identifying approaches to better regulation and creating greater clarity around the benefits of better regulation and the work of regulators locally and nationally; and
- monitoring wider changes and horizon scanning to ensure regulatory delivery is viewed within the wider context.

That the Compliance Common Capability Programme uses its review of the organisation’s future shape, direction and resourcing to:

- identify gaps in the current organisational framework and explain why it is in the best position to fill some of them;
- set out its specific roles as either a provider of training services or an adviser; and
- explain the issues about which it would provide advice, and how it would ensure that its advice is broadly based from across the regulatory sector.

Map programmes and identify gaps

Identifying gaps in competencies and in programmes for improving them is a prerequisite for identifying where the largest returns on investment are likely. The Skills Organisation has provided papers to the Commission that indicate it is collecting and analysing this kind of information.

The Skills Organisation should coordinate effort to identify skill levels and gaps across the compliance sector and assess the adequacy of current programmes to fill those gaps.

Forums for sharing good practice

People who work in regulatory roles can develop their competencies by exchanging information about their experiences:

Regulator capacities can be strengthened where knowledge about what has been effective or has not worked well is shared and where regulators work cooperatively together to identify ways to overcome common problems. … Small regulators particularly stand to gain …. (APC, 2013a, pp. 203-204)

Forums often depend on the energy of a few committed individuals. This can be a strength, but it becomes a weakness if these people move on without having found a successor. Forums are likely to work best when they have organisational backing, are given a meaningful agenda of issues to consider, and are required to come up with proposals for action that senior managers then properly consider. This may be hard to achieve: best practice regulators may feel that they have little to gain by becoming involved and that forums may be dominated by “followers” with little to contribute. Some kind of central promotion of forums, by organisations such as the CCCP, may be needed to overcome this problem.

Appropriate groups of regulators should encourage forums aimed at sharing good practice among the regulatory workforce.

Accrediting training providers

In the future, The Skills Organisation will evaluate whether organisations seeking to deliver and assess against the NZQF unit standards and award NZQF qualifications, should be accredited, although it is the NZQA that awards the consent (The Skills Organisation, www.skills.org.nz). A single pathway to accreditation would promote consistent quality between training providers but can also reduce competition and diversity. The challenge is to set the accreditation standard and process so that it protects quality and consistency, but without unduly restricting competition. In its accreditation role, The Skills Organisation should seek both to maintain adequate quality and consistent standards, and to recommend for accreditation a number of service providers sufficient to promote diversity and competition.
That The Skills Organisation, as the accreditor of training providers, should seek both to maintain quality and consistent standards of provision, and to promote diversity and competition.

Performance reviews
Performance reviews can identify and spread good practices, discover areas for potential improvement, and strengthen regulators’ incentives to focus on developing their staff’s competencies. Publishing the reviews would let other regulators benefit from relevant findings. Such reviews could be undertaken in a number of ways. They are more likely to be effective if the sector is the driving force behind them, as regulators would more likely take on “ownership” for the findings and respond to them.

The PIF is an existing process used to test agencies’ fitness-for-purpose that could be used to review their approaches to building staff competencies. The PIF already includes questions about capabilities, and developing staff is one of the four areas considered under the topic of organisational management. The compliance sector already recognises that PIF reviews could be undertaken of regulators: the Achieving Compliance guide is intended to help agency managers meet the expectations set out in the PIF (Department of Internal Affairs, 2011, p. 23).

Few PIF reviews of regulators have been undertaken. Instead, government departments are most often reviewed. Given that regulators may be a small part of a department’s employment and responsibilities, there is a risk that they will be overlooked when PIFs are developed. If the Government considers that PIFs of individual regulators are not appropriate, it could consider commissioning ad hoc reviews modelled on the approach used in the PIF. This issue is discussed further in chapter 13.

Regulators’ performance in developing staff should be reviewed, either as part of the Performance Improvement Framework process or through commissioned reviews modelled on that process.

These recommendations are intended to build on the process of change that is already underway in developing the capability of the regulatory workforce in New Zealand. If this process is successful, it has the potential to contribute to the achievement of regulatory outcomes, by leading towards:

- a compliance sector that is focused on competency development;
- a well-respected national qualifications framework;
- an effective process for improving the competencies of the existing workforce and for training new people to be effective regulators;
- greater mobility between regulators; and
- more effective collaboration between regulators in relation to competency development.
13 Funding regulators

Key points

- The way that regulators are funded can affect the efficiency of resource use, equity and the achievement of policy outcomes.

- The Commission’s survey of businesses, and submissions to the inquiry, reveal concern in the business community about:
  - the quality of the consultation before regulatory fees or levies are introduced;
  - weak constraints on the level of charges; and
  - the structure of charges.

- While in principle there can be benefits from regulators recovering some costs through fees or levies, case-by-case assessment is required to secure these benefits in practice. The framework for choosing between sources of funding needs to encourage this to happen.

- The funding frameworks in selected jurisdictions are similar to New Zealand in that they:
  - set out efficiency and sometimes equity as the main objectives of cost recovery;
  - require consent, usually of a minister or Parliament, before a fee or levy is introduced; and
  - are based on a distinction between cost recovery and taxation.

- There are, however, examples in other jurisdictions of:
  - more rigorous consultation and impact assessment before fees are introduced;
  - more detailed advice about how to implement cost recovery;
  - stricter requirements for performance standards and reporting against those standards; and
  - penalties for failing to achieve the standards.

- There is scope to improve New Zealand’s approach to cost recovery through strengthening the governance and accountability framework, by:
  - publishing the Government’s cost recovery policy;
  - making portfolio ministers responsible for ensuring that agencies within their portfolio have complied with that policy – also chief executives of agencies proposing a new or amended fee or levy for regulatory services should be required to certify that their agency has made adequate use of the Treasury Guidelines;
  - strengthening performance reporting;
  - amending the role of the Regulations Review Committee and increasing the number of audits of cost recovery by the Office of the Auditor-General;
  - introducing regular reviews of regulators’ cost recovery practices;
  - improving the implementation of cost recovery by refreshing and rationalising the guidance material, and ensuring adequate departmental advice is available to regulatory agencies about how to approach cost recovery.
13.1 Introduction

Regulators can be funded from various sources, including Crown contributions; levies on the regulated industry; or through fees imposed either on the beneficiaries of regulation or on those who cause the “problem” that needs to be regulated. How regulators are funded can affect the outcomes of regulation and the efficiency with which these outcomes are achieved. The funding of regulators may also interact with other regulatory design features, such as independence, engagement, accountability, and transparency. And some ways of funding regulators are likely to be seen as fairer than others. Many countries, including New Zealand, have established frameworks whose purpose is to assist those designing and implementing regulation to select the appropriate sources of funds.

This chapter describes New Zealand’s approach to funding regulators (Section 13.2) and assesses it from three perspectives:

- insights from economic analysis (Section 13.3);
- issues raised by inquiry participants (Section 13.4); and
- lessons from other jurisdictions (Section 13.5).

This analysis suggests that New Zealand’s framework for funding regulators has many positive features, although the Commission has found little evidence about how well it is working. Economic analysis suggests that, in principle, recovering some costs of regulation through fees is beneficial. But poor implementation can undermine the benefits. Some business participants consider that implementation risks are evident in New Zealand. Other jurisdictions use a variety of approaches to reduce these risks.

Overall, the chapter argues that while there is not a major problem with the approach to funding regulators in New Zealand, there are opportunities to improve it that would apply equally to new and existing regulators (Section 13.6).

13.2 The approach to funding regulators in New Zealand

Sources of funding

The Commission has found no data to show how New Zealand’s regulators, as a whole, are funded. However, 19 departments and other regulators that the Commission contacted provided data. That information shows that:

- six are fully funded by Crown funding and 13 receive funding from both Crown funding and fees, levies, and/or other sources of revenue;
- there are numerous Acts for which the regulator is fully or nearly fully funded from fees or levies, including the Building Act 2004, the Cadastral Survey Act 2002, the Health and Safety in Employment Act 1992, the Land Transfer Act 1952, the Radiocommunications Act 1989 and the Ratings Valuation Act 1998;
- the proportion of their funding that major regulators receive from fees and/or levies varies considerably. The Civil Aviation Authority (95%), the Gas Industry Company Limited (100%), and the Electricity Authority (100%) are at the upper end, while the Office of Film and Literature Classification (36%), Environment Protection Authority (24%), Takeovers Panel (15%-20% in most years), and Reserve Bank of New Zealand (close to 0%) are at the lower end, along with those agencies fully funded from Crown funding.

Fees and levies

Table 3.3 identified that regulators recover costs through fees and levies. The Commission found no formal New Zealand definitions of these terms. The Australian Productivity Commission (APC, 2001b, p. xxxii) defined a fee for service as a direct charge that reflects the costs of the service, and that the service must be rendered to, or at the request of, the party paying the account. It defines a levy as a form of tax that is
imposed on a specific industry or class of persons. In New Zealand, it does not appear so clear-cut that a levy is regarded as a tax (Box 13.1). One distinction between fees and levies suggested to the Commission is that levies are typically set through legislation, while fees may not be. However, there are examples of fees set through subordinate legislation. Fees are typically collected by regulators and retained by them.

Box 13.1  Fees and levies

Neither term is defined in the guidelines for setting charges in the public sector issued by the Treasury. The Office of the Auditor-General’s guidelines suggest that

[a] levy differs from a fee for a specific good or service; it is more akin to a tax, but one that is charged to a specific group. It is usually compulsory to pay a levy. Levies charged to a certain group are usually used for a particular purpose, rather than relating to specific goods or services provided to an individual. (OAG, 2008, p. 6)

The Legislation Advisory Committee (LAC) Guidelines imply that whether a levy – like a fee – is a tax depends on whether it is used to recover costs:

Although an Act may empower the making of fees regulations, this does not mean that the Act empowers the Crown to impose a tax. The cases establish that a fee, due, rate, levy, or toll may in fact be a tax by another name. Re a By-law of the Auckland City Council [1924] NZLR 907 at 911 (SC). In such cases the fee or charge is invalid. However, a fee, due, rate, levy, or toll will not be considered to be a tax if the amount charged is merely for recovering administrative costs reasonably incurred in regulating an activity. (LAC, 2012, s. 3.4.2)

The Concept Consulting Group suggest that a levy is paid by industry participants while a fee is paid by users/beneficiaries, and a levy is paid to the Government, while a fee is paid to the funded entity. However, they note that there are exceptions to this definition (sub. 50, attachment one, p. 11).

Source: OAG, 2008; LAC, 2012; and sub. 50, attachment one.

In the case of levies for Departmental regulators, they may be:

- received directly (and recognised as revenue), but with an appropriation still required to cover any related expenses, with any surpluses returned to the Crown unless permitted to do otherwise, or
- recorded as revenue by the Crown (but not the department), with any funding of the administering department provided separately as Crown funding (and the department’s costs appropriated accordingly).

In the case of Crown entity regulators, the levies may be:

- received directly and recognised as revenue, without an appropriation process; or
- received on behalf of the Crown (that is, not as Crown entity revenue), with any Crown funding of the Crown entity’s costs provided separately as Crown funding (and appropriated accordingly as a non-department expense).  

Given the difficulties in distinguishing between fees and levies, the Commission does not discuss them separately in this chapter. It would welcome advice about whether there is in fact a clear and legally accepted distinction in New Zealand between fees and levies, and whether there are issues relating individually to each of them that the Commission should consider.

Q13.1 Are there clear and legally accepted definitions of fees and levies in New Zealand? If not, does this matter? Are there issues that are specific to either fees or levies that the Commission needs to consider?

The rest of this section outlines the main features of the legal and institutional framework within which funding arrangements are determined.
The legal and institutional framework for funding regulators

Important features of New Zealand’s framework for guiding the choice of funding sources for regulators include:

- specified objectives of cost recovery;
- legal authorisation;
- governance and accountability arrangements;
- guidelines about how to choose between different funding sources; and
- processes for reviewing the effectiveness of funding arrangements.

Specification of objectives

The Government, drawing on advice from departments, decides whether regulators should be funded from taxpayer resources or through some form of cost recovery. The choice between funding sources will be guided by the objectives that the Government considers funding should achieve. The only general explanation of these objectives is in the Treasury Guidelines for setting charges in the public sector, published in 2002. These guidelines indicate that options for user charges should be assessed against a combination of efficiency and equity objectives and ensure that the fees promote other government policy objectives (Box 13.2).

There are inherent tensions between some of the objectives.

- Fees that improve efficiency could be passed on to less well-off consumers, which may be seen as inequitable.

- Fees justified on the grounds of reducing reliance on general taxation could exceed efficient levels.

- Imposing a charge may undermine other policy objectives. For example there have been concerns that the border-charging regime might discourage reporting of biosecurity risks: a person unloading a

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[70] The guidelines deal with charges for services for which the Government is a monopoly supplier. The services may be supplied by departments or other Crown entities and may be intended to provide benefits to individuals and groups and/or limit risks to public health or other negative effects. The guidelines also apply to charges for the supply of information. The guidelines do not deal with taxes to limit externalities, services produced in competitive or contestable markets, services in which income redistribution or social insurance are important, and charges for the use of Crown-used resources such as minerals.
container at a transitional facility who finds a pest may be concerned about higher inspection charges if they notify the Ministry for Primary Industries.

**Legal authorisation**

Most regulators derive their authority to charge fees from legislation. A public entity requires legal authority, through an Act of Parliament, to charge a fee for goods and services that it is legally obliged to provide. Regulations attached to the legislation, or sometimes the legislation itself, may set out the level and types of fees or levies that can be imposed:

The legislation will usually include an empowering provision that authorises the entity or the Governor-General to set the amount through regulation, rather than specify the amount in the primary legislation. (OAG, 2008, p. 9)

For example, the fees that are used to fund the Office of Film and Literature Classification are authorised by the Films, Videos and Publications classification (Fees) Regulations 1994, and regulatory oversight of gambling is funded through fees set out in the Gambling (Fees) Regulations 2007.

The authorisations differ between regulators and can be complex.

- Although section 115 of the Electricity Industry Act 2010 authorises regulations to be made relating to fees, the requirement under section 128 of the Act that the Authority’s costs are fully met from a levy means the fees cannot be used to recover costs in relation to the Authority’s statutory functions. The practical effect of these arrangements is that all Authority funding is ultimately determined by Parliament through the annual appropriation process. The Authority is not able to charge and receive a fee direct from users for any statutory function carried out pursuant to the Act – but the levy can exhibit some of the characteristics of a fee (sub. 50, attachment one, p. 6).

- Unlike the Electricity Authority, the Financial Markets Authority (FMA) can raise some revenue from fees, which are not subject to the yearly appropriation and levy consultation process (since the revenue is received directly by the FMA).

- The Commerce Commission can recover some costs through fees, but not other costs.

- The Gas Industry Company, which is a co-regulatory company, is permitted to raise funds through levies, market fees and annual fees (sub. 50, attachment one, pp. 25-26).

For some regulators, legislation defines criteria for determining the most appropriate method of cost recovery. For example, under the Biosecurity Act 1993 (s 193 (a)), a levy recovering the costs of providing or performing a particular service or function must accord with the principles of equity and efficiency. The Wine Act 2003 requires that justifiability and transparency are considered, as well as equity and efficiency (s 84 (2)).

Regulators need to ensure that fees or levies are linked to provision of a benefit and to avoid charges that exceed costs, which could be interpreted as a tax. A tax that is not authorised by or under an Act of Parliament contravenes section 22(a) of the Constitution Act 1986 and could be declared ultra vires and invalid by a court (New Zealand Treasury, 2002, p. 3).

**Governance and accountability arrangements**

Organisations that determine, implement, monitor or review the approach to funding regulators include:

- the regulators and the ministers responsible for them, who may set fees acting on the advice of the departments responsible for administering appropriations;

- the Treasury and the Office of the Auditor-General (OAG); and

- the Regulations Review Committee (RRC) of Parliament.

The process for reviewing the performance of funding after implementation is another important feature of the governance framework.
Ministers responsible for regulators

Legislation that sets out the functions and powers of individual regulators may indicate that the minister responsible for the regulator recommends fees, or is responsible for the legislation that provides the power to impose fees or levies. This is the case, for example, in the Biosecurity Act, Electricity Industry Act 2010, and the Financial Markets Authority Act 2011. The legislation may, as in the Biosecurity Act, set out options for cost recovery (s. 135) and the authority to impose levies (s. 137). It may also set out how to approach the task.

Departments

Departments administer parliamentary appropriations on behalf of ministers. As part of this role, departments advise ministers on funding and cost recovery and may, as described above, recover levies for Crown entities.

The Treasury

The Treasury Guidelines (New Zealand Treasury, 2002) provide advice about when and how to set fees, although ministers are not obliged to make use of them. These Guidelines are discussed below. Treasury officers provide advice on request about how to implement them. The Commission has found no evidence to suggest that Treasury (or other departments) monitor whether regulators have complied with the Guidelines.

The Treasury has also issued guidance (New Zealand Treasury, 2011c) for the operation of departmental memorandum accounts, which record the accumulated surplus from providing services on a cost recovery basis that can be caused by temporary discrepancies between costs and revenues. The guidance states that memorandum account balances are expected to trend to zero “over a reasonable period of time”, with interim deficits being met either from the department’s balance sheet or by a capital injection sought from the Crown. Agencies are required to have regular monitoring of memorandum account balances (at least quarterly) and these balances are audited. However, there is flexibility on the path that agencies can take to trend to zero balance over time (Box 13.3). The treatment of memorandum accounts is asymmetric, as there are penalties for persistent deficits (these are added to the departmental net assets for the purposes of calculating the capital charge) but not for persistent surpluses (these are exempt from the capital charge, as they are user funds, not departmental capital).

Box 13.3 Memorandum accounts

Entities that provide services on a full cost-recovery basis, and for which the revenue and expenses will not necessarily agree in each financial year, must operate a memorandum account that records the accumulated surplus or deficit arising from providing the service. Memorandum accounts improve transparency and provide assurance that entities are not gaining from over-recovery. Requiring entities to prepare memorandum accounts increases their accountability to those purchasing the services and to wider stakeholders.

Surpluses and deficits in memorandum accounts can be significant. For example, at 30 June 2012, the account for Occupational Licensing of Building Practitioners reported a deficit of $15.3 million, while the account for Civil Aviation Security Charges reported a surplus of $23.1 million.

Treasury instructions state that departments must ensure that there is regular monitoring of all memorandum account balances, at least quarterly. This has been reinforced by the Office of the Auditor-General (2013), which points out that regular monitoring of account balances will allow management to put plans in place to reduce significant deficits and surpluses and that allocating costs accurately is important to ensure that costs are borne by the correct party:

For entities with memorandum account balances, having effective monitoring systems in place is important. Entities should ensure that there is regular monitoring of account balances on either a monthly or quarterly basis. (p. 97)

The Office of the Auditor-General

The Auditor-General has also issued guidelines for charging fees for public sector goods and services (OAG, 2008). The Auditor-General can examine the process used by a public entity in setting fees, as part of its role in providing assurance to Parliament that public entities are operating in a manner consistent with Parliament’s intentions (OAG, 2008, p. 17).

The Regulations Review Committee

The RRC is the parliamentary select committee that scrutinises regulations, including regulations that set fees, to ensure that delegated law-making powers are being used appropriately. It examines regulations, investigates complaints about them, and assesses proposed regulation-making powers in bills for consistency with good legislative practice. Standing Order 378 (2) sets out nine grounds under which the Committee can draw a regulation to the attention of the House (Box 5.5). These grounds focus on issues such as whether the regulation is consistent with the objectives of the relevant Act, whether the matter is suitable for inclusion in regulation, and whether it was introduced after a proper process. The grounds do not cover whether the fees are inefficient. Parliament can disallow a regulation that contravenes one of the nine grounds.

The RRC’s reports on fees include proposed new fees for lodging a claim with the Disputes Tribunal (Box 13.4), civil aviation charges (2012), fees set by the Medical Radiation Technologists Board (2010), and Unit Titles – Fees Regulations (2011). The RRC typically asks the agencies concerned to demonstrate that the fee was calculated in accordance with the Treasury and OAG guidelines, and to address the constitutional principles for setting fees outlined in the RRC’s previous reports. In its comments on the medical radiation technologists’ fees, for example, the RRC criticised the Medical Radiation Technologists Board for not setting its fees in accordance with the Treasury and OAG guidelines.

Applying cost recovery: guidelines published by the Treasury and the Office of the Auditor-General

As indicated above, the Treasury and the OAG have both published guidelines to assist regulators contemplating recovering their costs through charges. Table 13.1 compares some of their key features, which indicate considerable differences between them.

Table 13.1  Key features of Treasury and Office of Auditor-General guidelines

<table>
<thead>
<tr>
<th>Feature</th>
<th>Treasury Guidelines</th>
<th>OAG Guidelines</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal status</td>
<td>Not legally binding</td>
<td>Not legally binding</td>
</tr>
<tr>
<td></td>
<td>Guidelines are “intended as a checklist”</td>
<td>Guidelines set out “matters that we expect public entities to consider”</td>
</tr>
<tr>
<td>Coverage of agencies</td>
<td>All public sector agencies</td>
<td>All public sector agencies</td>
</tr>
<tr>
<td>Coverage of charges</td>
<td>User charges, including fees and levies</td>
<td>Levies are not covered</td>
</tr>
<tr>
<td>Feature</td>
<td>Treasury Guidelines</td>
<td>OAG Guidelines</td>
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<tr>
<td>------------------------------</td>
<td>--------------------------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------</td>
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<tr>
<td>Costs to be recovered</td>
<td>Charges should be at full cost, unless policy considerations justify less than this</td>
<td>Fee should be set at no more than is necessary to recover costs, unless there is specific authority to do so</td>
</tr>
<tr>
<td>Context</td>
<td>Agencies should describe characteristics of good or service (public, club, merit or private good) and identify outcomes to which it contributes, identify the beneficiaries</td>
<td></td>
</tr>
<tr>
<td>Approach</td>
<td>Stepped approach that draws heavily on economic concepts</td>
<td>Focuses on requirement that public entities are guided by the principles of authority, efficiency and accountability</td>
</tr>
<tr>
<td>How fees should be set</td>
<td>Public entities should explain the context; identify who is to be charged; analyse the structure of costs; and identify ways to hold down costs</td>
<td>Public entities should consider:</td>
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<tr>
<td></td>
<td></td>
<td>• legal authority it has to charge a fee</td>
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<tr>
<td></td>
<td></td>
<td>• the justification</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• how fees should be calculated</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• whether its decisions, charging systems and revenue and costs are clearly documented and transparent</td>
</tr>
<tr>
<td>Structure of charges</td>
<td>Consider whether to set charges at short run marginal cost and, if so, how to recover the revenue shortfall</td>
<td>Fees may be set at average cost, unless the costs involved in producing individual goods or services vary significantly</td>
</tr>
<tr>
<td></td>
<td>Consider whether to standardise costs across locations or time, for reasons of administrative simplicity or equity</td>
<td>Goods and services should be grouped logically, and the resources used to produce them identified</td>
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<tr>
<td></td>
<td></td>
<td>Costs need to be divided into direct and indirect costs, and allocated against goods and services</td>
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<tr>
<td>Cost control</td>
<td>Identify ways to hold down costs and, where possible, provide evidence that these mechanisms will be effective</td>
<td>Fees should be reviewed regularly to ensure that they remain appropriate and based on valid assumptions</td>
</tr>
<tr>
<td>Role of consultation</td>
<td>Important. Requirements can be found in Wellington International Airport v Air New Zealand 1993 1NZLR 671</td>
<td>Important. Guidelines provide advice on requirements</td>
</tr>
</tbody>
</table>


**Processes for reviewing how well cost recovery is working**

The RRC reviews cost recovery mechanisms *before* implementation, and when fees are set in regulations a regulatory impact statement (RIS) may need to be prepared. However, there does not appear to be a systematic approach to reviewing how well cost recovery performs *after* implementation, even though the Treasury and OAG guidelines both propose that regulators develop a process for undertaking regular charging reviews (New Zealand Treasury, 2002, p. 21; OAG, 2008, p. 12). The Commission asked 18 agencies with regulatory functions whether they have processes for periodically reviewing fees, levies or other cost-recovery mechanisms. Four responded that there is no process for at least some of their agencies and eight replied that the question was not applicable to them. Six identified review processes, which differ considerably:

- the Civil Aviation Authority (CAA) has triennial funding reviews, with the next one due in 2015;
the Electricity Levy is reviewed each year;

- levies to fund the FMA are to be reviewed after two years;

- levies to fund the Gas Industry Company Limited are set each year;

- the New Zealand Qualifications Authority periodically reviews its fees and charges to ensure that it is achieving the estimated medium-term, full-cost recovery; and

- the Department of Conservation periodically reviews its fees, levies and other cost-recovery mechanisms, by direction from senior managers rather than by statute or regulation.

Summary

The framework for funding regulators outlined in this section has significant positive features. Organisational responsibility for advising, implementing and scrutinising funding arrangements has been established, and guidelines offer regulators and advisors guidance on how to approach funding issues.

The Commission has found little evidence about how well the arrangements are working. There appear to be few studies of whether implementation of the Treasury and OAG guidelines is comprehensive or patchy, or of how funding arrangements have affected the performance of New Zealand regulators. The two sets of guidelines differ considerably. There is no general requirement for ex post evaluation of regulations,71 which might have generated evidence of the impacts of funding arrangements. This inquiry has therefore attempted to address this gap by surveying businesses about the fees that regulators charge, and by seeking information from regulators, and comments through submissions to the inquiry (Section 13.4).

13.3 Insights from economics

This section considers economic concepts that influence the choice between different approaches to funding regulators.

Public or private goods

As the Treasury guidelines set out, the starting point for considering how regulators should be funded, is to assess whether their services are public goods, which should be funded from taxation, or private goods, for which charging is feasible. Providing guidance material on a website is an example of a regulatory service with public good characteristics,72 because there are few if any additional costs involved in providing the material to more people. Charging for public goods is inefficient, because it discourages consumption of additional amounts of a service that, at the margin, costs nothing to supply. So public goods provided by regulators are typically funded from budget appropriations.

Private goods are goods for which it is feasible to charge and to exclude non-purchasers. Issuing licences or inspecting premises are regulatory services more likely to have these characteristics.

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71 There may be requirements in some Acts that particular regulations are reviewed.

72 A public good has the property that excluding people from its benefits is either hard to do or costly, and that its use by one person conflicts with its use by another (New Zealand Treasury, 2002, p. 7).
The benefit of recovering the cost of regulatory services for private goods

Recovering the costs of regulatory services with private good characteristics can in principle improve the efficiency of resource use.

- Building the full costs of production (including the costs of regulation) into products encourages users of regulatory services to adjust their use of those services in line with their willingness to pay for them. This discourages frivolous use of regulatory services and confronts consumers choosing between products with the full costs of their choices. The Independent Pricing and Regulatory Tribunal in New South Wales noted:

  Cost-reflective pricing enables consumers and producers to make informed decisions on the services demanded and supplied. This further reduces the potential for government to provide services that cost more than the value consumers place on them (or more than the benefits they create). (IPART, 2013, p. 21)

- The responses of those who pay for regulatory services to “buy” more or less of these services signals to regulators which of them are in demand. For example, fees for the urgent and after-hours services for issuing passports are about double and four and a half times the standard fee, respectively. And regulators that charge for their services should be able to respond more flexibly and quickly to unexpected changes in demand than would be the case if they had to seek additional Crown funding.

- Appropriately structured charges can motivate regulators to look for better ways to provide services. The quality of consultation between regulators and those they are regulating is important in this context since consultation provides the opportunity for the shape of services to be altered in line with the requirements of both regulators and regulated parties (sub. 50, attachment one, p. 34).

- Those who have to pay for regulatory services may be motivated to monitor regulators’ performance, so as to constrain their costs to efficient levels.

- Cost recovery reduces the call on taxation revenue to fund regulators and so decreases the costs of tax administration and compliance (APC, 2002).

Recovering the costs of regulation may also appear more equitable, in the sense that less of the cost of regulation will be paid by those taxpayers who do not benefit from the regulations or use the regulated products.

Giving regulators access to their own funding sources can protect them from political interference. However, the significance of this argument may be limited in a country such as New Zealand. Smith and Shin, writing almost 20 years ago, argue that

[the significance of this concern will depend on the governance traditions of particular countries. In most OECD [Organisation for Economic Co-operation and Development] countries, this concern is rarely given as a rationale for use of industry levies or user fees. (1995, p. 3)]

But there are practical considerations

Practical factors may constrain the achievement of these in-principle benefits. Cost recovery may in some situations:

- encourage gold plating – charges exceeding efficient costs or over-servicing by the regulator;

- have little impact on the behaviour of users of regulated services, particularly if the fees are small, and the firm or consumer that faces the charge has no alternative but to use the regulated service – in such cases, the efficiency gains from charging for regulatory services may not be large, particularly if being able to impose charges makes it easier for regulators to “pad” their costs;

- conflict with a policy objective, as illustrated by the border-charging example provided earlier;
• distort competition, by discouraging new firms that have to pay registration and assessment charges from entering a market or bringing a new service to a market – Chapter 12 suggested that the accreditation system for new training providers must be designed in a way that avoids this effect;

• encourage regulators to focus on activities for which they can charge (for example, inspections), even when another approach for which they cannot charge (for example, education) may be superior;

• discourage innovation, by penalising first movers (this could happen if a firm has to pay to secure a new standard for an unpatented product) – the standard would be available to competitors, who have not borne the cost of generating it;

• lead to cross-subsidies, which distort resource use;

• disadvantage small firms – for example, all firms may benefit from or contribute to the need for a service, but a flat fee calculated by averaging across the number of businesses will impact disproportionately on small firms, especially if there is a large fixed cost component (New Zealand Food Safety Authority, 2006, p. 11);

• be costly to administer;

• stray into taxation, unless constraints ensure that fees and levies do not exceed efficient costs; and

• weaken the independence of regulators – for example, the World Bank argues that levies based on profits would create a conflict of interest (Brown et al, 2006, p. 223).

Equity and efficiency objectives may clash. Preferential treatment of particular classes of consumers may improve equity, but at the cost of reduced efficiency and higher administration costs. The OECD suggests that “measures through the tax and benefit system may be a more efficient way of ensuring equity than reduced charges” (1998, p. 6).

These possible problems mean that case-by-case assessment is needed that takes into account the characteristics of the service being provided and the costs of administering charges. This highlights the importance of a guidance framework that encourages regulators to work through issues such as those identified above. The complicated impacts of cost-recovery arrangements also suggest a case for reviewing periodically how well cost-recovery arrangements are performing.

While in principle there can be benefits from regulators being at least partially funded through cost recovery, case-by-case assessment is required to secure these benefits in practice.

Who should pay?

When it is efficient to recover the costs of regulatory services through fees, the next question is whether the beneficiary of regulation or the entity that is causing the problem that needs to be regulated (the exacerbator) should pay.

Charging the beneficiary can be justified on the basis that those who benefit from regulation should pay for it:

The ‘beneficiary pays’ principle has been widely cited as a major rationale for developing and implementing cost recovery. It is based on the notion that those that benefit from the provision of a particular activity or product should pay for it. This has both economic and equity dimensions. It encourages those who benefit from the activity or product to recognise that there are resource costs involved, and it decreases the taxation burden on those who do not benefit. (APC, 2001b, p. 15)

The APC explains further that:

The concept of beneficiary pays has its origins in the public finance concept of the benefit principle. This principle suggests that economic efficiency would be improved by requiring people to contribute
(through taxation) according to the value they place on the public goods and services they consume. In practice, it is almost always impossible to estimate these values. (APC, 2001b, p.16)

Finding a way to encourage the beneficiaries of regulation to reveal the values they each place on it may be challenging. A broad-brush approach such as an industry levy is one – albeit crude – way to apply the benefits principle, when an industry is perceived to be the beneficiary.

Consumers are often the beneficiaries of regulation. If there are many beneficiaries – which happens frequently – charging them directly can be costly to administer. In addition, the final incidence of a fee may sometimes not vary significantly whether it is imposed on the beneficiary or on the exacerbator. If those who initially pay a fee can pass some of it on, the beneficiaries of regulation bear part of the costs of regulation even when the charges are imposed on the exacerbator. For example, people who purchase food in retail outlets benefit from food safety regulation, but charging them directly for its costs would not be practical. And retailers normally pass on at least some of the costs of regulation.

So it is often more feasible to recover the costs of regulation from exacerbators than from beneficiaries. This consideration led IPART to propose that, when assessing who to charge for local land services in New South Wales, regulators should adopt a hierarchy, with exacerbators first (where they are identifiable), beneficiaries second and the general taxpayer as the funder of last resort (IPART, 2013, p. 3)

13.4 Issues raised by the survey of businesses and by inquiry participants

Survey of businesses

The Commission’s survey of businesses found that, of the businesses surveyed, just over a quarter (28%) agreed that it was clear what regulatory services the fees covered and just under a quarter (24%) disagreed. Only 9% agreed that the fees charged are fair and reasonable, while 48% disagreed (Colmar Brunton 2013, p. 28). The survey also found that of the businesses that expect regulation to pose a significant barrier to expansion, 60% considered that a reason for this was the cost of obtaining a licence, permit or decision (Colmar Brunton, 2013, p. 22).

These results are broadly consistent with the finding in the Commission’s inquiry into local government, that 70% of the businesses the Commission surveyed were dissatisfied with the regulatory fees that councils charged (NZPC, 2013a, p. 59). Fees for regulation are only part (and often a small part) of the costs that businesses face, but they sit within the context of general concern about the costs that regulation impose.

Submissions

Observations in submissions indicated that how regulators are funded is significant for some inquiry participants. They generally accepted that the efficient costs of regulatory activities need to be funded, and that under-funding can cause problems. For example, the Meat Industry Association considers that recent failings by regulators, such as the recent interruption of meat exports to China “due to a mistake in the over-stretched market access team at Ministry for Primary Industries”, have been caused by under-resourcing of regulatory activities (sub. 40, p. 12). However, several participants have concerns about:

- the way charges are determined;
- weak constraints on the level of charges;
- the impact of charging on regulators’ independence; and
- poorly structured charges.

The way that charges are determined

Several participants consider that processes for determining charges are deficient. For example, the New Zealand Bankers Association believes that the Ministry for Economic Development imposed fees to fund the FMA without considering concerns raised by the industry.
Another example of a lack of accountability and transparency in a regulator’s actions was the process taken by the then Ministry of Economic Development (MED) in deciding the levy structure to be placed on industry to fund the newly formed Financial Markets Authority (FMA) in 2011.

... With little warning MED issued a brief proposal which was heavily criticised by industry participants. Little rationale was provided by MED as to how they arrived at this model and the justification for imposing disproportionate costs on large banks, who were already prudentially regulated and least likely to require FMA attention. Despite extensive feedback from the many different industry participants on how the proposal could be made more equitable, the regulator did not accept or address any challenge to the principles upon which the levy allocation was based.

... The approach taken by the regulator had minimal transparency and accountability and this is unacceptable in the development of a policy that resulted in significant costs being imposed upon the regulated organisations. (sub. 43, p. 6)

The Insurance Council of New Zealand has similar reservations about these charges:

...there is serious concern about the way the insurance industry is currently funded. ... The focus in setting levies seems to have little correlation to how the FMA’s resources will likely be concentrated. (sub. 5, p. 8)

Application of the Treasury and OAG guidelines should reduce concerns such as these. However, Aviation New Zealand commented that “when government is cash strapped our experience is that these guidelines are not applied” (sub. 36, p. 25). Similarly, Business New Zealand suggested that user charges are sometimes applied simply to reduce the impact on the Government’s budget, rather than where cost recovery is justified:

[O]ne area of Government practice where a number of industries have found unbalanced involves the funding methods of various authorities, for instance the Electricity Authority and the Energy Efficiency & Conservation Authority (EECA). This was instituted on the establishment of the Electricity Commission by the then Labour Govt, simply as a means to reduce the additional cost to taxpayers on their establishment as Crown agencies, but has survived with the establishment of the Electricity Authority.

...The move to have the Electricity Authority and a portion of EECA funded by industry has no basis in principle, but was purely a method to avoid taxpayers having to fund their establishment. (sub. 19, p. 13)

As noted earlier, the distinction between public and private goods is a central feature of the Treasury guidelines. Yet it can be hard to make this distinction. Tasman District Council suggested that “improved disciplines around determining the public versus private benefit split in delivering regulation may have some merit” (sub. 1, p. 3).

A common theme between most of these concerns is that there was inadequate consultation before fees were introduced. The CAA, however, disagrees, suggesting that the processes required before fees are introduced may be too onerous:

All regulators whose funding is set by Regulation have funding transparency due to the process for making regulations, which includes the delivery of a Regulatory Impact Statement, and a mandatory consultation phase. ... However, the degree of this transparency is becoming increasingly onerous and expensive, particularly so because of the (apparent) expectation that the organisation will undergo a full business Value-for-Money review as a precursor to any fees charges and levies update. It may create the risk that the funding review process distracts the CAA from its primary role – aviation safety. (sub. 6, p. 37)

Weak constraints on the level of charges
Several participants suggested that weak constraints on the level of charges imposed by regulators can lead to charges exceeding efficient costs (gold plating).

The Meat Industry Association considered that charges imposed on the industry are not transparent and may not in fact be for services that do not contribute directly to regulatory activity:

The costs of regulation are extremely heavy on business. A good example of the costs is from meat hygiene regulatory activity, for which industry is fully cost recovered. Industry pays around $40 million each year to MPI (the regulator and who provides on-site veterinarians) and $47 million to Asurequality
(the provider of meat inspection services). … A problem is that the costs charged to industry are not fully transparent. In particular, it is very unclear to industry what overheads industry is actually paying for – in the view of the MIA, it is inappropriate that industry pays for services that do not directly contribute to the regulatory activity being provided … There has also been poor budgeting and reporting by government regarding cost recovery … These are direct costs to industry. In reality, the indirect costs to industry in having to meet regulatory requirements are probably greater. (sub. 40, pp. 8-9)

Vector noted that if the Commerce Commission over-spends its budget, it can pass on the extra costs through its industry levy:

Most functions of the Commerce Commission under Part 4 are currently funded by an industry levy, which can be passed through to consumers by regulated suppliers. If the Commerce Commission over or under-spends, the amount that varies from budget is passed back to suppliers to pass on to consumers. This means the Commerce Commission is not necessarily constrained by the budgets that are set for it. (sub. 29, p. 23)

Aviation New Zealand similarly considered that there are weak constraints on regulators that are:

… state owned and operated monopolies but there is no redress to the Commerce Commission and the complaint to the Regulations Review Committee must be framed in the context of a breach of standing orders. Without full financial disclosure it is difficult to sustain a challenge and many of the agencies do not have systems which record hours spent on particular activities with any precision – to develop these financial management systems imposes a cost on the users so it’s a vicious cycle. (sub. 36, p. 25)

There are also concerns about possible over servicing when fees can be charged. Aviation New Zealand noted that:

… it is not simply the charges but the lack of control over activities; ie the CAA is the final arbiter of when a “job” is finished. The industry is unable to get to any other provider to seek the service. There are no appeal rights and there are no controls on price, quality or service. … Because of the mixed funding model for CAA we are firmly of the view that it is nearly impossible for CAA to ensure Government contributes its fair share. (sub. 36, pp. 25-26)

While comparing the charges imposed by similar regulators could provide some discipline on their level, making comparisons may be difficult:

We think the Electricity Authority and Gas Industry Co provide good information about their future work programmes and associated costs. However, because this is provided in different forms it can be difficult to draw comparisons between both agencies which have similar functions. (Minter Ellison Rudd Watts, sub. 28, p. 38)

A small number of industry participants were concerned less with the weak constraints on regulators’ charges. For example, Mighty River Power explained:

The Electricity Authority is funded under levy arrangements. Mighty River Power considers the benefit of levy funding is that it is generally transparent (requiring annual consultation with stakeholders) and the Authority has demonstrated a commitment to manage its operating costs. (sub. 30, p. 10)

Impacts on independence

Participants noted that the way that funding is determined can affect a regulator’s independence.

The New Zealand Council of Trade Unions considered that regulators need secure funding because regulators that are under-funded become reliant on the employers they are regulating and so less independent:

Where a regulator is carrying out a controversial or unpopular role (perhaps unpopular only with one interested party) there is pressure to reduce its activity by underfunding. Again, that was demonstrated in the occupational health and safety system. The Pike River Royal Commission inquiry documented the falling resources made available to the regulator with demonstrated but long term impacts on accidents, injuries and deaths. The regulator was unable to do its job properly as a result of the falling funding, which increased the attractiveness of taking short cuts including relying on employer processes or their word rather than carrying out proper inspections and investigations. This meant the regulator was highly reliant on employer goodwill, undermining its independence. (sub. 25, pp. 22-23)
The Reserve Bank suggested that having a 5-year funding agreement with the Government supports its independence:

> Our primary source of funding is return on the investments we hold. The amount of this income is negotiated with the Minister of Finance in a funding agreement that has a five year term. These funding arrangements are consistent with enabling us to retain operational independence from government while not giving rise to any risk that an individual employee would obtain any benefit from taking imprudent risks with the Bank’s funds. (sub. 9, p. 6)

On the other hand, Carter Holt Harvey was not convinced that providing regulators with access to an uncontested stream of income would encourage independence and accountability:

> The Waste Minimisation Act mandates the imposition of a tax on solid waste disposed to landfill. … It is not clear to us that an income guaranteed by regulation (the WMA) and expended on an uncontested basis gives rise to the level of objectivity and independence identified by Treasury as necessary to promote accountability. (sub. 8, p. 10)

**The structure of charges**

Participants raised several issues about the structure of charges imposed by regulators.

- Cross subsidisation can occur – for example, until recently between the costs of renewing a driver’s licence and other licensing services (Ministry of Transport (sub. 39, p. 3).

- Charges not closely linked to changes in costs may reduce regulators’ capacity to fund their expenditure. For example:
  - levies that partially fund the CAA are based on passenger numbers, while the costs of regulation are driven by growth in hours flown. Fluctuations in passenger numbers can affect the CAA’s cashflow and financial position (Aviation New Zealand, sub. 36, p. 22);
  - the Gas Industry Co is partly funded by a wholesale levy based on purchased gas volumes, which can fluctuate with the weather even if the regulator’s costs do not fluctuate (sub. 28, p. 36);
  - the Insurance Council of New Zealand is concerned that levies to fund the FMA are not related to costs, as they have “little correlation to how the FMA’s resources will likely be concentrated“ (sub. 5, p. 8).

- The CAA argues that basing charges on costs can mean that maximum use is not being made of the capacity of charges to dissuade bad behaviour (sub. 36, p. 36). However, fees that exceed costs could be characterised as taxes. Requiring fees to be cost-related does not, in principle, prevent the Government from imposing a tax (in addition to this fee) to discourage such behaviour.

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The Commission’s survey of businesses, and submissions to the inquiry, indicate concern in the business community about:

- the quality of the consultation that takes place before regulatory fees or levies are introduced;
- weak constraints on the level of charges, including limited transparency about how they are determined; and
- the structure of charges.

### 13.5 Lessons from other OECD jurisdictions

Comparisons with other jurisdictions can provide insights into New Zealand’s approach. This section describes the frameworks for funding regulators in Australia and two Australian states, Canada, and the United Kingdom. It also draws on the OECD’s user-charging guidelines (OECD, 1998). The description focuses on the features used in Section 13.2 to describe the approach in New Zealand; that is:
objectives of cost recovery;
legal authorisation for different forms of funding;
governance and accountability arrangements;
application of cost recovery; and
processes for reviewing the impacts of funding arrangements.

The objectives of cost recovery
Like New Zealand, efficiency is the main objective in other jurisdictions (Box 13.5). Raising additional revenue is not an explicit rationale in any of them.

Box 13.5  The objectives of cost recovery
- In the United Kingdom, HM Treasury suggests that cost recovery “can be a rational way to allocate resources because it signals to consumers that public services have real economic costs”.
- Australia’s guidelines note that “cost recovery can provide an important means of improving the efficiency with which Australian Government products and services are produced and consumed”.
- The guidelines in Victoria, Australia indicate that “appropriate cost recovery can improve the way that resources are allocated within the economy, thereby contributing to allocative efficiency”.
- The Treasury Board of Canada considers that user charges’ “main economic rationale is not to produce revenue. Rather it is to promote economic efficiency by providing information to public sector suppliers about how much clients are actually willing to pay for particular services and by ensuring that the public sector supply is valued at least at (marginal) cost by citizens…”.
- The OECD’s user charging guidelines specify that “the objective of user charging is not only to achieve cost recovery from users, but also to make government services more effective and efficient”.

Equity is sometimes mentioned. The Australian guidelines state that
… (cost recovery) may also improve equity by ensuring that those who use Australian Government products and services or who create the need for regulation bear the costs.

Similarly, Victoria’s guidelines note that “the establishment of a standard cost recovery framework improves equity by facilitating consistent treatment across regulated industries”.

Increasing accountability is seen as a rationale for user charges in Canada:

Proper user charges can significantly improve accountability by making clients aware of the costs of the services they receive and managers aware of the benefits and costs of the services they provide.


Legal authority for cost recovery
As in New Zealand, legal authorisation in other jurisdictions invalidates using cost recovery as a form of taxation. The APC (2001b, p. G.6) points out that

[...]any constitutions require that taxes be implemented through specific legislation, and this principle invalidates user charges that have the characteristics of a tax but are not supported by such specific legislation. This is the situation in Australia, Canada, New Zealand, and the UK and among other countries.
Governance and accountability arrangements

Mechanisms to build accountability and transparency include requirements to:

- consult before a fee is imposed;
- justify fees in a RIS or equivalent processes;
- seek ministerial consent before imposing a fee; and
- disclose fees to Parliament.

The requirements that regulators must satisfy before imposing a fee seem more demanding in overseas jurisdictions.

Consultation

Canada’s framework, set out in the User Fees Act 2004, is particularly rigorous, imposing obligations on regulators to justify fees and to deliver “value for money” to those who pay them. The Act sets out:

- consultation requirements before a fee is fixed or changed, including how to manage complaints about proposed fees (Box 13.6);
- the role of parliamentary committees and of Parliament in approving, rejecting or amending proposals;
- scope for a fee to be reduced if established performance standards are not met; and
- a requirement that ministers report annually to Parliament on all user fees in effect.

An important feature of Canada’s approach is the “policy of the government that those who pay fees for government services are entitled to fundamental information on the services being provided and any associated service standards”. To give effect to this policy, fees must be accompanied by measurable and relevant service standards, developed in consultation with paying and non-paying stakeholders and reported to Parliament each year, together with a summary of stakeholder feedback from consultation (Treasury Board of Canada Secretariat, 2004a, p. 1). Regulators can draw on long-established guidance on how to establish service standards (Treasury Board of Canada Secretariat, 1996).

Box 13.6  The approach to consultation in Canada

A 4-phase approval process involving extensive consultation precedes the imposition of fees.

- Phase 1: An iterative process under which the Department proposing a fee presents its rationale and analysis (covering elements referenced in the User Fees Act) to clients, who provide feedback, including in relation to recommendations for service improvement. Documentation should include pricing factor analysis and any methodologies that lead to the proposed fee level.

- Phase 2: The Department publicises the fee proposal in the light of the consultation proceedings from phase 1. An independent panel review may be established to review any client complaints, and its recommendations are considered by the Department.

- Phase 3: The Minister tables the fee proposal in both Houses of Parliament, for approval or amendment. The proposal must be presented in line with a template that, among other aspects, requires:
  - explanation of the cost elements of the fee;
  - comparisons with other countries;
  - a summary of the findings of the impact analysis of the fee;
Impact assessment

The Canadian approach can also be described as a detailed impact assessment specifically for fees. Australia also has a specific process for assessing the impact of fees. Regulators proposing significant cost recovery arrangements must document compliance with the Government’s cost recovery policy in a cost recovery impact statement (CRIS). The CRIS should:

- demonstrate that charges reflect the costs of providing the good or service;
- identify the beneficiaries or the individuals/groups that have created the need for regulation; and
- identify the most appropriate means to impose the charge (as a fee for service or as a levy).

The preparation of a CRIS should involve “appropriate” consultation with stakeholders. The Expenditure Review Committee of Cabinet reviews each CRIS. Summary of a CRIS is included in Portfolio Budget Statements for public scrutiny. Agencies that are required to produce a regulation impact statement (RIS) do not need to produce a CRIS, because the RIS incorporates the requirements of the CRIS (Commonwealth of Australia, 2005, pp. 54-55).

Seeking consent

It is common for regulators in other jurisdictions to be required to seek the consent of a Minister, Parliament or Treasury before imposing a fee.

- In Victoria, any increase in fees above a specified rate set by the Treasurer that is expected to generate revenue of more than $100,000 each year requires the approval of the Treasurer (Department of Treasury and Finance, 2013, p. 34).

- In Australia, portfolio ministers are responsible for ensuring that the cost recovery arrangements of agencies within their portfolios comply with the policy and will report on implementation and compliance in their portfolio budget submissions (Commonwealth of Australia, 2005, p. 3).

- In the United Kingdom, Treasury consent is required for all proposals to extend or vary charging regimes (HM Treasury, 2013, p. 46). Charges that exceed the cost of provision, or are not clearly related to a service, require an explicit ministerial decision and specific statutory authority. Further, the Treasury does not automatically allow departments to budget for net expenditures associated with charges above cost (HM Treasury, 2013, p. 44).

- In Canada, the responsible Minister must table fee proposals in Parliament, for approval, amendment or rejection.
Disclosure to Parliament

In the United Kingdom, the annual report of the charging organisation should indicate:

- the amount charged;
- full costs and unit costs;
- total income received;
- the nature and extent of any subsidies and/or overcharging; and
- the financial objectives and how far they have been met (HM Treasury, 2013, p. 49).

In Canada, the User Fees Act 2004 (s 7) requires every Minister to table in Parliament each year a report that sets out all user fees in effect, including information on matters such as the performance standards and actual performance levels reached and revenue raised.

Application of cost recovery

When cost recovery is appropriate

All of the selected jurisdictions have guidelines for cost recovery. The guidelines differ in the amount of detail provided (with the United Kingdom the least detailed) and their approach, although they are generally underpinned by the public-private good distinction that is at the centre of the New Zealand Treasury guidelines (Box 13.7).

Box 13.7  Determining whether cost recovery is appropriate

The Treasury Board of Canada (2009) sets out a three-step process:

- costing;
- estimating the full cost of the service, which represents the maximum allowable price; and
- considering pricing factors such as:
  - the mix of public and private benefit (taking into account rival consumption and excludability);
  - impact and contextual analysis;
  - stakeholder consultation;
  - additional fee structure features, such as adjustment formulas and differentiated pricing; and
  - fee level review.

The Australian guidelines identify four different types of regulatory activity:

- registration and approvals;
- issuing exclusive rights and privileges;
- monitoring ongoing compliance; and
- investigation and enforcement.

For each type of service, the guidelines suggest a sequence of questions that help to identify whether charging is efficient and, if so, whether a charge or levy is appropriate.

Victoria’s guidelines advise regulators to analyse the economic characteristics of the regulatory service (where it sits on the private/public good spectrum), the beneficiaries of the activity, the parties and circumstances that create the need for the government activity, and whether the activity contributes to
other government objectives. A table summarises the different types of government activity and associated charging considerations. The guidelines note that the charging approach that is ultimately adopted will depend on a range of factors, including the relative weight given to equity and efficiency objectives, practical implementation and legal issues, and consistency with other government policy goals.

Sources: Treasury Board of Canada Secretariat, 2009; Commonwealth of Australia, 2005; and Department of Treasury and Finance Victoria, 2013, pp. 10-14.

Which costs should be recovered

The Australian Guidelines provide that the charge for each regulatory activity or product should incorporate the full cost of regulation, subject to the caveats of efficiency, cost effectiveness and consistency with policy objectives.

The Victorian Guidelines stress that the costs of all outputs that are integral to the good, service, or activity subject to cost recovery are included in the full cost calculation. Costs that are not a fundamental part of, or directly related to, the output - such as the broad development of policy or regulation - should be excluded.

The UK Guidelines provide a list of the cost elements (capital and operating) that need to be included and excluded when calculating the cost of providing a service. Among the excluded items are externalities imposed on society and the costs of policy work (HM Treasury, 2013, Annex A6.1).

How capital costs should be calculated and allocated

The guidelines of other jurisdictions generally provide more advice about how to measure the cost of capital and how to allocate joint costs (Table 13.2).

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Measuring the cost of capital</th>
<th>Allocating joint costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Kingdom</td>
<td>Full cost recovery normally means recovering the standard cost of capital, currently 3.5% in real terms. A higher return is required for services that compete with private sector suppliers of similar services.</td>
<td>The guidelines describe various approaches to allocating these costs to products</td>
</tr>
<tr>
<td>Australia</td>
<td>Agencies should justify their approach to determining capital costs and depreciation</td>
<td></td>
</tr>
<tr>
<td>Victoria</td>
<td>A real rate of return (currently 8% real) should be applied as a proxy for the cost of capital, and applied to capital that is integral to the delivery of the service</td>
<td>Activity-based costing and the “pro rata” approach can be used to allocate indirect costs between outputs. An appendix explains how to do this.</td>
</tr>
<tr>
<td>Western Australia</td>
<td>The WA guidelines provide extensive advice on how to calculate and allocate costs, with more than one third of guidelines devoted to defining and estimating direct and indirect costs</td>
<td></td>
</tr>
</tbody>
</table>


How efficient costs should be demonstrated

Guidelines in other jurisdictions focus more on this issue than is the case in New Zealand.

The Victorian Guidelines point out that poorly designed cost-recovery arrangements can create incentives for inefficiency and cost padding. Techniques to keep costs at efficient levels include:
One purpose of the Australian Government’s CRIS process is to ensure that costs are at efficient levels at the time the new regulation is introduced.

In Western Australia, each year agencies are required to review the fees and charges that they levy. Under some circumstances, a detailed submission to the Treasury is required before a proposed increase is submitted to the Expenditure Review Committee (Department of Treasury and Finance WA, 2007, p. 4).

In Canada, the Treasury Board (2009) recommends that reviews of the components of the pricing decision are undertaken every 3–5 years.

F13.4 The funding frameworks in other selected countries are similar to New Zealand in that they:

- set out efficiency and, to a lesser extent, equity as the main objectives of cost recovery;
- require consent, usually of a minister or Parliament, before a fee or levy is introduced;
- are based on a distinction between cost recovery and taxation; and
- provide guidance material.

There are, however, examples in other jurisdictions of:

- more rigorous consultation and impact assessment requirements before fees are introduced;
- stricter requirements for performance standards and reporting against those standards when new fees are introduced;
- penalties for failing to achieve the standards; and
- more detailed advice about how to implement cost recovery.

13.6 Implications for funding regulators in New Zealand

The concerns that participants have raised about the current framework, combined with insights from economic analysis and international practice, suggest that options for improving the approach to cost recovery in New Zealand include:

- strengthening the governance and accountability framework, by:
  - publishing a clear statement of the Government’s cost recovery policy, including its objectives;
  - increasing the status of (refreshed) guidelines;
  - requiring more consultation before a levy or fee is introduced or amended;
  - strengthening performance reporting;
  - increasing the involvement of the RRC and Auditor-General in ensuring that the guidelines are applied; and
- introducing regular reviews of regulators’ cost recovery practices;
- improving the implementation of cost recovery by:
  - refreshing the guidance material; and
  - providing more support to regulators.

**Strengthening the governance and accountability framework**

**Publishing a statement of the Government’s cost recovery policy**

A short statement of the Government’s expectations would enhance the incentives and capability of those involved, to implement cost recovery in line with the Government’s expectations.

An example is provided by Australia’s cost recovery guidelines, which are introduced by a statement of 14 key principles that support the Australian Government’s formal cost recovery policy to improve the consistency, transparency and accountability of Commonwealth cost recovery arrangements and promote the efficient allocation of resources. The principles cover issues such as which costs should be recovered, when cost recovery should not be applied, legal authority, that costs should be recovered on an agency rather than activity basis, consultation requirements, obligations to review arrangements after implementation, and the responsibility of portfolio ministers to ensure that agencies within their portfolios comply with the policy (Commonwealth of Australia, 2005, pp. 2-3).

If it decided to prepare a policy statement, the Government could consider whether to re-focus cost recovery towards a single and well-specified efficiency objective. Kerr (2004) argued that

… there is too much focus on getting additional sources of revenue for the government and its agencies and not enough focus on economic efficiency – the best use of resources in the economy. Part of the problem stems from the badly formulated Treasury Guidelines for cost recovery, which do not have a clear efficiency objective. (p. 8)

While Kerr’s concern is about the potentially excessive use of cost recovery to raise revenue at the expense of efficiency, the reference to both equity and efficiency objectives in the Treasury Guidelines requires trade-offs. These may reduce regulators’ accountability and may lead to funding being targeted at equity objectives that may be more effectively achieved using other policy instruments. On the other hand, equity objectives exist in other jurisdictions, perhaps because cost recovery is more politically acceptable when impacts on equity have to be considered. If the Government decides to retain both efficiency and equity objectives, it could consider providing guidance about how to make trade-offs when these objectives conflict.

The Commission recommends a government policy statement on cost recovery.

<table>
<thead>
<tr>
<th>R13.1</th>
<th>The Government should publish its cost recovery policy, covering issues such as:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>• policy objectives;</td>
</tr>
<tr>
<td></td>
<td>• guidance about how to make trade-offs should objectives conflict;</td>
</tr>
<tr>
<td></td>
<td>• when cost recovery may be appropriate;</td>
</tr>
<tr>
<td></td>
<td>• consultation requirements before implementation;</td>
</tr>
<tr>
<td></td>
<td>• how and when arrangements are to be reviewed and by whom; and</td>
</tr>
<tr>
<td></td>
<td>• responsibility for ensuring compliance with the policy.</td>
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</tbody>
</table>

**Enhancing the status of (revised) advisory guidelines**

The status of the Treasury guidelines is ambiguous. Some text implies that they are advisory only: they “do not set out to be definitive” (p. 2) and “use of the guidelines is not obligatory” (p. 5). On the other hand,
there is also firmer language: ministers are “likely to seek assurances that the guidelines have been applied” (p. 5), and the guidelines “are primarily intended to ensure services are charged at full cost to the appropriate parties” (emphasis added) (p. 2). In addition, as noted earlier, when the RRC examines whether a fee should be disallowed, it investigates whether the guidelines have been consulted. Ambiguity should be removed from the cost recovery guidelines.

There is a case for increasing the incentives to apply the Treasury guidelines, particularly if they are reviewed to ensure that they will enable agencies that use them to implement a government cost recovery policy. Table 13.3 sets out four options and their main advantages and disadvantages. In Australia, as noted above, it is the responsibility of portfolio ministers to ensure that agencies in their portfolios comply with the policy. The Commission considers that this responsibility ultimately lies with the portfolio minister, but that to give effect to that responsibility either the Treasury or the chief executive of the agency proposing the fee should be required to certify that the guidelines have been applied adequately through appropriate mechanisms. Imposing this obligation on the chief executive has the advantage that it focuses responsibility on the agency that introduces the fees.

### Table 13.3 Options for increasing the use of the Treasury Guidelines

<table>
<thead>
<tr>
<th>Option</th>
<th>Advantage</th>
<th>Disadvantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incorporate the guidelines in legislation</td>
<td>Would make application of the guidelines legally binding</td>
<td>Discourages updating of guidelines as knowledge develops, given that legislation would need to be amended</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Would need to be supported by advisory material</td>
</tr>
<tr>
<td>Impose a legal obligation on portfolio ministers to ensure that the agencies have applied the government cost recovery policy within their portfolio</td>
<td>Strengthens incentives for agencies to apply the guidelines</td>
<td>Minister needs to delegate responsibility for ensuring that agencies do comply</td>
</tr>
<tr>
<td></td>
<td>Guidelines could be amended as knowledge develops</td>
<td></td>
</tr>
<tr>
<td>Require Treasury to certify that guidelines have been applied adequately</td>
<td>Provides for independent evaluation of the quality of fee proposals</td>
<td>Additional cost incurred by Treasury</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Shifts responsibility away from the agency imposing the fee</td>
</tr>
<tr>
<td>Require the chief executive of agency proposing the new/amended fee to certify that the guidelines have been applied adequately</td>
<td>Strengthens incentives for agencies to apply the guidelines</td>
<td>Additional cost for agencies that would not otherwise have applied the guidelines</td>
</tr>
</tbody>
</table>

**R13.2** Portfolio ministers should be responsible for ensuring that agencies within their portfolio have complied with the Government’s cost recovery policy. Chief executives of agencies proposing a new or amended fee or levy for regulatory services should be required to certify through an appropriate mechanism that their agency has made adequate use of the Treasury guidelines.

**More effective consultation before fees or levies are introduced or amended**

The amount of consultation before fees are amended or introduced seems patchy. Some agencies already run thorough consultation processes before introducing or amending fees. Fees that are given effect in regulations will normally require a RIS, which will involve some consultation. On the other hand, as noted earlier, some submissions pointed to inadequate consultation.
Additional consultation, and a “shared” direction, could lead to better-designed fees with more support from those who pay them. For example, while the Meat Industry Association is currently concerned that regulatory transparency is often poor, earlier experience in this industry highlights the benefits of consultation (Box 13.8).

**Box 13.8 Consultation about cost recovery in the meat industry**

Cost recovery for the meat inspection service was introduced in the mid-1980s. This covers the direct and indirect costs of about 1,600 meat inspectors, veterinarians and others involved in regulatory work focused on market access. The costs were high and there was pressure from industry to be more transparent and to cut costs. During the early 1990s, the costs of inspection and regulatory work focused on market access were itemised and recovered separately, and from 1998 onwards separate organisations carried out these functions. AsureQuality, an SOE, carried out the inspection function, and MAF managed the regulatory work focused on market access.

To facilitate cost recovery and better underpin the meat sector, MAF management moved the way it worked from each year holding a token meeting with the industry about cost recovery with ultimate imposition, to one of seeking industry input and ultimately agreement with, the strategy for regulatory market access. This translated to yearly work plans (with their associated costs), with industry being closely involved in determining their format. Meetings between MAF and the meat industry were held every 3 to 4 months to report back on progress against the plan and spending.

Three examples indicate how this approach created a level of comfort in the industry about cost recovery.

- When the MAF’s planning process revealed a shortage of (market access) staff experienced in the international environment, the industry agreed to pay about $200,000 to fund a post in Washington.

- The industry agreed to boost funding to improve recruitment and retention of veterinarians when the strategy indicated risk exposure from insufficient veterinarians.

- One year when cost recovery generated a surplus, rather than reduce costs, industry stipulated that MAF use the surpluses to fund operational research aimed at reducing market access risks/costs.

*Source:* Personal communication, 18 February 2013.

Consultation could be improved by requiring preparation of a CRIS, as in Australia, or the phased consultation process that is required in Canada. Either approach would, however, add cost and time, which might discourage small regulators in particular from pursuing cost recovery. While any obligations to consult would therefore need to be designed carefully, the Commission is inclined to the view that some form of requirement to consult should be mandated. Concerns that the extra cost may discourage worthwhile cost recovery might be reduced by only imposing obligations to consult above a threshold level of revenue. Another option is to impose on regulators a duty to undertake “reasonable” consultation before implementing new or amended fees and to take account of the views of those affected by these fees, before they are introduced.

**Q13.2 Would there be net benefits from imposing a general obligation on regulatory agencies to consult before fees or levies are introduced or amended?**

**Amending the approach to memorandum accounts**

As noted earlier, memorandum accounts are intended to be in balance over a “reasonable” period, but there is asymmetric treatment of surpluses and deficits during the period that accounts are not balanced. Options for reducing this asymmetry could be for some form of charge to be imposed on surpluses, or for
surpluses that persisted beyond, say, two years, to trigger a review of fees. It would be good practice to have the review policy set out up front, perhaps reflecting criteria such as size of deficit/surplus, the number of years since the last review, variability in demand, the extent to which the fees are avoidable, and the nature of the costs being recovered.

Both approaches might, however, weaken regulators’ incentives to constrain their costs and the second option might trigger unnecessary reviews in cases where, for example, the factors causing the surplus were temporary. The Commission welcomes comments about whether surpluses and deficits on memorandum accounts signify a problem and, if so, whether there are worthwhile options to address it.

Q13.3 Do surpluses and deficits on memorandum accounts signify a problem? If so, are there worthwhile options to address the problem?

Linking fees to performance reporting

Some inquiry participants are concerned about inadequate constraints on the level of regulators’ fees. Canada addresses this problem by requiring regulators to report to Parliament whether their services are achieving service standards, with the possibility that fees can be temporarily reduced when they do not achieve such standards.

The Commission is not convinced that this approach is necessary in New Zealand. First, performance reporting does not yet set out standards that could be used for this purpose. Second, penalising regulators for poor performance by reducing their revenue could reduce their capacity to deliver government policy objectives.

That said, as performance reporting by regulators improves, it would become more feasible to link the imposition of fees to reporting on the delivery of regulatory services. A requirement that regulators develop such frameworks and publicly report their performance against specified indicators, along with the cost of delivering these services, would strengthen the incentives for efficient delivery of services by regulators.

F13.5 It is desirable that regulators, as they develop improved performance reporting frameworks, use these frameworks to measure the cost of delivering regulatory services and report this information publicly.

The role of the Regulations Review Committee and the Auditor-General

While the RRC has regard for the OAG and Treasury guidelines when reviewing fees regulations, the grounds on which it can recommend that a fee be disallowed (Box 5.5) do not include whether the fees comply with an economic framework, such as the one outlined in the Treasury Guidelines. One option is to add a new ground for potential disallowance that the RRC would consider, to include that the regulator has had adequate regard for the economic framework set out in the (revised) cost recovery guidelines. While the RRC already appears to consider whether those proposing fees consider the guidelines, making this a formal requirement is likely to complement Recommendation 13.2 by further strengthening regulators’ incentives to apply the guidelines.

The proposal to add this new ground could increase the RRC’s workload. However, other recommendations proposed in this chapter illustrate how to reduce the number of cases in which the RRC needs to be involved. Examples include seeing that:

- better guidance material is provided;
- departmental staff are available to advise about difficult issues;
- additionally, regulators should move towards linking fees to service provision and reporting on service standards.
The grounds on which the Regulations Review Committee can disallow a regulation should include that the regulator in developing and implementing a fee or levy has had inadequate regard for the economic framework set out in the Government’s guidelines for setting charges in the public sector.

Enhancing the RRC role to review could be supplemented by audits of how regulators implement cost recovery. The incentives on regulators to improve their cost-recovery arrangements could be strengthened if the Auditor-General set out a programme of audits of these arrangements. These could start immediately and would, at first, review compliance with the present Treasury guidelines and OAG guidelines. Later, it would review compliance with the revised guidelines, should the Government accept the Commission’s recommendation (below) to improve the two current guidelines.

The Auditor-General should introduce an enhanced programme of audits of regulators’ compliance with Government cost-recovery guidelines.

Regular reviews of regulators’ cost recovery practices
Reviews of regulators’ cost-recovery arrangements – either of individual regulators or as part of a broader portfolio review – are common in other jurisdictions.

New Zealand’s Performance Improvement Framework provides for reviews of the current state of agencies and how well they are placed to deal with emerging issues. Requiring that these reviews consider the approaches to cost recovery of regulators within each portfolio would highlight good practices, identify cases of over-charging and, conversely, may suggest areas where cost recovery could be introduced.

Alternatively, agencies could also be required to report on their approach to cost recovery in their Regulatory Systems Report, which is required as part of their obligations under the regulatory stewardship programme. Cabinet has agreed to a set of Initial Expectations for Regulatory Stewardship for departments in exercising their stewardship role over government regulation and has tasked Treasury with progressively developing more specific regulatory expectations and guidance that covers key aspects of regulatory management. The Regulatory Systems Report will complement the development of the Performance Improvement Framework (Offices of the Ministers of Finance & Regulatory Reform, 2013b, paragraphs 16 and 17).

Portfolio reviews undertaken within the Performance Improvement Framework, and/or the Regulatory Systems Reports prepared under the expectations for regulatory stewardship, should review and report on the adequacy of the approaches to cost recovery of regulators within each portfolio.

Improving the implementation of cost recovery
Refreshing the guidance material
The recommendations outlined above would lead to increased use of the Treasury Guidelines to enable and encourage efficient funding arrangements for regulators. Yet, as described earlier, Treasury and the OAG have both published guidance material for regulators contemplating cost recovery, and there are overlaps both between the two sets of guidance and the seemingly different approaches to similar issues (Table 13.1). These weaknesses could undermine the benefits from giving the guidance material a more important role in the policy framework.

Despite these apparent problems, only three departments or regulators that the Commission contacted through its information request considered that the existing guidelines needed to be improved. Even so, it appears to the Commission that regulators considering whether to introduce or amend a charge are not helped by having to consult two sets of guidelines which, while intended to complement each other, often
cover the same issues in slightly different ways. To avoid confusion, these matters should be explained once only, either in one unified set of guidelines or in two separate guidelines that have clearly different yet complementary, non-overlapping, roles. In addition, the Treasury Guidelines were published 12 years ago, so are unlikely to reflect the lessons that have accumulated in New Zealand and overseas over that period about when and how to implement cost recovery and about how to address the potential problems with cost recovery as outlined in Section 13.3.

It is possible that the different responsibilities of the Treasury and the OAG justify having two sets of guidelines. If so, each set should indicate clearly:

- their respective roles;
- which entities and types of funding arrangements each covers;
- how the two sets of guidelines complement each other; and
- in the event that a regulator considers that the two sets of guidelines provide conflicting advice, how that regulator can seek resolution of the conflict.

The Government and Auditor-General should review the Treasury’s Guidelines for Setting Charges in the Public Sector and the Auditor-General’s Charging Fees for public sector goods and services, to ensure that the guidelines reflect current knowledge about when and how to implement cost recovery.

Users of the guidelines (whether the two sets of guidelines continue or are combined) should:

- only have to go to one place for advice on any issue;
- not receive conflicting advice from the guidelines; and
- be clearly informed about the scope of the entities and charges that the guidelines cover.

This review would also present opportunities to use the guidelines to provide more practical advice. For example, the Treasury guidelines provide little advice about how to distinguish public and private goods.

Australia’s Department of Finance is currently redrafting the Australian Government’s Cost Recovery Guidelines. One aim of this review is to make the guidelines more useful to regulators as they implement the Government’s cost recovery policy. This review has been informed by extensive consultations with government and non-government stakeholders. The current intention is that the new guidelines will be implemented from July 2014. Given this effort, and that both cost recovery frameworks have similar rationales, there would be benefits from any review of the New Zealand guidelines being informed by the experience in Australia.

Any review of New Zealand’s guidelines should also be informed by considering the advantages and disadvantages of adopting common features of these frameworks across the two countries. One advantage of a common approach is that it could assist the introduction of single trans-Tasman regulators.

The Government, when it reviews New Zealand’s cost recovery guidelines, should seek to collaborate with the review of the cost recovery guidelines currently being undertaken in Australia.

Providing more support to regulators that implement cost recovery

While guidance material can help, even if improved it will not address all the case-by-case issues that will arise. Further, most regulators rarely establish or review fees and levies. Smaller regulators in particular are
unlikely to have the expertise to do this in-house, although they may be able to contract that expertise. Options for improving the capability of regulators include:

- using established or new forums of regulators to exchange lessons learnt in introducing and administering fees and levies; and
- ensuring that departments have adequate capability to help regulators;

As will be discussed in Chapter 11, there is sector support for more use of forums of regulators, which could add cost recovery to their agenda. Particularly if new guidelines are developed, however, it is likely that advice from Treasury and/or portfolio departments would be needed in addition to these forums. The Commission has not heard about significant gaps in current arrangements, but it would be timely to confirm that the support for regulators remains adequate.

**R13.8** That the Government consider whether those agencies that set or amend fees or levies can access adequate advice and experience from other agencies and departments.
Chapter 14 | Accountability and performance monitoring

14 Accountability and performance monitoring

Key points

• Existing accountability processes provide multiple avenues to interrogate and challenge regulators about their behaviour, and a range of levers that ministers can pull to influence this behaviour.

• To influence a regulator in a timely and appropriate fashion, ministers must have a sound understanding of how well the organisation is performing.

• Monitors of regulators have a key role to play in ensuring ministers are well informed about performance and risk levels. When done well, monitoring can also help test the quality and effectiveness of regulatory regimes.

• Where regulators are Crown entities, the relevant portfolio department acts as monitor. Where the regulator is a department, central agencies (the Treasury and the State Services Commission (SSC)) have monitoring functions. Effective monitors need good overall sector knowledge, so that they can understand the regulator’s operating environment and be independently aware of emerging issues and risks.

• Monitoring is both a key link, and the weakest link, in the current accountability system. Some departments appear not to fully understand their monitoring roles and responsibilities, monitoring is not having enough effect on regulatory quality, and expectations on departments to monitor well are not strong enough. Regulator chief executives do not see the Treasury and SSC as playing a significant role in holding agencies to account for their regulatory functions.

• Performance expectations for monitoring are either too low or unclear, and monitoring performance could be strengthened. The Commission recommends that:
  - more detailed guidance be prepared for departments and ministers on Crown entity monitoring, outlining issues they should look for in reviewing regulator performance;
  - the Treasury and SSC work with departments to develop performance measures that better, and more consistently, reflect good practice in monitoring;
  - departments develop and maintain explicit statements of their monitoring roles and responsibilities (in doing so, they should regularly review whether their monitoring approaches give ministers sufficient assurance of risk management, permit accurate performance assessments, and promote substantive dialogue with regulators about whether their regimes are “fit-for-purpose”);
  - SSC and the Treasury play a more active oversight role for departmental regulators and more tightly integrate their tools for assessing regulatory stewardship performance into current accountability processes, especially chief executive performance reviews.

• The changes recommended are not designed to create new accountability mechanisms. They are intended to ensure that the existing mechanisms are used to their full effect.

14.1 Introduction

Accountability mechanisms are a key catalyst of effective regulation. Processes for holding regulators to account for their behaviour help ensure that the agencies act efficiently, effectively and lawfully, and can
encourage regulators to improve their performance. This section explores regulator accountability processes in New Zealand, highlights some areas of weakness, and makes recommendations to offset these weaknesses.

- Section 14.2 defines accountability in the context of regulation, and outlines why accountability is important for regulatory quality.
- Section 14.3 describes the accountability systems that apply to regulators in New Zealand.
- Section 14.4 assesses the effectiveness of processes for monitoring regulator performance.
- Section 14.6 outlines areas where the monitoring of regulators might be improved.

### 14.2 What is accountability in the context of regulation, and why does it matter?

The concept of accountability has been defined in many ways. Most definitions describe accountability as a “relational concept” (Mashaw, 2006), where one party “is required to explain or justify its actions” to another (Bird, 2011). In the context of regulators, agencies are generally expected to explain or justify their actions to external parties against three main criteria: “financial accountability, procedural accountability and substantive accountability” (Ogus, 1994). Bird (2011) elaborates on each of these criteria:

In relation to the first type of accountability, regulators should satisfy high standards of financial management because they are spending public money. In relation to the second, regulators’ procedures should be fair and impartial and comply with administrative law principles because they are exercising public power. Finally, regulators should be accountable for their substantive decisions. They should be accountable for the policies and regulations they make and their administration of the regulatory regime, which includes, for example, the way they conduct licensing processes, the approvals they give, and the way they maintain public records and registers. They should be responsible for their compliance and enforcement decisions. Perhaps most importantly, regulators should be responsible for the overall management of their regulatory regime, that is, the priorities they set and how they allocate their resources. All these substantive decisions should achieve the public interest goals of the regulatory regime that the regulator administers. (p. 742)

Black (2012) identifies a similar, but slightly wider, set of criteria:

That criteria may relate to one or more sets of issues, such as whether they have acted in accordance with their legal mandate; whether they have used their financial resources appropriately; whether they have operated in accordance with fair procedures; whether they have engaged in adequate consultation and participation in decision making; and/or whether the goals that they are seeking to achieve are normatively acceptable. (pp. 4-5)

Accountability mechanisms can be classified in terms of their strength. According to Bird (2011), weak mechanisms “merely require regulators to explain and justify their actions” (p. 741). Strong mechanisms “involve some sort of response (if the regulator does not meet the required performance standard)” (Ibid).

The obligation on regulators (or the ministers responsible for them) to account for their actions matters for a number of reasons.

- **Lawfulness and reasonableness:** Effective accountability mechanisms assure Parliament and regulated parties that the regulators are acting within their statutory mandates, and give confidence that regulated parties are being treated fairly and appropriately. The Commission discussed the extent to which judicial review and appeals can ensure lawfulness and reasonableness in Chapter 10.

- **Effective risk management:** Accountability processes should demonstrate to ministers, lawmakers and the public that regulators are targeting the most important public harms and controlling them effectively.

- **Incentives to perform and improve:** The obligation to report on future intentions, and then report later on what was attained, encourages regulators to identify the interventions and processes that most effectively and efficiently achieve their objectives. Where accountability systems work well, they also allow regulators, ministers and lawmakers to identify areas for improvement.
14.3 Accountability mechanisms in New Zealand

As noted above, accountability involves a duty to answer for one’s actions. However, this definition raises a number of questions:

…who is liable or accountable to whom; what they are liable to be called to account for; through what processes accountability is to be assured; by what standards the putatively accountable behaviour is to be judged; and, what the potential effects are of finding that those standards have been breached. (Mashaw, 2006, p. 118)

In New Zealand, four main groups can call regulators to account: the Executive, Parliament, regulated parties and the wider public (Figure 14.1). This section lays out the mechanisms through which these four groups hold regulators to account and which accountability criteria (such as financial, procedural or substantive) each mechanism meets. Each mechanism is also assessed in terms of its strength following the approach used by Bird (2011).

- **Weak**: A weak mechanism simply requires the provision of information, generally in a pre-determined format.

- **Moderate**: A moderate mechanism is where a regulator (or their responsible minister) may be expected to carry out a specific action, but has some latitude about whether and how to carry out that expectation.

- **Strong**: A strong mechanism is where a regulator (or their responsible minister) can be compelled to change direction, undo a decision or action, or carry out other actions.

Although this section explores each accountability mechanism individually, it is worth recalling that a number of these mechanisms inter-relate (for example, Statements of Intent, Annual Reports and financial reviews are part of the annual performance cycle). As a result, the weakness of one individual mechanism may be offset by strength in another mechanism.
## Accountability to the Executive

### Table 14.1 Mechanisms for accountability to the Executive

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Accountability criteria</th>
<th>Frequency</th>
<th>Strength</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Regular mechanisms</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Statements of Intent</td>
<td>Mainly financial and substantive</td>
<td>Yearly</td>
<td>Can be strong, although Ministerial powers over independent Crown entities are constrained.</td>
</tr>
<tr>
<td>Output agreements/plans;</td>
<td>Substantive</td>
<td>Yearly</td>
<td>Can be strong, although ministerial powers over independent Crown entities are constrained.</td>
</tr>
<tr>
<td>letters of expectation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Performance reporting to</td>
<td>Mainly financial and substantive</td>
<td>Generally quarterly</td>
<td>Weak, but may lead to ministerial action</td>
</tr>
<tr>
<td>Ministers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chief executive performance assessment</td>
<td>Mainly substantive</td>
<td>Yearly</td>
<td>Moderate</td>
</tr>
<tr>
<td>Annual Reports</td>
<td>Mainly financial and substantive</td>
<td>Yearly</td>
<td>Weak</td>
</tr>
<tr>
<td>Treasury oversight of regulatory management system</td>
<td>Financial; procedural; substantive</td>
<td>Ongoing</td>
<td>Weak, but can lead to strong ministerial action</td>
</tr>
<tr>
<td><strong>Irregular mechanisms</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ministerial Directions</td>
<td>Depends on circumstances</td>
<td>As required</td>
<td>Strong</td>
</tr>
<tr>
<td>Board or Chief Executive appointments/removals</td>
<td>Depends on circumstances</td>
<td>As required</td>
<td>Indirect, but can be strong. Board members of independent Crown entities can only be removed in specific circumstances.</td>
</tr>
<tr>
<td>Policy review/baseline review/Royal Commission</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Moderate, but can lead to strong ministerial action</td>
</tr>
<tr>
<td>Performance Improvement Framework reviews</td>
<td>Financial; procedural; substantive</td>
<td>Varies</td>
<td>Strong</td>
</tr>
</tbody>
</table>

Under New Zealand constitutional conventions, ministers have direct and indirect responsibility for the performance of regulators, depending on their form and degree of statutory independence (such as a department, Crown agent, autonomous Crown entity or independent Crown entity). Ministers “are individually responsible to the House for their official actions and for the general conduct of their departments and officials. This is a political accountability. It is not limited to matters over which the Minister has legal control” (McGee, 2005, p. 92). Where regulators are Crown entities, ministers “are responsible to Parliament for overseeing and managing the Crown’s interest in, and relationships with, the Crown entities in their portfolios” (Cabinet Office, 2006). The different nature of the accountability for Crown entities reflects the fact that they are legal bodies in their own right, outside of the Crown, and governed by boards, whose members are responsible for the performance of their organisation.

### Regular mechanisms

Virtually all regulators are subject to the state sector financial and performance management processes laid out in the Public Finance Act 1989, State Sector Act 1988 and Crown Entities Act 2004. Regulators that are
Chapter 14 | Accountability and performance monitoring

not subject to those processes (mainly occupational regulators that are not part of the State sector) have similar obligations to report their performance to ministers and Parliament.73

Financial and performance management processes in the state sector operate on a yearly cycle, starting with specifying departmental or Crown future operating intentions through the Strategic Intention or Statement of Intent (SOI) and the Supporting Information in the Budget Estimates.

SOIs and Strategic Intentions are strategic documents that set out the agency’s direction and objectives, over at least the next four financial years. Crown entities must also outline how they propose to assess their performance. Minimum content requirements for each are outlined in Table 14.2.

Table 14.2 Minimum content requirements for Strategic Intentions and Statements of Intent

<table>
<thead>
<tr>
<th>Departmental Strategic Intentions</th>
<th>Crown Entity Statement of Intent</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Period of the document.</td>
<td>• Period of the document.</td>
</tr>
<tr>
<td>• Whether the department hosts a departmental agency.</td>
<td>• The Crown entity’s strategic objectives.</td>
</tr>
<tr>
<td>• The department’s strategic objectives.</td>
<td>• The nature and scope of the entity’s functions and operations.</td>
</tr>
<tr>
<td>• The nature and scope of the department’s functions and operations.</td>
<td>• How the entity will manage its functions and operations to achieve its strategic objectives.</td>
</tr>
<tr>
<td>• How the department will manage its functions and operations to achieve its strategic objectives.</td>
<td>• How the entity will manage its organisational health and capability, including equal employment opportunities, capital investment and asset management.</td>
</tr>
<tr>
<td>• Pay and employment equity strategies.</td>
<td>• How the entity proposes to assess its “strategic performance”.</td>
</tr>
<tr>
<td>• Any other information “reasonably necessary” to understand the department’s strategic intentions.</td>
<td>• Any process to be followed in the proposed acquisition of shares or interests in companies, trusts or partnerships.</td>
</tr>
<tr>
<td>• Any other requirements of the responsible minister or Minister of Finance.</td>
<td>• Any other information “reasonably necessary” to understand the entity’s strategic intentions.</td>
</tr>
</tbody>
</table>


Departmental Strategic Intentions must be agreed with the relevant minister. Ministers responsible for Crown entities may direct that information in an SOI be presented in a specific format, make comments on a draft SOI, and direct amendments to an SOI. The minister may also ask for a new SOI at any time. Even so, Ministerial Directions may not affect statutorily independent functions of a Crown entity.

Ministers may also seek an output plan (with their department) or output agreement (with a Crown entity). Output plans or agreements are yearly agreements between the minister and chief executive (for departments) or board (for Crown entity). These plans or agreements:

• describe the full range of outputs to be delivered, including the associated performance measures and standards;

• set out the amount and basis on which the agency will be paid, or expects to earn revenue for delivering the outputs. This includes Crown funding, fees and levies or trading revenue (Steering Group Managing for Outcomes Roll-out 2002).

Output plans are cross-referenced in the job descriptions of departmental chief executives, to reinforce incentives for performance. The State Services Commission (SSC) conducts annual reviews of each chief

73 For example, the health sector occupational regulatory bodies recognised through the Health Practitioner Competence Assurance Act 2003 must report yearly to the Minister of Health (s. 134). Similarly, the Plumbers, Gasfitters and Drainlayers Board must provide a yearly report to the Minister for Building and Construction, who in turn must present it to the House (ss. 152-154 of the Plumbers, Gasfitters and Drainlayers Act 2006). These bodies tend not to receive any funding from the Crown.
executive’s performance against their job description and other government or ministerial expectations. Part of a chief executive’s salary is “at risk”, and paid out depending on levels of performance.

Another mechanism for signalling ministerial expectations to Crown entities is the Letter of Expectations. Letters of Expectations set out a minister’s specific priorities for the planning period or for the entity’s strategic direction. They are generally issued yearly or after the appointment of a new Chair, after legislative changes that affect the entity’s environment, or when a new minister takes up responsibility for the entity (SSC, 2006).

The Information Supporting the Estimates are part of the Budget documents. These documents describe how different areas of spending (appropriations) contribute to the government’s goals (including priorities, outcomes and impacts). They also outline trends in expenditure and the performance measures and delivery standards that will be applied to each appropriation.

Throughout the financial year, departments and Crown entities must report to ministers on their progress in delivering on their outputs and strategic objectives. Departments are also responsible for monitoring the performance, financial viability and capability of Crown entities and providing “Ministers with an independent view of the financial performance and cost-effectiveness of the entity” (SSC, 2006). Alongside this, the Treasury monitors the regulatory quality management system and periodically advises ministers on options to improve its performance (see Chapter 3 for more discussion of the Treasury’s role).

At the end of the financial year, departments and Crown entities must report to ministers on their achievements, and ministers are required to present these annual reports to Parliament. The reports form the basis for any future select committee financial review (see below). Departmental annual reports must include audited financial statements; a statement of service performance spelling out the levels of performance, the revenue and expenses achieved for each class of outputs supplied, as well as the information that is necessary to enable an informed assessment to be made of the department’s performance during the financial year (including an assessment against the intentions, measures, and standards set out at the start of the financial year in the information on the department’s future operating intentions. (s. 45(2), Public Finance Act 1989)

Crown entity reports have similar content requirements, but must (among other aspects) also include commentary on their performance as good employers, payments made to board members, and any Ministerial Directions issued during the year (s.151, Crown Entities Act 2004).

A recent innovation in the New Zealand accountability and performance assessment cycle is the Performance Improvement Framework (PIF) review. A PIF review is a review of an agency’s fitness-for-purpose today and for the future … a PIF review looks at the current state of an agency and how well placed it is to deal with the issues that confront it in the medium-term future. It then proposes areas where the agency needs to do the most work to make itself fit-for-purpose and fit-for-the future. (SSC, New Zealand Treasury & Department of Prime Minister and Cabinet (DPMC), 2012a, p. 3)

PIF reviews were introduced in 2009 and are conducted by independent reviewers. The reviewers make recommendations to agency Boards (for Crown entities) or chief executives (for departments), which they then accept or reject. 74 For departments, the agreed outcome of the review is reflected in the chief executive’s performance agreement.

The final regular accountability mechanism on ministers responsible for regulators is the electoral cycle. Although the performance of regulatory agencies seldom features prominently in election campaigns, ministers may be called on to justify their own performance on regulatory matters.

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74 The State Services Commission also has the right to comment on the lead reviewers’ recommendations, but the reviewers are not obliged to accept these comments.
Irregular mechanisms

Ministers have a number of other accountability levers they can pull, which can be of particular use where ministers are dissatisfied with aspects of a regulator’s performance.

Where the regulator in question is a Crown entity, ministers can, in some circumstances, issue directions and appoint or remove board members. These powers, and the constraints placed on ministers by the degree of Crown entity independence, were discussed in Chapter 5 (see Table 5.2). As noted in Chapter 5, Ministerial Directions have not been used often. The State Services Commissioner, with the agreement of the Governor-General in Council can remove departmental chief executives from office for “just cause or excuse” (s. 39, State Sector Act 1988).

Ministers may commission fundamental reviews of the performance of a regulator or regulatory regime. Options include an expenditure review, a policy review, a performance audit by the Office of the Auditor-General (see below), or Commissions of Inquiry. The options vary in terms of their intrusiveness and public profile, and focus on different issues.

Expenditure (or “baseline”) reviews test the value-for-money obtained from spending in a particular sector or organisation, especially the efficiency of agency management and the effectiveness of interventions (New Zealand Treasury, 2008). Policy reviews assess the fitness-for-purpose of underlying frameworks or legislation. They can be conducted internally by officials (for example, the current review of the Telecommunications Act 2001) or by external parties appointed by ministers (for example, the Capital Markets Taskforce).

Commissions of Inquiry “exist as distinct entities as they do not technically belong to the Legislature, the Executive, or the Judiciary. They do not decide questions put before them as a court does; rather they are set up by government to inquire into and report on all kinds of matters” (Palmer & Palmer, 2004). As Sir Ivor Richardson, former president of the Court of Appeal, notes, Commissions of Inquiry are often established to conduct “a searching inquiry … into events or rumours which have given rise to public concern with the object of ascertaining the truth and attributing blame if blame is due” (Richardson, 1989, p. 4). They tend to fall into one of two categories – investigation of “behaviour or conduct and the propriety of it” (such as the Cave Creek Commission and Pike River Commission); and investigation of policy issues (such as the Royal Commission into electoral law and Royal Commission into genetic modification) (Palmer & Palmer, 2004, p. 309).

Accountability to Parliament

Table 14.3 Mechanisms for accountability to Parliament

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Accountability criteria</th>
<th>Frequency</th>
<th>Strength</th>
</tr>
</thead>
<tbody>
<tr>
<td>Select committee inquiries</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Moderate</td>
</tr>
<tr>
<td>Select committee Estimates and financial review</td>
<td>Financial</td>
<td>Yearly (Estimates); as required (financial review)</td>
<td>Moderate</td>
</tr>
<tr>
<td>Regulations Review Committee</td>
<td>Procedural; substantive</td>
<td>As required</td>
<td>Potentially strong (but full power is seldom used).</td>
</tr>
<tr>
<td>Performance audit or investigation by the Office of the Auditor-General</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Moderate</td>
</tr>
<tr>
<td>Parliamentary questions or parliamentary debate</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Weak</td>
</tr>
</tbody>
</table>

75 For Crown entities, the responsible minister “may review the operations and performance of a Crown entity at any time” (s. 132, Crown Entities Act 2004).
Parliament is, in many respects, the central accountability mechanism of New Zealand’s political system. The Executive and its agents may not tax, borrow, levy or spend money without parliamentary authority,76 and ministers and their agents exercise powers granted through parliamentary means.

The main way that Parliament can call regulators or their responsible ministers to account is through Select Committees. As noted in Chapter 2, Select Committees play a prominent role in the New Zealand political system, scrutinising almost all draft legislation. Under Standing Orders (Parliament’s rules of operation), Select Committees have a wide scope of activity and considerable independence and influence. Palmer & Palmer (2004) comment:

Select committees are empowered to initiate their own inquiries. They are not dependent on receiving a direction from the House of Representatives … Select committees can inquire into virtually any subject of government policy, expenditure, and administration, and the decision whether to conduct such an inquiry will depend upon how important and politically significant the committee members consider the topic to be. Whether the recommendations made are taken up will be a question for the government, although it is obliged by Standing Orders to make a formal response to such select committee reports and the recommendations not more than ninety days after the report has been presented to the House. (p. 170)

Depending on the question and Select Committee in question, a committee may summon witnesses or documents as evidence or ask the Speaker of the House to issue a summons. However, this power is not used lightly and, as McGee (2005) notes, it is “used only as a last resort in a case where the evidence is vitally necessary to the inquiry that is being carried out” (p. 429).

Reflecting the constitutional principle that public money may only be spent with parliamentary authority, Select Committees play a central role in scrutinising how agencies use the funds allocated to them. Outside of inquiries, this scrutiny takes place through two main mechanisms: the annual review of the Estimates, and financial reviews.

- **Annual review of the Estimates:** After the Budget has been presented to Parliament, Select Committees have two months to examine the government’s proposed spending plans for the coming financial year. The Finance and Expenditure Committee may carry out this examination, or it may refer specific areas of spending (Votes) to the relevant subject Select Committee. Committees call for evidence from the responsible minister to justify the proposed spending and, under Standing Order 333, may recommend changes to the Vote. Any recommended changes must be confirmed by a parliamentary vote. Although the review of Estimates looks at all spending within a ministerial portfolio, it does provide an opportunity for Parliament to focus on particular areas, including the performance and value-for-money from regulators.77

- **Financial reviews:** Each year, Select Committees review the performance of a selection of departments, Crown Entities, officers of Parliament, State-owned enterprises or any other public organisation the House wishes to investigate. The purpose of the reviews “is to determine whether the entity concerned has performed as promised – whether its actual performance, both in supplying services and in managing its balance sheet and other assets, is consistent with forecast performance. It also involves considering how the entity is currently performing” (McGee, 2005, p. 510). The Finance and Expenditure Committee decides which agencies will be reviewed, and whether it will conduct the review itself or refer the topic on to the relevant subject Committee. While Select Committees do not have the power to require an agency to act on the findings of a review, a poor financial review report can be embarrassing. In addition, where a review reveals matters of concern, a Select Committee can conduct an inquiry into the agency or invite the Auditor-General to investigate (McGee, 2005, p. 513).

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76 Section 22, Constitution Act 1986.
77 Select Committees also review the Supplementary Estimates (which outline any additional expenses and capital spending required for the fiscal year that is about to end). While this presents an opportunity to explore specific areas of spending or agencies, in practice this seldom happens.
The Regulations Review Committee (RRC) is a specialised select committee that focuses “on the appropriateness of the use of regulations” (Regulations Review Committee, cited in Malone & Miller, 2012, p. 10). Chapter 5 in this report considered the role of the RRC in more detail.

A fourth accountability lever available to Parliament is the Office of the Controller and Auditor-General (OAG). OAG is an Office of Parliament, which “provides Parliament with independent assurance that state sector agencies are operating and accounting for their performance in line with Parliament’s intentions” (New Zealand Treasury, 2011d, p. 6). This includes auditing the financial statements of the Government and of all public entities, as well as conducting performance audits or inquiries into “any matter concerning a public entity’s use of its resources” (section 18(1), Public Audit Act 2001).

Performance audits can examine a public entity’s efficiency and effectiveness, compliance with statutory obligations, probity and financial prudence and use of public resources. Performance audits or inquiries can be conducted at the request of Parliament, a minister or agency or be initiated by the Auditor-General. In all cases, however, the decision on whether to carry out an audit or inquiry rests with the Auditor-General.

OAG has considerable investigatory powers, including the power to enter premises and inspect bank accounts, and the power to require the giving of evidence under oath or the presentation of documents. People or organisations who do not comply with a lawful request from the OAG may be fined. In addition, the Auditor-General also has a number of powers to ensure financial accountability, including the power to direct a minister to report to Parliament for unappropriated or otherwise unlawful spending and the ability to stop payments from Crown or departmental accounts that may be applied for unlawful or unappropriated purposes. Recommendations from an OAG performance audit or inquiry are not mandatory, but carry significant moral authority.

Finally, Members of Parliament can

- put written or oral questions to the minister responsible for a specific regulatory regime or agency, seeking information on its performance; or
- raise the performance of a specific agency in the House during the general debate or the debate on the Estimates, or seek the agreement of the Speaker and the House to have an urgent debate on the agency.

In the case of oral or written questions, Standing Orders require that an “answer that seeks to address the question asked must be given if it can be given consistently with the public interest” (Standing Order 383(1)). Parliamentary questions or debate do not oblige the minister or regulator to change behaviour, but can serve to highlight performance issues and create pressure for change.

**Accountability to regulated parties and the wider public**

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Accountability criteria</th>
<th>Frequency</th>
<th>Strength</th>
</tr>
</thead>
<tbody>
<tr>
<td>Judicial review or appeal</td>
<td>Procedural; substantive</td>
<td>As required</td>
<td>Strong, but depends on the capability of regulated parties to take action in court</td>
</tr>
<tr>
<td>Regulations Review Committee</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Potentially strong (but full power is seldom used)</td>
</tr>
<tr>
<td>Official Information Act 1982</td>
<td>Financial; procedural; substantive</td>
<td>As required</td>
<td>Moderate</td>
</tr>
<tr>
<td>Investigation by the Ombudsman</td>
<td>Procedural; substantive</td>
<td>As required</td>
<td>Strong (but can be overridden)</td>
</tr>
<tr>
<td>Media investigation</td>
<td>Can cover all three criteria</td>
<td>Varies</td>
<td>Moderate</td>
</tr>
</tbody>
</table>
The courts are more than just an accountability mechanism

As discussed in Chapter 10, the courts are more than just an accountability mechanism. They are “one of the arms of government,…exert an important checking function on the executive and legislative branches” and “go a considerable distance towards checking government excesses and preventing arbitrary and unfair decisions” (Palmer & Palmer 2004, pp.285-6).

In the context of regulation, the courts exercise this power when regulated parties seek to challenge a regulator’s decision or processes. Regulated parties can seek to call regulators to account for their actions through judicial review or an appeal. As noted earlier, the High Court has an important role supervising the Executive through its inherent powers of judicial review, which can test the legality, procedural fairness and reasonableness of a regulator’s action. At times, this can involve reviewing the substantive merit of a decision. Where Parliament provides for them, appeals deal directly with the substantive merits and correctness of a decision. In this way the Executive is not only accountable to regulated parties through the courts, but it accountable to the courts themselves.

Regulated parties (and the wider public) can also make use of the RRC, where the actions of a regulator fall within the grounds for drawing a regulation to the attention of the House.

Finally, as described in Chapter 8, statutory and common law obligations on regulators to consult with regulated parties also create accountability relationships. While these are generally weak accountability mechanisms, failure to properly fulfil the obligations may prompt a judicial review.

The main accountability mechanism open to the wider public is the Official Information Act 1982. The Act establishes the principle that official information “shall be made available unless there is good reason for withholding it” (section 5). The onus is on the minister or agency receiving the official information request to demonstrate that there are grounds for withholding the information, in line with the criteria laid out in the Act. Ministers or agencies receiving a request must also process it within a statutorily-specified period of time.

“Official information” is defined broadly as

[All information held by a Department, a Minister of the Crown in his or her official capacity, or an organisation subject to the OIA or Local Government Official Information and Meetings Act (LGOIMA) is official information. This includes information held by an independent contractor engaged by an agency, and information held by any advisory council or committee established for the purpose of assisting or advising a department, Minister or organisation.

The Ombudsmen consider that the definition of official information also includes knowledge of a particular fact or state of affairs held by officers in such organisations or Departments in their official capacity. The fact that such information has not yet been reduced to writing does not mean that it does not exist and is not “held” for the purposes of the Act. (Office of the Ombudsman, 2012b, p. 7)]

Official information may be requested by New Zealand citizens, permanent residents, a person who is in New Zealand, a body corporate incorporated in New Zealand, or a body corporate incorporated elsewhere but which “has a place of business in New Zealand” (s. 12, Official Information Act).

Most, but not all, regulators are subject to the Official Information Act. All departments of state are subject to the Act, as are virtually all Crown entities. However, the Law Commission’s 2012 review of official information legislation found that:

• the grounds for which agencies were included or not within the scope of the legislation were unclear,
• the public found it hard to find out whether or not a specific organisation was covered, and
• there were a number of anomalous exclusions from the scope of the Act (Law Commission, 2012b).

For example, the Law Commission found that:

The Plumbers, Gasfitters and Drainlayers Board and the Building Practitioners Board are included, but not the Electrical Workers Registration Board. … The Accounting Standards Review Board is included, but not the Council of Legal Education. (p. 336)
Most, but not all, regulators are subject to the Official Information Act.

Public interest criteria for withholding information are specified in legislation. A request may be declined without further inquiry where it is judged to meet the “conclusive” grounds for withholding information in section 6. These cover such matters as the impact of release on the defence, security and international relations of New Zealand, or where release would “prejudice the maintenance of the law”. Where a request is judged to meet the “other” grounds for withholding information (section 9), “a further inquiry is necessary as to whether other considerations make it desirable in the public interest to make the information available” (Law Commission, 2012b, p. 124).

Where a request for official information is declined, the requestor may appeal to the Ombudsman, an Officer of Parliament. If the Ombudsman concludes after an investigation that a declined request should be released, he or she can report to the minister or agency in question, recommending release. This recommendation imposes “a public duty” on the minister or agency to release the information within 21 working days (s. 32, Official Information Act). The Governor-General, through an Order in Council (also known as the “veto”), can override the public duty to release. But the veto has never been used (Law Commission, 2012b, p. 240). The Ombudsman is also restricted from recommending the release of information where the Prime Minister certifies that the release would prejudice defence, security of international relations, or where the Attorney-General certifies that it would “be likely to prejudice the prevention, investigation, or detection of offences” (s. 31b).

Official information investigations are only one part of the Ombudsmen’s functions. The Ombudsmen have a wide range of investigatory powers, covering over 4,000 organisations in the state sector and including:

- investigating state sector administration and decision making;
- dealing with requests for advice and guidance about alleged serious wrongdoing;
- monitoring and inspecting places of detention for cruel and inhuman treatment; and
- providing comment to the Ministry of Transport on applications for authorised access to personal information on the Motor Vehicle Register (Office of the Ombudsman, 2013).

Chapter 10 discussed the impact of resource constraints on the Ombudsmen’s ability to carry out its accountability functions.

Finally, investigation and campaigns by the media can create pressure on regulators or ministers to change behaviour. As Black (2012) observes,

> [a] highly critical media campaign can be more effective in causing the resignation of a chief executive of a regulatory body than any legal power to sack him. (p. 5)

**Accountability is a necessary but insufficient condition for better performance**

Accountability serves a range of purposes. It generates performance information and is used to give confidence to a range of stakeholders that the activities of the regulator are achieving the objectives of the regime. However

> … accountability by itself cannot ensure that regulatory or other programs are effective because performance also depends on such things as the appropriateness of the policy design, the mix of instruments that are used and quality of implementation. As articulated by Aucoin and Heintzman (2000), accountability concerns control of abuse of public authority, assurance that public resources are being appropriately used, and learning that facilitates pursuit of improvements. Stated differently, ensuring regulatory accountability might be considered a necessary but insufficient condition for increasing regulatory effectiveness. (May, 2007)
14.4 Performance and monitoring

The existing accountability processes provide multiple avenues to interrogate regulators about their behaviour, and a range of levers that can be pulled to influence this behaviour. To influence a regulator for the better in a timely and appropriate fashion, policymakers must have a sound understanding of how well the organisation is performing at the moment. Even so assessing the performance of regulators can still be a challenging task. Information is a critical input to evaluating regulator performance, but it needs to be the right information. The Commission found in Chapter 3 that there is a lack of regular and detailed reporting on the state of New Zealand regulators, and made recommendations to fill this gap. Gathering the right information requires monitors who understand the context the regulator operates in, who know what questions to ask, who are not afraid to probe when necessary, and who know how to use the data collected. Experience in New Zealand suggests that monitors of regulators have not always demonstrated these capabilities.

This section assesses the current state of monitoring. It discusses the inherent problems in assessing regulator performance, explores commentary on how effective current monitoring practice is, and points to areas for improvement.

What does Crown entity monitoring involve?

As discussed briefly in Section 14.3, where the regulator is a Crown entity, the portfolio department is responsible for monitoring the entity and providing advice to their Minister on the entity’s performance and strategic directions. This includes:

- engaging with the entity on draft SOIs, and advising their minister on the suitability of drafts (and on any changes required);
- advising Ministers, where relevant, on the content of any output agreements and/or Letters of Expectation;
- working with the entity, where relevant, to understand, assess and prepare requests for new funding from an upcoming Budget;
- monitoring upcoming Board vacancies, assessing skill and capability requirements, and advising the Minister on potential new Board members;
- monitoring the entity’s progress against the objectives, outputs or targets laid out in their Statement of Intent, output agreement and Letter of Expectation, and advising the Minister on how well the entity is performing;
- monitoring how well the entity is maintaining its financial viability and capability to deliver in future;
- keeping an eye on broader developments in the sector, and advising the Minister on the need for reviews, legislation and policy change (SSC, 2006).

As some of the items above show, monitoring is a relationship instead of a one-way process. The OAG (2009) observed:

> A professional, open relationship between Crown entities and monitoring departments assists departments in collecting the information they need for their monitoring work. It also allows them to have free and frank discussions about issues and risks when necessary. This sort of relationship is also important from a Crown entity’s perspective, so that they can be confident in discussing issues with the department. (p. 20)

It is also a far more active process than the term “monitoring” implies, and can involve challenging or posing hard questions to regulator Boards or staff about areas of performance. “Oversight” is perhaps a better way to describe the function.

Departments have a role in communicating Ministerial expectations and priorities to Crown entities. Crown entities, in turn, have obligations to keep their Ministers and departments informed of their performance or
emerging issues and risks. The Civil Aviation Authority (CAA) spelled out its external reporting and accountability processes in its submission:

“Weekly reports to the Minister (cc to the Ministry of Transport);
Regular briefings of the Minister and the Ministry of Transport on issues of importance…
Quarterly governance reporting to the Minister (cc to the Ministry of Transport);
An Aviation Safety Summary Report is published on a quarterly basis;
A Strategic Directions document is published periodically;
A Statement of Intent is published annually;
An Annual Report is published annually;
Ad-hoc Reports by the Auditor-General and others on aspects of the CAA’s operations; and
Monitoring by the ICAO [International Civil Aviation Organization] of the CAA’s performance in defined areas”’. (CAA, sub. 6, p. 65)

The State Service Commission recommends that departments:

• set a memorandum of understanding or “relationship letter” with the Crown entity to “clarify the services that a department performs - whether on behalf of the Minister, or to assist the Minister in carrying out his or her functions” (SSC, 2006, p. 6); and
• establish a monitoring plan to “focus monitoring efforts” and “help gather resources and build commitment” from the department’s senior management (Ibid, pp. 23-24).

Where the regulator is a department, Ministers may call on independent purchase advisors (such as seconded or appointed staff in their office) to help them with planning and accountability processes and performance assessment. Unlike Crown entities, no equivalent formalised and external monitoring process exists. This is in part because Ministers have greater control over, and more frequent interaction with, their departments. However, central agencies monitor the financial and regulatory management processes of departments (the Treasury) and the performance of chief executives in departments (SSC). This role is explained in more detail in Section 14.6.

What should monitoring and oversight of regulators involve?

In many respects, monitoring of regulators is not different from monitoring of other entities. Ministers need assurances that regulators are managing their finances and capability well, focusing on the delivery of agreed strategic objectives, reviewing their own performance and learning from experience, and acting in accordance with the law.

Ministers also need assurance that organisations are appropriately managing risks. Chapter 11 noted that regulation often deals with the management and control of risks to the public, and recent failures highlight how important it is for regulators to identify the full range of risks, accurately assess their scale and stability and respond effectively. Monitoring can help achieve these objectives, by reviewing risk identification and assessment processes.

Intelligence provided through monitoring is also an important input to the development of regulatory policy. Departments should use monitoring processes to assess the “quality and effectiveness of frameworks of regulation” and promote “good regulatory practices and sound advice on the subject” (SSC, New Zealand Treasury & DPMC 2013a, p.24). For example, in reviewing the performance of a regulator, departments should consider whether the regulatory framework is still fit-for-purpose. This might involve asking questions such as:

• How high are compliance levels? If they are not high, is this due to the performance of the regulator or weaknesses in the legislative framework (e.g. not enough powers, regulatory objectives that no longer reflect business or social expectations, wrong regulatory standard)?
• How stable are compliance levels? If they fluctuate considerably, what is driving this variability?
• Are the compliance strategies used by the regulator efficient – that is, do they achieve compliance at the lowest cost to both the regulator and regulated party? If not, are more or different tools required?

• Are issues emerging which potentially pose a significant risk of public harm, but for which the regulator has no or inadequate powers to respond?

Indicators that a regulatory regime is performing well are outlined below in Box 14.2.

F14.3 Key tasks for monitors of regulators are:

• providing assurance to Ministers that regulators have robust risk identification and assessment processes; and

• assessing the ongoing fitness-for-purpose of regulatory regimes.

The challenges of assessing regulator performance

Black (2012) highlights the many challenges that face those who hold regulators to account.

• **“Multiple hands”:** Often more than one regulator is involved in regulating a sector or pursuing specific objectives. This can make it hard to determine which agency has made the greatest contribution to the achievement of regulatory objectives.

• **Unclear roles or objectives:** Regulatory objectives may be expressed in vague or general terms, or may involve competing goals without guidance on how trade-offs should be made. There are “considerable difficulties in measuring performance against generally framed outcomes” (p. 9). The Commission discussed options for improving role clarity and reducing overlaps in Chapter 4.

• **Highly specialised knowledge:** A number of regulatory roles require “a high degree of technical and specialised knowledge, but which are often highly contestable” (p. 10). Non-experts can face serious challenges assessing whether regulators have made the right judgements.

• **The opacity of regulatory process:** Regulation is “a continuous process of negotiation, compromise and challenge – on both sides of the regulator-regulatee relationship. It is very hard for outsiders to penetrate or have visibility of that process”. (p. 11). This opacity is enhanced by the move to principle-based or process-based regulatory standards that both “rely more on the professional judgement of regulators”. This has implications for workforce capability (as discussed in Chapter 12).

• **Attribution:** How confident can monitors be that the absence of regulatory failures is due to the actions of the regulator? As Black (2012) observes,

  … assessing performance can require judgements to be made on counter-factuals: if there is no environmental degradation, is that because the environmental regulator has done a good job in preventing it and thus is a success, or does that show that it has not been sufficiently active as environmental indicators, though remaining stable, have not improved? Or is it because there has been an economic downturn and so industries are producing less pollution? (p. 9)

Attribution issues are not specific to regulators, and apply to many public agencies.

In the case of monitoring Crown entity regulators, a further challenge can be the “multiple hats” that a department wears with regard to their entity (Figure 14.2).
On one hand, departments must form an independent view of the entity's performance, which can involve tough questions and criticism (wearing their monitoring hat). On the other hand, departments often rely upon their entities to successfully deliver government policy initiatives. This requires a form of partnership between the two organisations (wearing the policy hat). These two objectives may conflict.

**How effective is monitoring and oversight?**

Commentary from a number of sources suggests significant scope exists to improve monitoring of regulators. These sources include the OAG, PIF reviews of departments responsible for overseeing major regulators, submissions to the inquiry and responses from chief executives in the public sector to a Commission survey.

**Office of the Auditor-General**

The OAG conducted a performance audit in 2009 on how departments monitor Crown entities. The audit focused on the practices of three departments, all of which oversaw regulators. While the Auditor-General found that all three departments were reasonably positioned to support their Ministers through their monitoring work, he also saw clear room for improvement. The OAG (2009) identified a number of common areas where better practice was needed, including:

- testing the robustness of Crown entity financial planning: It should be very clear how departments know about, or intend to check, the robustness of each entity’s financial planning, and what assurance or advice they are expected to provide to the Minister about this;
- clarifying roles and responsibilities for monitoring each Crown entity;
- using information about issues and risks to inform their monitoring work;
- providing relevant, timely advice to Ministers about each Crown entity’s statement of intent and its financial and non-financial performance; and
- working with Crown entities on specific monitoring work, so that the work could be carried out in a timely and efficient way (OAG, 2009).

The OAG made a number of recommendations to improve Crown entity monitoring (see Box 14.1).

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78 The Department of Internal Affairs, Ministry for Culture and Heritage, and Ministry of Economic Development (which has since been merged into the Ministry of Business, Innovation and Employment).
These recommendations do not appear to have been acted on. The Finance and Expenditure Select Committee considered the report and concluded it had “no matters to bring to the attention of the House” (Finance and Expenditure Select Committee, 2009). The Commission has not found evidence that the recommendations have been taken up across monitoring departments.

PIF reviews

Performance Improvement Framework reviews of departments responsible for overseeing significant Crown entity regulators reveal variable levels of practice and capability, and room for improvement:

Monitoring is an important means for the Ministry to exercise leadership within the sector; however, current arrangements with regard to Crown entity monitoring are narrowly focused on financial performance, with insufficient attention given to the extent to which the entity contributes to critical elements of the overall education sector performance. Some of this ineffectiveness in monitoring results from the lack of clarity about the key mechanisms and alignments needed to get the desired educational results. (SSC, New Zealand Treasury & DPMC, 2011b, p. 34)

There is no overarching organisational approach to assess effectiveness and efficiency of the monitoring function, although the evidence suggests that the team undertaking the function within MED is relatively small compared to the number and size of Crown entities monitored. Crown entities report significant improvement in their monitoring relationships with MED, with improved alignment between the Crown entity’s own performance analysis and reporting to its Board and Minister, and the
information requested by MED...There is significant lack of clarity between the roles of the Crown entity Boards and MED regarding monitoring, resulting in most Crown entities reporting that the relationship is positive (nice people at MED) but adds limited value or challenge. Engagement between MED and Crown entity personnel is generally collegial and positive but there is some frustration for Crown entities' chief executive officers and chairs where they find they are interacting on critical strategic issues with Tier 3 and 4 personnel within MED. (SSC, New Zealand Treasury & DPMC, 2012b, p. 32)

...the workload related to appointments compromise the ability of the team to undertake a truly value-add monitoring functions for the entities it has responsibility for. (SSC, New Zealand Treasury & DPMC, 2012c, p. 38)

EPA and MfE consider their working relationship to be strong...While it is early in the process, EPA considers MfE has added value in its oversight to date. MfE needs to do more than compliance monitoring and to ensure it continues to add value through its monitoring. To improve performance, MfE needs to monitor EPA's performance through a value-for-money lens, as well as assessing whether it is meeting its statutory objectives. (SSC, New Zealand Treasury & DPMC, 2012d, p. 34)

We received a number of comments about the Ministry's role in monitoring the various Crown entities it has accountability for. Some of these comments were positive, particularly as to the role the Chief Executive plays in ensuring there is good ongoing contact with the chief executives of the Crown entities. Other comments questioned whether the Ministry was aware of some of the key challenges facing these Crown entities and suggested therefore that the Ministry was not well placed to add value. The focus was often on more operational issues rather than those of a more strategic nature about goals, performance requirements and how to meet them. (SSC, New Zealand Treasury & DPMC, 2013a, pp. 24, 27)

Submissions

A number of submitters highlighted insufficiently resourced or active monitors as a problem:

Our sense is that the Treasury is currently under-resourced to effectively monitor and scrutinise the Reserve Bank and proposals coming from the Bank. We believe a much more focused and better-resourced effort is needed by the Treasury in this area. (Insurance Council of New Zealand, sub. 5, p. 6)

Some regulators come under the scrutiny of other government agencies – e.g. the Reserve Bank is overseen to some limited degree by the Treasury – but the extent of scrutiny and its effectiveness is open to question. Often, the overseeing government agencies also lack the accountability to perform the oversight well – it is likely that their own performance (and that of their CEO and other senior officials) is assessed by reference to higher priority functions than the assessment of regulators that come under their purview. (Mortlock Consulting, sub. 31, pp. 8-9)

Currently MBIE has oversight of independent economic regulators utilising tools under the Crown Entities Act. The difficulty is that there is no dedicated unit and any review of a regime has to fit within other priorities. This means whether there is a review is often arbitrary. The question of review is also subject to political input and may conflict with the department’s relationship with the regulator, which can be multi-faceted. (Vector, sub. 29, p. 29)

Another common theme in submission was that regulators had too much discretion over their own accountability and performance documents, and that too little use was made of the levers available to Ministers or departments:

Although regulators are generally required to publish annual reports of some nature, the tendency in New Zealand is for regulators to publish very little high quality information that relates to the performance of their functions. What is published is generally at a highly summarised level and mainly relates to such matters as:

- a summary of their activities over the reference period; and
- information on their costs (by reference to their budget), staffing levels, etc.

By and large, there is little quality information on the performance of their functions in ways that provide a basis for meaningful transparency and accountability. (Mortlock Consulting, sub. 31, p. 8)

Performance requirements in the SOIs are determined by the entity and tend to be high level. There are no specific requirements on the monitoring agency (MBIE), no consequences for poor performance and no process for obtaining stakeholder input...The Minister does not appear to use existing powers to input into and/or amend the SOI or review operations and performance. (Genesis, sub. 48, pp. 5-6)
Existing monitoring mechanisms under the Crown Entities Act are underutilised, possibly because they are viewed as weak accountability tools and/or because there are limited consequences for poor performance. (Vector, sub. 29, pp. 28-29)

The Ministry of Business, Innovation and Employment (MBIE) observed that “a key component of all of our regulatory failures” was “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” and a resulting “tendency to work-around systemic issues rather than addressing them”. Given their prevalence, MBIE questioned whether these barriers “may extend across the public service more generally” (sub. 52, pp. 3-4). They also highlighted that the risks of regulatory failure rise where

organisational norms and values … 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. (p. 4)

Regulator culture is discussed in more detail in Chapter 7.

Public sector chief executives

Regulator chief executives were split over the issue of whether formal monitoring of regulatory functions by other agencies improved the quality of regulation: 35% agreed, while 31% either disagreed or strongly disagreed (Figure 14.3). During its engagement meetings with regulators, the Commission also sought their views on the impact of monitoring on their operations. Regulators did not report monitoring processes as adding value to their work. This is consistent with the Commission’s previous findings in its inquiry into local government regulatory functions (NZPC, 2013a).

Figure 14.3 Chief executive agreement with the statement “formal monitoring of regulatory functions by other agencies improves the quality of regulation”

<table>
<thead>
<tr>
<th>0%</th>
<th>35%</th>
<th>26%</th>
<th>22%</th>
<th>9%</th>
<th>9%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>Agree</td>
<td>Neither agree nor disagree</td>
<td>Disagree</td>
<td>Strongly disagree</td>
<td>Don’t know</td>
</tr>
</tbody>
</table>


When asked which parties were most important in holding regulators to account, chief executives were most likely to identify regulated parties and then agency boards. External accountability relationships (such as to Ministers, the courts and OAG) rated more highly than those with other government departments or central agencies (Figure 14.4).
Figure 14.4 Which three organisations/stakeholders play the greatest role in holding your agency’s regulatory functions to account?

![Chart showing the percentage of respondents regarding the greatest role in holding the agency's regulatory functions to account.]


Notes:
1. Only 19 of the 33 (58%) regulators who received the survey had boards in place. 23 responses were received. Responses were confidential, so the Commission cannot identify what proportion of respondents had boards. As a result, the results in Figure 14.4 may underplay the significance of boards as sources of accountability.

14.5 Summing up

Monitors play a key role in ensuring the effective and efficient performance of regulators. If Ministers are to use their substantial powers to influence or direct regulators, they need good advice on how well regulators target and reduce harms, respond to wider developments and use the resources allocated to them. Current monitoring activity does not appear to meet this standard. Analysis by the Auditor-General indicates that some departments fail to provide satisfactory support to their Ministers. Similarly, the PIF review findings, and ambivalent responses from chief executives about the role of monitoring, suggests it is not contributing enough to regulatory quality and performance.

Comments in submissions about inactive monitors or underused intervention powers must be treated with care. The fact that “nuclear options” such as Ministerial Directions have seldom been used does not necessarily mean that Ministers and departments are failing to wield influence in other ways. The Commission did not collect evidence to directly test whether or how well Crown Entities Act powers are being used.
But the evidence from the Auditor-General and views of chief executives do lend weight to the notion that some Ministers are not being appropriately advised when to take action, as does MBIE’s assessment of the factors that have led to recent regulatory failures. There is also comment in public management literature that some Ministers have either struggled or chosen not to set clear performance expectations and demand that these be delivered (for example, Scott, 2001; Ryan, 2011).

At another level, however, feedback from submitters indicates that the accountability system may not be achieving one of its objectives – namely, giving confidence to regulated parties and the public that regulators are acting lawfully, reasonably, proportionately and effectively.

14.6 Areas for improvement

In considering how monitoring of regulators could be improved, the Commission explored existing performance information and processes. There is scope to clarify and raise performance expectations on monitoring departments, in particular through:

- more detailed guidance for departments and Ministers on Crown entity monitoring, which outlines issues they should look for in reviewing the performance of regulators;
- performance measures that better, and more consistently, reflect good practice in monitoring;
- departments developing and maintaining explicit statements of their monitoring roles and responsibilities; and
- more active oversight of departmental regulators by the SSC and the Treasury.

Better guidance for Ministers and departments

Although monitoring plays a key role in enabling accountability, the current guidance for monitors does not set high enough expectations, or provide enough detail around the sorts of issues that should be explored.

The three current sources of guidance for Ministers and departments are:

- a 2006 Cabinet Office Circular, spelling out Ministers’ roles and responsibilities in relation to Crown entities;
- an SSC guide for Ministers, which is designed to be read with the Cabinet Office Circular; and

Three broad weaknesses can be identified with the guides. First, the guide for Ministers underplays the importance of the monitoring relationship and the need for monitoring departments to be vigilant. Instead, departments are advised to minimise burdens on Crown entities:

> Ministers and their monitoring departments will ideally tell Crown entities in advance what information they must provide, and will try to keep requests for additional information to a minimum. Unanticipated demands for information can disrupt an effective working relationship between Ministers (and/or monitoring departments) and their Crown entities. (SSC, 2006)

While it is clearly preferable for departments to have agreed monitoring processes in place with their Crown entities, this should not take priority over ensuring that Ministers have the information and advice they require to assess the scale of any risks and the need for action.

Second, the guidance risks sending the signal that a monitoring department does not need to have a good and deep understanding of a Crown entity’s operating environment:

> Monitoring departments should focus monitoring activity on major opportunities and risks. Monitoring should be proportionate to the:
  - Minister’s needs;
  - scale of investment in, and spending on, Crown entities;
• risk posed by Crown entities; and
• opportunities that could be realised across the Minister’s area of responsibility. (SSC, 2006)

It is correct that monitoring departments should aim to take a proportionate approach in overseeing regulators, reflecting such issues as the scale and type of risks to the public being managed, and the competence of the regulator in carrying out its duties. The role of a monitor is not to duplicate or second guess operational decisions by Boards; it is to review an organisation’s overall performance.

However, a proportionate approach does not necessarily entail focusing solely on major opportunities and risks. As discussed in Chapter 11, regulators can face low frequency but high consequence events, small risks that can accumulate into significant threats, and new and emerging risks that are “off the radar”. In order to accurately assess a regulator’s performance, monitors need to form a view on how aware the organisation is of the full range of risks and how well it is responding to them. As noted by the Auditor-General, to form these views, monitors need “good overall sector knowledge, so that the department can alert the entity to more general issues that may affect the entity, connect the entity with other parts of the sector when necessary, and can be independently aware of emerging issues and risks” (OAG, 2009, p. 6).

Existing guidance for departments and Ministers on monitoring Crown entities underplays the importance of the monitoring relationship and risks sending the signal that a monitoring department does not need to have a detailed understanding of a Crown entity’s operations.

Third, the guidance documents provide little detail on the sorts of questions or issues monitoring departments and Ministers should look for and raise.

As noted earlier, monitors gain assurance that the regulatory system has the capabilities and attributes required to effectively identify and manage risks. MBIE’s submission identified “practices or conditions present in regulatory systems which are performing well” (Box 14.2).

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 Directions

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.

Source: MBIE, sub. 52, pp. 4-5.

The policy department is responsible for delivering some of these attributes. Others – especially c, d and e – are good measures of effective regulator and monitoring practice, and should be explicitly factored into monitoring processes.

**R14.1**

The State Services Commission and the Treasury should update guidance for Ministers and departments on monitoring Crown entities to:

- provide more detail on the issues that monitoring departments and Ministers should look for in reviewing the performance of Crown entity regulators;
- clearly express the importance of monitoring departments having the deep sectoral knowledge necessary to understand the regulator’s operating environment; and
- place more emphasis on vigilance and free and frank advice from monitoring departments.

**Clearer performance standards**

The detail and quality of performance standards around Crown entity regulator monitoring varies considerably. Without a clear statement of what is expected, it is hard to measure performance, hold departments to account or identify areas for improvement. Making performance standards explicit and public can also help counteract the risk that the department’s “policy hat” imperatives outweigh its “monitoring hat” responsibilities.

For a number of departments, monitoring activities are captured within output appropriations that cover a wide range of activities, with little in the way of performance measures that reflect good monitoring practice. The appropriations listed in Table 14.5 cover monitoring of the Commerce Commission, Financial Markets Authority, Electricity Authority, and Environmental Protection Authority (as well as several other non-regulatory Crown entities).
Table 14.5  Selected 2013/14 Crown monitoring appropriations and performance measures

<table>
<thead>
<tr>
<th>Vote</th>
<th>Description</th>
<th>Appropriation scope</th>
<th>Performance measure</th>
<th>Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td>VOTE COMMERCE: Business Law and Competition Operational Policy, Ministerial Servicing and Crown Entity Monitoring</td>
<td></td>
<td>This appropriation is limited to the development of operational policies in relation to financial sector legal frameworks, competition law and corporate governance, intellectual property, technical barriers to trade, trade rules remedies and tariffs, and other border issues, services to support the Minister, monitoring the performance and compliance of Crown Entities, and providing support and monitoring of statutory bodies.</td>
<td>Responses to Parliamentary Questions, Ministerial Correspondence and Ministerial Official Information Act 1982 requests are to be completed within either specified or statutory timeframes.</td>
<td>2013/4 Budget standard</td>
</tr>
<tr>
<td>VOTE ENERGY: Energy and Resources Operational Policy, Ministerial Servicing and Crown Entity Monitoring</td>
<td></td>
<td>This appropriation is limited to the development of operational policies in relation to the operation of energy and resource markets (electricity, oil, gas, geothermal, coal, minerals and natural related resources) and energy efficiency and conservation issues, services to support the Minister, and monitoring the performance and compliance of Crown Entities.</td>
<td>Responses to Parliamentary Questions, Ministerial Correspondence and Ministerial Official Information Act 1982 requests are to be completed within either specified or statutory timeframes.</td>
<td>2013/4 Budget standard</td>
</tr>
<tr>
<td>VOTE ENVIRONMENT: Resource Management Policy Advice (part of Improving Resource Management MCOA)</td>
<td></td>
<td>This output class is limited to the provision of advice (including second opinion advice and contributions to policy advice led by other agencies) to support decision making by Ministers on government policy matters relating to the management of natural and physical resources in New Zealand.</td>
<td>Percentage of agreed deliverables in relation to monitoring relevant Crown entities that are completed within agreed timeframes.</td>
<td>2013/4 Budget standard</td>
</tr>
</tbody>
</table>


Other Votes provide a richer set of performance measures for monitoring. Vote Transport (which covers such regulators as the New Zealand Transport Agency, Civil Aviation Authority and Maritime New Zealand) is one example:

<table>
<thead>
<tr>
<th>Vote</th>
<th>Description</th>
<th>Appropriation scope</th>
<th>Performance measure</th>
<th>Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td>VOTE TRANSPORT: Governance and Performance Advice on Crown Entities (part of Improving Resource Management MCOA)</td>
<td></td>
<td>This output class is limited to monitoring of and advice on the governance, performance and capability of transport Crown agencies.</td>
<td>Advice on transport Crown entity board appointments provided to agreed timeframes.</td>
<td>2013/4 Budget standard</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Regularity of Ministry strategic discussions with each Crown entity Chair/Board</td>
<td></td>
</tr>
</tbody>
</table>
There is scope to provide a more consistent and detailed set of monitoring performance standards. Some important measures of performance – such as detailed understanding of the entity’s operating environment and departmental vigilance in testing entity performance – may be difficult to define, and may fit better in other accountability documents. But difficulty in defining performance expectations is no reason not to try, especially as the issue applies to a range of public services.

The Treasury and the SSC, as the central agencies responsible for the performance management and Crown entity frameworks, should lead a process with departments responsible for monitoring regulatory Crown entities to:

- define common and richer performance measures for regulatory Crown entity monitoring, drawing off the OAG’s recommendations around good practice, existing examples of good performance measures, and the conditions of well-performing regulatory systems outlined by MBIE;
- update performance information around regulatory Crown entity monitoring in accountability documents (especially Strategic Intentions, output plans, Information Supporting the Estimates, Annual Reports) in time for the 2015/16 financial year; and
- reflect the new performance measures in the performance agreements and reviews of departmental chief executives.

The Treasury and the State Services Commission should work with monitoring departments to:

- define common and richer performance measures for regulator Crown entity monitoring;
- update performance information in accountability documents around monitoring in time for the 2015/16 financial year; and
- reflect the new measures in the performance agreements and reviews of departmental chief executives.

Clearer and more sophisticated statements of the monitoring role

One key finding from the Auditor-General’s audit of Crown entity monitoring was that departments and entities often lacked a clear and shared understanding of each other’s role:

> Formal agreements between Ministers and Crown entities set out their roles and responsibilities, and included information about the broad role of the monitoring departments. However, representatives from four Crown entities told us that a lack of clarity about the monitoring department’s role created difficulties for them. …It is important that each of the three parties has a clear understanding of their roles and responsibilities, and how this relates to the roles and responsibilities of those they interact with. This helps to avoid confusion about, or duplication of, roles. (OAG, 2009, p. 15)

The Auditor-General recommended that monitoring departments develop a “clear, up-to-date record of the monitoring responsibilities, together with clear information about the monitoring department’s role”. In the OAG’s view, this would help staff to:

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79 For example, measures of a monitor’s capability might more logically fit in the department’s Strategic Intentions, output plan or Annual Report, reflecting the chief executive’s statutory responsibility to maintain the organisation’s “medium- and long-term sustainability, organisational health, capability, and capacity to offer free and frank advice to successive governments” (s. 32, State Sector Act 1988).
understand the scope of the monitoring work they are expected to carry out;

plan for monitoring work;

approach monitoring tasks with a view to fulfilling their monitoring role; and

check that they have carried out the monitoring tasks they needed to do. (p. 18)

The Commission agrees that there would be benefit in departments developing and maintaining clear statements of their monitoring responsibilities and approach. If done in conjunction with Crown entities and Ministers, such a process would allow the parties to review the health of the relationship. It would also help clarify expectations and provide a benchmark against which each party could hold the other to account.

Most importantly from the perspective of monitoring regulators, this process of developing the statement would allow departments to assess whether they are asking the right questions and monitoring the right issues. Discussion above and in other chapters in this report have highlighted areas where greater attention from monitors could be fruitful. A framework that could be applied in developing a departmental regulator monitoring statement is outlined in Figure 14.5 below.

**Figure 14.5 Possible framework for a regulator monitoring statement**

- **The Ministry’s approach to monitoring**
  - Assessing the success of boards’ efforts to drive performance is at the centre of the Ministry’s monitoring model
  - An ‘assist’ relationship with entity chief executives
  - A risk aware perspective
  - Day-to-day information exchange takes place between entity managers and the Ministry

- **What Ministers need to know**
  - Is the entity doing what it says it’s doing?
  - Is the entity achieving the goals it intended to achieve?
  - Is the entity’s work value for money?
  - Do any material risks arise from the entity’s work or proposals?
  - Do the entity’s proposals for new work have merit?
  - Does the entity have visibility of all the risks?
  - Is the entity effectively monitoring and managing sources of potential public harm?

- **Typical questions the Ministry needs to know**
  - Are the entities and their interventions effective and what evidence supports this?
  - Are current arrangements coherent?
  - Are costs justified for the quantity and quality of services provided?
  - What is the entity doing to reduce costs?
  - How effectively is the entity reviewing and improving its implementation of the regime?
  - Does the entity make effective use of business intelligence?
  - Does the entity have a culture of raising risks and issues, and clear procedures for working through and addressing them?
  - How well does the entity measure and respond to changes in the regulated sector?

- **Characteristics of effective monitoring**
  - Based on a rich information trade
  - Focuses on information the board also needs
  - Enables tough questions to be answered
  - Minimises compliance costs
  - Leads to substantive dialogue about the ongoing fitness-for-purpose of the regulatory regime, and opportunities for improvement

*Source: adapted from Ministry for Culture and Heritage, 2013.*
Departments responsible for monitoring regulator Crown entities should develop and maintain explicit statements of their monitoring roles and responsibilities. In doing so, departments should regularly review whether the monitoring relationship:

- gives Ministers the assurance they need about risk identification and management;
- allows departments to accurately assess the performance of regulators; and
- promotes substantive dialogue with entities about the fitness-for-purpose of the regime.

Are there other questions or characteristics that a monitoring approach for Crown entity regulators should include?

More active oversight of departmental regulators

Much of the evidence considered so far in this chapter has focused on the relationship between Ministers and Crown entities. At one level this is entirely appropriate: a significant proportion of regulatory agencies are Crown entities and the model involves a degree of distance from Ministers that requires careful consideration of accountability processes. But departments also play a major role in implementing regulatory regimes and this role may be increasing, with the trend towards greater agency consolidation that was identified in Chapter 5. In addition, two of the more prominent regulatory failures to have occurred over the past 20 years – the Pike River mine tragedy and leaky buildings – were in regimes implemented by departments.

Ministers have more control over departments than Crown entities, and “decide both the direction and the priorities for their departments” (Cabinet Office, 2008, p. 37). Ministers can change these directions and priorities as required and the opportunities to do so are greater than with Crown entities, given the frequent Ministerial interaction with their departments. However, as with Crown entities, if Ministers are to intervene effectively and in a timely manner to ensure effective regulatory implementation by departments, they need good sources of information about risk and performance levels.

The Treasury and the SSC play a role with regards to departments that is most analogous to the monitoring department-Crown entity relationship. The Treasury monitors the financial and regulatory quality performance of departments, and the State Services Commissioner has a number of statutory functions of relevance, including:

- reviewing the State sector system in order to advise on possible improvements to agency, sector, and system-wide performance;
- reviewing the performance of each department and each departmental agency;
- appointing leaders of the Public Service, which includes—
  a) acting as the employer of chief executives of departments and chief executives of departmental agencies; and
  b) reviewing the performance of chief executives of departments and chief executives of departmental agencies;
- promoting leadership capability in departments and other agencies;
- promoting and reinforcing standards of integrity and conduct in the State services; and
- promoting transparent accountability in the State services (s. 6 of the State Sector Act 1988).
Both departments have taken steps recently to increase their oversight of departmental regulatory performance. As outlined in Chapter 3, in 2013 the Treasury collected information from departments on how they are giving effect to Cabinet’s regulatory stewardship expectations. In addition, the SSC updated its PIF model in January 2014 to more intensively assess how well the agency being reviewed is carrying out its regulatory stewardship responsibilities (one of the new questions is outlined in Table 14.6). The upgrade will be trialled with MBIE and is intended to be used with agencies that have a “significant regulatory footprint” (SSC, New Zealand Treasury & DPMC, 2014, p.3).

### Table 14.6 New PIF question on regulatory stewardship

<table>
<thead>
<tr>
<th>Lead question</th>
<th>Lines of inquiry</th>
<th>Signposts</th>
</tr>
</thead>
<tbody>
<tr>
<td>How well does the agency exercise its stewardship role over regulation?</td>
<td><strong>Understanding of regulatory span.</strong> How does the agency understand the scope of the regulation for which it has a stewardship responsibility?</td>
<td>The agency manages key legislative interventions to deliver benefits that exceed total costs.</td>
</tr>
<tr>
<td></td>
<td><strong>Understanding of regulatory impact and risk.</strong> How does the agency know about the impacts (positive and negative) of the different areas of regulation for which it is responsible? Has the agency clearly identified the key areas of risk to the effectiveness of that regulation?</td>
<td>Analysis demonstrates current interventions deliver higher net benefits than alternatives.</td>
</tr>
<tr>
<td></td>
<td><strong>Approach to regulatory improvement.</strong> How proactive is the agency in identifying and flagging the need or opportunity for regulatory changes? Does the agency consider all avenues for potential regulatory improvement? How does the agency prioritise its identified opportunities for regulatory improvement?</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Quality of regulatory analysis and advice.</strong> How does the agency use evidence and operational intelligence to inform its analysis of the underlying problem and available policy options? How complete and coherent is the agency’s analysis of potential impacts? To what extent does the agency offer free and frank advice to Ministers on the relative merits and risks of the regulatory options?</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Robustness of regulatory design.</strong> Are affected parties, subject experts and other stakeholders appropriately consulted on the regulatory design choices? What other testing processes and techniques are used by the agency to ensure the regulatory design is workable and covers all necessary matters?</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Capacity and capability to manage.</strong> How well does the agency understand the regulated community and how it operates? How effectively does the agency communicate with the regulatory community, other agencies with related regulatory roles and other interested stakeholders? Does the agency have the technical skills, capacity and sources of evidence of intelligence to appropriately discharge its regulatory duties? What strategies does the agency employ for mitigating the key risks to the effectiveness of its regulation?</td>
<td></td>
</tr>
</tbody>
</table>

*Source: SSC/New Zealand Treasury/DPMC, 2014.*

Although submitters were largely silent on the issue of monitoring departments, a number argued for the Treasury to play a more prominent role and several proposed an independent organisation to carry out performance reviews or audits of regulators (IAG, sub. 10, pp. 10-11; Vector, sub. 29, pp. 28-29; Mighty River Power, sub. 30, p. 15; New Zealand Airports Association, sub. 33, pp. 18-19; Genesis, sub. 48, pp. 3-4).
The Commission was not convinced of the need for a new, independent organisation to oversee regulators. Enough tools and avenues are available under current accountability processes to provide meaningful oversight of regulators. The challenge is to put enough attention and energy into these processes.

For central agencies, the challenge is to ensure that their new tools for focusing on regulatory management provide useful information for policymakers and encourage chief executives to lift performance. Findings from the Commission’s survey of regulator chief executives indicate that central agencies have some way to go before they are seen to be playing a major role in holding regulators to account (Figure 14.4). The Commission also noted the assessments in the recent PIF review of the SSC that

> [t]he challenge now is for SSC to use the system findings from PIF to drive improvement in individual agencies and the system… To enable SSC to deliver on this measure, and to drive effective improvement through the system, we suggest that specific improvement measures, as identified by PIF reviews, need to be applied to individual agencies as well, through the annual chief executive expectations letter. (SSC, New Zealand Treasury & DPMC, 2013b, p. 37)

To promote better performance and provide greater confidence to the public and regulated parties about the accountability system, the information about departmental regulatory performance that PIF generates and Treasury surveillance should be made more transparent and used to inform reviews of the chief executive’s performance. This implies:

- the Treasury publishing findings from the Regulatory System Report and other surveillance mechanisms (including the standardised information processes recommended in Chapter 3) about departmental regulatory stewardship activities; and
- the SSC developing explicit measures for regulatory performance in chief executive performance agreements and annual expectations letters, and using PIF and Treasury surveillance information in reviewing performance.

The SSC’s response to its recent PIF review stated that it will “change its approach to setting chief executive performance expectations. We will align these more closely to the priorities of government and to the fulfilment of stewardship obligations. The system for chief executive remuneration will also be changed to support this” (SSC, New Zealand Treasury & DPMC, 2013b, p. 5). This is a timely opportunity to more closely reflect in their performance expectations the regulatory stewardship obligations of chief executives.

**R14.4**

The performance of departmental regulators should be strengthened by:

- the Treasury publishing the findings from the Regulatory System Report about departmental stewardship activities;
- the State Services Commission (SSC) developing explicit measures for regulatory performance in chief executive performance agreements and annual expectations letters; and
- SSC using PIF and Treasury surveillance information about departmental regulatory performance in reviewing the performance of chief executives.

**14.7 Conclusion**

New Zealand’s accountability systems provide multiple opportunities for those affected by regulation to challenge agencies and for those responsible for a regulator to change the agency’s behaviour, where necessary. The issue is whether the opportunities to change a regulator’s behaviour are being taken up frequently enough, or at the right time.

Under the New Zealand system, Ministers have overall responsibility for regulators and hold many of the levers to change agency behaviours. Their ability to ensure regulators are acting efficiently, effectively and appropriately depends in large part on the information and advice they receive. Where regulators are
Crown entities, this information and advice comes from the Minister’s department. Where the regulator is a department, it should come from central agencies.

The Commission considers that monitoring is a key link and the weakest link in the current accountability system. Evidence collected through the inquiry indicated that some departments may not fully understand their monitoring roles and responsibilities, monitoring is not having enough effect on regulatory quality, and that expectations on departments to monitor well are not strong enough. For departmental regulators, central agencies have recently added new tools to assess regulatory performance. But these tools are either still being implemented or need to be properly connected with other accountability processes, in particular chief executive performance reviews.

The changes recommended in this chapter seek to clarify and raise performance expectations on monitors. They are not designed to create new mechanisms, but are intended to ensure that the existing mechanisms are used to their full effect. This is not to say that departments will not need to make changes to their practices. Effective monitoring requires a combination of capable staff, good sector knowledge and intelligence, and a commitment by senior leaders of departments to ensure that the imperatives of the “policy hat” do not cut across the duties under the “monitoring hat”.
15 System-wide regulatory review

Key points

- The New Zealand Government is implementing a suite of initiatives to improve how the stock of regulation is managed. New Zealand does not use many of the approaches to system-wide evaluation of regulatory regimes that are used in other countries, some of which have been identified as involving low effort and potentially low/high return in those countries.

- To improve the effectiveness of these initiatives, the Government should:
  - articulate in more detail its strategy for improving how the stock of regulation is managed, indicating how the initiatives it is implementing fit within the strategy and how success will be measured;
  - ensure departments satisfy Cabinet’s expectations of their responsibilities for keeping the regulatory regimes they are responsible for up to date; and
  - require departments to explain their plans for monitoring, evaluation and review in their papers for Cabinet Legislation Committee, and amend the “Disclosure requirements for government legislation” to make this expectation clear. Departments’ plans should be proportional to the significance of the regulation.

- Implementation of the Government’s initiatives for keeping the stock of regulation up to date should be guided by principles, building an approach that:
  - ensures that the scale and scope of evaluations is proportionate to the impacts of regulation;
  - provides transparent reporting of the Government’s strategy, work programme and progress in achieving performance targets;
  - clearly defines responsibility for managing the stock of regulation;
  - is based on consultation with those affected by regulation;
  - is driven by a need to prioritise effort where the payoff is expected to be largest; and
  - is adequately resourced, so that people with the capabilities to undertake effective evaluations can implement it.

15.1 Introduction

New Zealand’s large stock of regulation is growing rapidly (Table 15.1). The Parliamentary Counsel Office’s database of legislation (www.legislation.co.nz) provides a breakdown of the number of Acts and “legislative instruments” (which is broadly similar in nature to the Commission’s definition of “secondary legislation” or “delegated legislation” in Table 2.1). Currently 1,077 Acts and 2,496 legislative instruments (including regulations) are in force. If amendment Acts and legislative instruments are included, the numbers increase to 2,871 Acts and 4,950 legislative instruments. In 2013, 148 Acts and 483 legislative instruments were enacted, 20 Acts were repealed and 243 legislative instruments were revoked. Determining whether this stock of regulation is achieving the outcomes for which it was enacted, and producing benefits that outweigh the costs, requires a process for evaluation.
Table 15.1  New Zealand regulatory stock

<table>
<thead>
<tr>
<th>Acts(^1) or Legislative Instruments</th>
<th>Number (^2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Acts currently in force (excluding amendment Acts)</td>
<td>1,077</td>
</tr>
<tr>
<td>Number of Acts currently in force (including amendment Acts)</td>
<td>2,871</td>
</tr>
<tr>
<td>Number of Acts enacted in 2013 (including amendment Acts and Acts not yet in force)</td>
<td>148</td>
</tr>
<tr>
<td>Number of Acts repealed in 2013 (including amendment Acts)</td>
<td>20</td>
</tr>
<tr>
<td>Number of Legislative Instruments(^3) currently in force (excluding amendment Instruments)</td>
<td>2,496</td>
</tr>
<tr>
<td>Number of Legislative Instruments(^3) currently in force (including amendment Instruments)</td>
<td>4,950</td>
</tr>
<tr>
<td>Number of Legislative Instruments enacted in 2013 (including amendment Instruments and Instruments not yet in force)</td>
<td>483</td>
</tr>
<tr>
<td>Number of Legislative Instruments revoked in 2013 (including amendment Instruments)</td>
<td>243</td>
</tr>
</tbody>
</table>

Source: New Zealand Legal Information Institute and Parliamentary Counsel Office databases (see Note 1 below).

Notes:

1. This table is limited in focus to “public” Acts, and excludes local, private, provincial, and imperial acts. The Parliamentary Counsel Office defines a “public Act” in the glossary to its Legislation New Zealand website: “A public Act is an Act that affects the public at large. It deals with matters of public policy and is promoted by the Government or a member of Parliament who is not a Minister”.


3. The Parliamentary Counsel Office defines a “legislative instrument” in the glossary to its Legislation New Zealand website: “Legislative instrument” is defined in section 4 of the Legislation Act 2012. They can include Orders in Council, regulations, rules, notices, determinations, proclamations, or warrants. Legislative Instruments are laws made by the Governor-General, Ministers of the Crown, and certain other bodies under powers conferred by an Act of Parliament. Certain resolutions of the House of Representatives are also classed as Legislative Instruments. Legislative Instruments generally deal with technical details that may be subject to frequent change. Before 5 August 2013, legislation of this type was in general known as “Regulations”, or “Statutory Regulations”. On this website, these documents are now found under “Legislative Instruments”.

Chapter 2 pointed out that regulatory regimes in New Zealand can easily become rigid and obsolete. This reflects the strongly statute-driven system in New Zealand and the weakness of review and evaluation systems. As a result, New Zealand regulation can struggle to keep up with changes in technology or public expectations. One consequence is that regulators often have to work with legislation that is outdated or not fit-for-purpose (Chapter 5). The Treasury suggests that there needs to be

more systematic identification and prioritisation of problems or potential improvements in the existing stock of legislation (because we know legislative mistakes can be made; that legislation can become less effective or redundant over time as the policy environment changes; and assessing the cost and performance is a neglected and under-resourced task compared with assessing government spending. (New Zealand Treasury, 2013h, p. 7)

Other countries face similar challenges in keeping their regulation up to date:

One of the most important tasks facing governments today is updating of the accumulated regulations and formalities that have gone unexamined over years or decades. National regulatory systems require periodic maintenance. Periodic and systematic review of existing regulations is needed to ensure that outcomes are assessed, unneeded or inefficient rules are weeded out, and needed rules are adapted to new economic and social conditions. (Organisation for Economic Co-operation and Development [OECD], 1997, p. 224)

Most approaches to managing the stock of regulation involve some form of evaluation. This chapter explains what evaluation is (Section 15.2) and shows that New Zealand has not picked up approaches to managing the stock of regulation (applying some form of evaluation) that are used internationally (Section 15.3). It argues that the Government’s evolving approach to managing this stock contains many initiatives, but still has gaps. Implementation of the policy initiatives will need to be managed carefully (Section 15.4).
15.2 What is evaluation?

The OECD defines evaluation as

… systematic and analytical assessments of important aspects of a government activity (here: regulatory tools and institutions) and its value, with a view to creating or enhancing regulatory policy feedback – that is, enhancing the future performance of the activity being evaluated. (2004b, p. 11)

Evaluation is not a well-developed process in New Zealand, although examples do exist such as the Performance Improvement Framework. Another important example is the Education Review Office (ERO), which reviews early childhood services and schools. Broader lessons from ERO’s approach include that reviews are intended to help schools strengthen their capacity, and that to achieve this it is useful to:

- combine internal and external reviews;
- base reviews on a clearly articulated process, with ERO support for schools in their use of that process; and
- vary the frequency of review according to ERO’s assessment of the educational health of the school, which signals a risk-based approach to review (Box 15.1).

Box 15.1 Evaluation by the Education Review Office

The evaluation of education providers is based on supporting effective self-review processes, supplemented with differentiated external review.

Schools are required to undertake self-review, and the ERO provides support tools and training to build self-review capability and use self-review for school improvement.

ERO is legally responsible for the external evaluation of school quality. It can initiate a review on its own initiative, at the request of the Minister, or as part of a regular review cycle. ERO has legal powers of entry and inspection.

The purpose of a review is to support a school to strengthen its capacity to promote students’ learning and achievement. Schools undertake their self-review in preparation for the external review, and the review coordinator and team work with the schools’ board and leadership team to establish a shared commitment to the review process.

- For schools experiencing difficulty, ERO institutes a longitudinal review methodology over a period of 1-2 years. These schools receive extra support and professional development from the Ministry of Education.
- Schools performing well are reviewed on average every 3 years, with a focus on identifying areas to improve and on ways to strengthen self-review.
- Schools with the strongest performance and self-review capacity are reviewed every 4-5 years, because it is expected they can understand their own performance and respond appropriately.


This chapter is about the evaluation of regulation. Evaluation can take place before or after a policy is implemented. A regulatory impact statement (RIS) is used in many countries, including New Zealand, to assess the anticipated impacts of a regulatory policy. However, a RIS is only a projection, and needs to be supplemented by evaluations of how a policy has worked in practice. International experts such as the OECD and the National Audit Office in the United Kingdom consider that ex post evaluation is an integral part of good policy making:
Management is often described as a cycle of planning/preparation, budgeting, implementation and evaluation. Evaluation is the link which closes the circle and completes the feedback loop. The evaluated policy or programme is improved, expanded or replaced. (OECD, 1999, p. 13)

Regulators should constantly review the efficiency and effectiveness of their regulations, in order to determine whether the desired improvements in regulatory outcomes are being realised and if these benefits still justify the costs of intervention. (NAO, 2007, p. 4)

Coglianese (2012, p. 14) suggests that evaluation “answers the question of whether a treatment (i.e., a regulation or regulatory policy) works in terms of reducing a problem”. To a considerable extent, this depends on how well a regulation or regulatory policy was implemented. This chapter considers the second set of questions that evaluations can consider: whether a regulation is still needed, and whether it remains effective in achieving its objectives and does so at lower cost than feasible alternatives. Regulations are typically long-lived, and the original problem that justified intervention, as well as the options for addressing it, may well change over the life of a regulation.

The key stages of evaluation usually include:

- determining the purpose of the evaluation;
- setting information requirements and formulating research questions;
- designing the evaluation (including choice of methodology);
- collecting data;
- analysing data, and
- formulating conclusions and recommendations (VCEC, 2011, p. 135).

These stages highlight that preparing for an evaluation begins when a policy is first implemented. For example, data collection needs to begin when a policy is implemented, not when the evaluation takes place some years later.

**Barriers to evaluation**

The barriers to evaluation are considerable.

- Evaluation is hard, even when data is available. For example, evaluation requires attributing how much regulation has contributed to outcomes that are also influenced by other factors. If key performance indicators, baseline estimation and a process for collecting data were not developed when a regulation was implemented, evaluating its impacts years later might not be possible (VCEC, 2011, p. 140).

- Ambiguous regulatory objectives make it difficult to evaluate what a regulation has achieved, for the obvious reason that what it was put in place to achieve has not been specified. Chapter 4 argued that ambiguity in objectives is common.

- Conducting evaluations involves costs, which may be substantial for sophisticated reviews, and diverts resources from activities that might seem to yield more immediate results.

- Evaluation results may reveal weaknesses in a policy or process and can provoke resistance to change, although well-managed evaluation processes will seek to avoid this.

- Evaluation may be also resisted by people who benefit from a regulation, and are concerned that evaluation may erode this benefit.

Given such barriers, evaluation may not be the norm (or even occasional) unless it has a “champion”. Yet Ministerial responsibility for managing the stock of regulation is not clear:

In principle the doctrine of Ministerial responsibility applies – Ministers are responsible for regulatory policy, and are answerable to the [H]ouse on policy and administrative and operational matters while public agencies are responsible for the actual administration of regulation. In practice the mechanisms
to make Ministers answerable for the management of the stock of regulations are highly attenuated. ... there is no standard process to make the executive answerable for the administration and maintenance of legislation as a matter of course. (Gill & Frankel, 2013, p. 9)

And there is little support for evaluation in official handbooks:

The Treasury’s (2009) Regulatory Impact Handbook provides guidance to staff developing new regulatory proposals. The handbook contains a half page of aspirational material on the need for monitoring, feedback and review. There is no formal expectation that the introduction of regulations will be accompanied by programmed review, nor requirements to undertake formative or summative evaluations, nor monitoring and reporting requirements beyond that required for compliance with the Public Finance Act as discussed above. There is no discussion in the handbook of how and when to develop evaluation plans, monitoring and measurement plans, embedded review clauses, sunset clauses or even links to examples of review provisions. (Gill & Frankel, 2013, p. 10)

15.3 Systemic approaches to reviewing the stock of regulation used internationally

A suite of approaches

There are many different approaches to managing the stock of regulation, with differing degrees of rigour and varying breadth of coverage, and some of which involve arbitrary rules rather than evaluation. Table 15.1 sets out nine approaches commonly used in other countries.

Two of these approaches have been used recently in New Zealand. Regulator-based reviews are undertaken, as outlined in Chapter 14. In depth reviews - one of the more costly approaches - are also used, often prompted by a major event or perceived regulatory failure. The Ministry for Business, Innovation and Employment (MBIE) submitted that three regulatory systems for which it is responsible have suffered systemic failures in recent years: financial market regulation, health and safety regulation, and building standards regulation. These have triggered in-depth reviews:

- the Commerce Committee inquiry into finance company failures;
- the Royal Commission on the Pike River Coal Mine Tragedy;
- the independent taskforce on workplace health and safety; and
- reports on building standards that include the Report of the Overview Group on the Weathertightness of Buildings and a review of the Building Act. (sub. 52)

New Zealand has not adopted general red tape targets, regulatory budgets, or “one-in, one-out” rules, and has made little use of embedded reviews, or of sunsetting, principle-based reviews, and stocktakes. There are, however, examples of some of these approaches being used in specific cases.

- While there is no general sunsetting requirement, it is occasionally required in individual Acts (for example, the Mental Health Commission Act 1996).
- Some legislation has embedded review provisions. For example, section 157AA of the Telecommunications Act 2001 requires the Minister to commence a review of the policy framework for regulating telecommunications services in New Zealand by 30 September 2016.
- A report by the Ministry of Economic Development, while stating clearly that it is not a comprehensive stocktake, surveyed a large number of initiatives to reduce the compliance costs of regulation in response to a Government commitment “to review existing regulation in order to remove requirements that are unnecessary, ineffective or excessively costly” (2011, p. 6).
## Table 15.2  Use of system-wide approaches to evaluation in New Zealand

<table>
<thead>
<tr>
<th>Approach</th>
<th>Description</th>
<th>Comment</th>
<th>Is it used in New Zealand?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulator-based reforms</td>
<td>Regulators evaluate own performance.</td>
<td>Limited to aspects of administration and enforcement over which regulators have discretion.</td>
<td>Yes</td>
</tr>
<tr>
<td>Stock-flow linkage rules</td>
<td>Introduction of new regulation conditional on an assessment of, and changes to, the stock (examples are regulatory budgets, and the “one-in, one-out” rule).</td>
<td>Can force prioritisation and prompt government to be more pro-active in seeking out regulation for simplification and elimination. Risks are that it may encourage hoarding of regulations as “bargaining coin” and focus attention on removing rather than improving regulation.</td>
<td>No</td>
</tr>
<tr>
<td>Red tape reduction targets</td>
<td>Targets that focus on reducing paperwork or administrative compliance costs.</td>
<td>Need independent quantification of the savings achieved. Require implementation of a framework (such as the Standard Cost Model) and can be costly to implement. Tends to ignore benefits of regulation.</td>
<td>No general target</td>
</tr>
<tr>
<td>Sunsetting</td>
<td>A process in which new regulations are given automatic expiration dates, unless re-made through normal rule-making processes. This ensures continuing review and updating of stock of regulations. Another (weaker) form of sunsetting is “review clauses”, which are requirements in regulations for a review to be conducted within a certain period.</td>
<td>Can help with removing redundant regulation, but will not achieve more broad-based improvement unless related regulations sunset at the same time. Is not discerning, as it can require review of regulations that are working well.</td>
<td>No general requirement</td>
</tr>
<tr>
<td>Embedded review requirements in new legislation</td>
<td>Australia, Canada and the United States have recently established requirements in their regulatory systems to undertake ex post evaluations of significant regulations.</td>
<td>Need a process for focusing reviews on priority areas and monitoring that required reviews have been carried out, with adequate quality.</td>
<td>No general requirement</td>
</tr>
<tr>
<td>Public stocktakes</td>
<td>Used as a discovery mechanism for unnecessary regulatory burdens.</td>
<td>Most effective when there is wide engagement. Should not be undertaken too frequently.</td>
<td>No</td>
</tr>
<tr>
<td>Principles-based reviews</td>
<td>Involves assessing regulation and legislation against a principle (for example, that anti-competitive restrictions should only be retained when they demonstrate a net benefit).</td>
<td>More resource-intensive than general stocktakes, but can be influential.</td>
<td>No</td>
</tr>
<tr>
<td>Approach</td>
<td>Description</td>
<td>Comment</td>
<td>Is it used in New Zealand?</td>
</tr>
<tr>
<td>--------------------------</td>
<td>-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
<td>---------------------------</td>
</tr>
<tr>
<td>Benchmarking</td>
<td>Provides information on comparative performance and leading practices (the World Bank’s <em>Doing Business</em> reports, the OECD’s indexes of regulatory restrictions on trade and investment, and Australian Productivity Commission benchmarking studies are examples).</td>
<td>Can identify leading practices, although the complex nature of the regulations means that comparisons are often qualitative.</td>
<td>No</td>
</tr>
<tr>
<td>Formal large-scale reviews</td>
<td>Generally commissioned when a case for reforming a major area has been identified, and there is a need to explore options.</td>
<td>Most important requirement is transparency, through publication of submissions, public hearings and publication of a draft report with preliminary findings and recommendations.</td>
<td>Yes</td>
</tr>
</tbody>
</table>

**Cost effectiveness of the different approaches**

Figure 15.1 reports an assessment by the Australian Productivity Commission (APC) of the cost-effectiveness of the different approaches (considered from the perspective of the Australian Government). The APC argues that the high-effort, low-return quadrant (major red tape costing exercises, regulatory budgets and stocktakes that are too frequent) should normally be avoided. The approaches in the low-effort, low-return quadrant may be warranted (and indeed “business as usual”), but it is important to ensure that the effort is proportionate to the return. The low-effort, high-return quadrant is most attractive. This leaves the high-effort, high-return quadrant, which the APC argues is where prioritisation of activities is most important.

**Figure 15.1  Approaches to managing and reviewing the stock of regulation: an effort-impact matrix (for individual areas of regulation)**

<table>
<thead>
<tr>
<th>Potentially low return</th>
<th>Potentially high return</th>
</tr>
</thead>
<tbody>
<tr>
<td>High effort</td>
<td></td>
</tr>
<tr>
<td>Broad red tape cost estimation</td>
<td>In-depth reviews</td>
</tr>
<tr>
<td>Regulatory budgets and one-in-one-out¹</td>
<td>Embedded statutory reviews</td>
</tr>
<tr>
<td>Frequent stocktakes</td>
<td>Benchmarking</td>
</tr>
<tr>
<td></td>
<td>Packaged sunset reviews</td>
</tr>
<tr>
<td>Low effort</td>
<td></td>
</tr>
<tr>
<td>Sunsetting</td>
<td>Known high cost areas and known solutions from past reviews</td>
</tr>
<tr>
<td>Regulator stock management</td>
<td>Regulator management strategies where weak in the past</td>
</tr>
<tr>
<td>Red tape targets²</td>
<td>Periodic stocktakes</td>
</tr>
<tr>
<td>RIS stock-flow link</td>
<td></td>
</tr>
</tbody>
</table>

**Source:** APC, 2011b, p. 90.

**Notes:**
1. High effort to do well and potential for perverse impacts.
2. Where the awareness of compliance burdens is still lacking can be high return.
15.4 Approaches to evaluating regulation in New Zealand

The approach to a “stock management system” is evolving

The Government recognises that the processes for evaluating the performance of existing regulations need to be improved:

- We have begun to put in place systems which require departments to better plan for proposals for regulatory change and to scan their regulatory stock for areas that require review, or are redundant; but we still do not have strong management expectations and systems to support and give us assurance about the ongoing operation of existing regulation. We tend to have a “set and forget” mindset to regulation....

- We have begun to make improvements in our regulatory management systems, but our departments still do not, in general, systematically apply basic good management principles and practices to the regulatory regimes that they administer. This is a clear and longstanding gap in our state sector arrangements. (Offices of the Ministers of Finance & Regulatory Reform, 2013b, pp. 3-5)

Since the New Zealand Treasury took over responsibility for regulatory management oversight in 2008, it has begun to build a stock management system, made up of initiatives including:

- best practice regulation assessments of key regulatory regimes: the Treasury has developed best practice regulation principles and its assessment of 56 regimes (New Zealand Treasury, 2012a, p. 1) against them has suggested that growth impact and regulator capability are the aspects of regimes requiring most focus (Offices of the Ministers of Finance & Regulatory Reform, 2013a, annex);

- ongoing regulatory scanning of existing legislative instruments, to identify where there are performance issues in the regulatory stock (Offices of the Ministers of Finance & Regulatory Reform, 2013b, p. 2): the initial scan undertaken in 2010 revealed that a number of departments were not aware of the actual regulations for which they were responsible and few had actively monitored the operation of the legislation (Gill & Frankel, 2013, p. 19);

- annual regulatory plans of expected new regulation, or reviews of existing regulation; and

- a Regulatory Review Programme, being driven by eight agencies (Department of Internal Affairs, Inland Revenue Department, MBIE, Ministries for the Environment and Primary Industries, and Ministries of Health, Justice, and Transport. Seventeen reviews have been completed.

In a related policy development, Cabinet has also placed the onus on departments to keep up to date the regulatory regimes for which they are responsible. Departments are expected, for example, to:

- monitor, and thoroughly assess at appropriate intervals, the performance and condition of their regulatory regimes to ensure they are, and will remain, fit–for-purpose;

- be able to clearly articulate what those regimes are trying to achieve, what types of costs and other impacts they may impose, and what factors pose the greatest risks to good regulatory performance;

- have processes to use this information to identify and evaluate, and where appropriate report or act on, problems, vulnerabilities and opportunities for improvement in the design and operation of those regimes; and

- maintain an up-to-date database of the legislative instruments they have policy responsibility for, with oversight roles clearly assigned within the department (New Zealand Treasury, 2013c, p. 6).

Treasury guidance advises departments about the information they will be required to provide in their yearly regulatory system report, about how they are meeting these expectations. The Government expects to develop more specific expectations over time. However, it recognises that it will take some time for departments to develop the revised capabilities, frameworks and information systems needed to develop a “more systematic, comprehensive life-cycle approach to the management of existing regulation” (Offices of the Ministers of Finance & Regulatory Reform, 2013b, para 15).
The Government is also implementing other initiatives that are intended to lift performance, and which may encourage more focus on evaluation, including:

- upgrading and expanding the regulatory component of the Performance Improvement Framework;
- the Better Public Services reform agenda – particularly a greater results focus and changes to performance reporting requirements – which opens up an opportunity to integrate regulatory management frameworks and processes within wider state sector management thinking and practice;
- changes to the State Sector Act 1988 recognise that chief executives have explicit stewardship responsibilities that include the legislation that their departments administer; and
- the Business Facing Services cluster (Better Public Services Result), which provides the opportunity to better inform and engage New Zealand businesses in the development, implementation, administration, enforcement, monitoring and review of regulatory requirements that significantly impact on business (Offices of the Ministers of Finance & Regulatory Reform, 2013b, para. 17).

It is too early to assess the effectiveness of this large number of initiatives. However, a recent survey concludes that there is no systematic and well-defined process to learn about regulation through monitoring, review and evaluation, and describes the approach as “at best a patchwork” (Gill & Frankel, 2013, p. 1). In addition, while there are a plethora of potential reviewers in New Zealand, some significant gaps remain.

Other than ad hoc reviews, and the role of researchers in analysing reviews and writing articles, there are few mechanisms to learn about the effectiveness of regulations in contributing to achieving near term impacts and final goals. Unlike comparable Westminster jurisdictions, there is no requirement for programmed reviews of existing regulations nor has there been a concerted effort to increase the supply of evaluative evidence to enable more evidence based policy decisions. … the formal requirements for review of existing regulations are limited relative to other comparable jurisdictions and underdeveloped relative to the provisions applying to new regulations. (Gill & Frankel, 2013, pp. 24-25)

The New Zealand Government is implementing a suite of initiatives to improve the management of the stock of legislation and regulation. It does not use many of the approaches to system-wide evaluation of regulatory regimes that are used in other countries, some of which have been identified as involving low effort and potentially low/high return in those countries.

Other options have been considered as well

Other initiatives have been considered or are still being considered.

- MBIE’s submission suggests that statements of intent for regulatory systems could be explored. These statements would set out the outcomes or objectives of the systems and the contributions that different parties are expected to make to these objectives (sub. 52, p. 6).
- MBIE has also identified a “regulatory systems programme”, aimed at establishing whether the regulatory systems it has identified are performing well. It considers that mandatory statutory reviews can become “pro forma”, but invited the Productivity Commission to consider ways to mitigate this risk.
- MBIE also suggests that there would be particular value in the Productivity Commission providing guidance on “how Ministers, agencies and Crown entities can systematically 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” (sub. 52, p. 9).
- The Treasury, in a RIS prepared in 2011, outlined a package of proposals, including investigating a substantive new review role for an Officer of Parliament, which would “provide the House with the sort of expert, independent oversight on legislation that the Auditor-General provides on government
spending” (New Zealand Treasury, 2011b, p. 26). Alternatively, rather than setting up a new Officer of Parliament, the mandates of existing Officers of Parliament, such as the Auditor-General, could be revised to include more regular investigation and reporting to Parliament on the regulatory questions (Gill & Frankel, 2013, p. 33).

- Cabinet has agreed to legislative disclosure requirements, which will place additional obligations on departments proposing new legislation. An early discussion paper suggested that the disclosure statement for delegated legislation should disclose when this legislation will be formally reviewed, or is expected to warrant review, to ensure it is still needed and remains fit-for-purpose (New Zealand Treasury, 2012b, p. 31). It also proposed that the Minister responsible for the enacted bill should commission an independent review of the performance of existing executive government processes and requirements intended to support the development and maintenance of high-quality, fit-for-purpose legislation (New Zealand Treasury, 2012b, p. 32). These proposals have, however, been omitted from the subsequently released technical guide for departments (New Zealand Treasury, 2013a).

**And there are many other possible options**

While Figure 15.1 was derived by the APC using Australian costs that might not be the same in New Zealand, it does still suggest options that might be worth exploring, including:

- sunsetting;
- a stocktake of existing regulation;
- embedding ex post review requirements in new legislation;
- requiring any RIS to consider related regulations; and
- requiring any RIS to set out an evaluation strategy.

### 15.5 Improving how the stock of regulation is managed

The Government is in the early stages of implementing a diverse agenda for evaluating the stock of regulation. Cabinet’s expectations require departments to devote more attention to this issue, and the Treasury is performing a key role by developing initiatives in a stock management system. Most initiatives are recent, and it is too early to tell whether they will be effective.

The previous section showed that there are many other potentially useful options. The challenge for the Treasury, as the main advisor to the Government on this issue, is to monitor the performance of approaches in other jurisdictions and to assess their relevance to New Zealand, but without losing focus on the effective implementation of the already broad domestic agenda. The Commission considers that a number of refinements to the current approach could improve how the stock of regulation is managed.

**Improve the articulation of the overarching strategy**

The large number of initiatives for improving how the stock of regulation is managed has been set out in a series of information releases. For example, recent Cabinet papers provide an update on the current state of knowledge of regulatory design and implementation in New Zealand and proposed new initiatives to continue to improve New Zealand’s regulatory environment and performance (Offices of the Ministers of Finance & Regulatory Reform 2013a; 2013b). These papers, and a series of other Cabinet papers and minutes available on the Treasury’s website, are informative and useful, but are not pitched at a general readership.

Given the large number of initiatives, it may be timely for the Government to provide a more accessible overarching paper that articulates the overall objective of the strategy that the Government is implementing, explains how the initiatives work together to achieve this objective, identifies the resources that will be deployed to implement the strategy, and explains how its success will be measured and will benefit the community. The main audience for this paper may well be within the public sector, as it could provide a useful way of articulating the “big picture” within which the Government is expecting the public
sector to implement the various initiatives. It would also, however, be of use to sections of the business and wider community and would help to build their support for the policy.

The next chapter will argue that the Minister responsible for the regulatory management system overall should publish a strategy report that sets out Government’s medium-term objectives for the system, its strategic prioritisation of effort for achieving these objectives, and its work programme. The Minister should report regularly on progress towards delivering this work programme, and update the statement as necessary. The proposed strategy on how to manage the stock of regulation could be published as part of the broader strategy report for the overall system.

R15.1 The Government should publish an overarching strategy that sets out how it will improve the management of the stock of regulation. The strategy should explain how specific initiatives fit within it, and should describe how successful implementation of the strategy will be measured and how it will benefit the community.

**Strengthen incentives for departments to perform in line with Cabinet expectations**

**Clarify roles and responsibilities**

A theme throughout the report has been that having clearly defined roles and responsibilities is a prerequisite for getting things done. This is no less important in relation to managing the stock of regulation:

The first and crucial step to improving the contribution of monitoring, evaluation and review to regulatory effectiveness is to establish a much clearer statement of the roles and responsibilities of departments administering legislation and regulation. This would be analogous to [departments] role in the maintenance and care of physical assets on the agency’s balance sheet or the assets that they are administering on behalf of the Crown. … Without this role clarity other areas, where standards and expectations are clearer, will continue to gain resources and attention. (Gill & Frankel, 2013, p. 30)

To this point, Cabinet has set out in broad terms its expectations of what departments will do. It has indicated, however, that these expectations will become more precise over time. These more precise obligations must be supported by clarity about which agencies are responsible for delivering them, so as to increase accountability for delivering improved performance.

**Performance reporting**

As noted above, the Treasury is collecting information about the performance of departments in meeting Cabinet’s expectations for the Regulatory Systems Report. While the quality of this information will improve as Cabinet’s expectations become more precise, even now the Report’s impact on strengthening the motivation of departments would increase if it were published. Linking performance outcomes with chief executive performance agreements, as suggested in Chapter 14, would further increase the priority that departments attach to managing the stock of regulation.

R15.2 The performance of departments, in satisfying Cabinet’s expectations that they keep current the regulatory regimes they are responsible for, should be strengthened by:

- the Treasury publishing the findings from the Regulatory System Report about departmental stewardship activities;
- the State Services Commission (SSC) developing explicit measures for regulatory performance in chief executive performance agreements and annual expectations letters; and
- the SSC using both the Performance Improvement Framework and Treasury surveillance information about departmental regulatory performance in reviewing how chief executives perform.
Scrutiny by Parliament

Some commentators have suggested that the role of Parliament in scrutinising the stock of regulation could be sharpened, to encourage the Executive to take more interest in this issue. Ways that Parliament could be more involved include:

- as noted above, revising the mandates of existing Officers of Parliament, such as the Auditor-General, to include more regular investigation and reporting to Parliament on regulatory questions;

- strengthening the mandate, resourcing and accountability of the Regulations Review Committee of Parliament to encourage a more structured and thorough regulatory review process (Mortlock Consultants, sub. 31, pp. 9-10); and

- establishing an Office of Regulatory Assessment and Review, funded partly by government and partly by industry levy, and requiring it to conduct reviews of regulations (drawing on appointed experts as necessary) and to report to its own minister on the results of these reviews, with a robust level of transparency and accountability in relation to these reviews (Mortlock Consultants, sub. 31, pp. 9-10).

The Commission would welcome comment on options such as these.

Q15.1 What would be the advantages and disadvantages of increasing the role of Parliament in scrutinising how the stock of regulation is managed? If Parliament’s role should increase, what approach should be used to achieve it?

Embedding requirements for evaluation

An additional inducement for departments to implement processes to keep their regulatory regimes current would be to embed in new legislation a requirement to review it, as applies in Australia and Canada. Gill and Frankel (2013, p. 32) suggest that requirements for plans for monitoring, evaluation and review could be required as part of the papers for the Cabinet Legislation Committee and included along with the RIS that normally accompanies the introduction of legislation. Importantly, given that evaluations can be expensive to undertake, they consider that any requirements would need to be proportional to the significance of the regulation.

The Commission considers that an approach along these lines would be useful, and suggests that departments should outline evaluation timeframes and approaches in their Cabinet Legislation Committee papers, and Cabinet Office should amend the Cabinet Guide to make this expectation clear.

R15.3 Departments should explain their plans for monitoring, evaluation and review in their papers for the Cabinet Legislation Committee seeking agreement to introduce new legislation. The Treasury should amend the “Disclosure requirements for government legislation” to make this expectation clear. Departments’ plans should be proportional to the significance of the regulation.

Applying some principles to guide implementation

The immediate challenge that the Government faces is to rationalise and re-energise the current agenda that includes a large and diverse set of initiatives, while remaining aware of good practices elsewhere. Implementation is likely to be more effective if guided by some fundamental principles that do not appear to being universally applied at the moment. Such principles include proportionality, transparency, accountability, consultation, prioritisation and capability.

Proportionality

The scale and scope of evaluation exercises should be proportionate to the impacts of the regulation being reviewed, with more extensive evaluation of regulations with large costs and impacts, in areas where technology, community attitudes and regulations are changing rapidly. As noted above, some 56 best
practice reviews and 17 other reviews have been conducted, but it is not clear whether the effort devoted to each has been proportionate to the significance of the issue at hand.

**Transparency**

One theme running through Recommendations 15.1, 15.2 and 15.3 is that there should be transparent reporting of the Government’s strategy, work programme and progress in achieving performance targets. While there is internal reporting with government on aspects of regulatory performance (Cabinet Office 2009a), these reports are not public. More transparent public reporting would add more scrutiny of a department’s performance, and would encourage them to consider carefully how their management of the stock of legislation and regulation affects the community.

**Accountability**

As noted above, roles and responsibilities for managing the stock of regulation have not been clearly defined and, while the Cabinet has provided expectations of what it wants, there are no hard targets. Further, some of the reviews being undertaken seem to combine self-assessment and limited transparency. This may provide weak incentives for rigorous evaluation.

More precisely defined accountabilities would build confidence that there will be a jump up in the quality of how the stock of regulation is managed.

**Consultation**

The benefits of consultation have been explained in Chapter 8. These benefits are evident in *ex post* and *ex ante* evaluation, and help to ensure that any reviews reflect the perspectives of those who are regulated as well as the regulators.

Consultation outside government about the Government’s programme has been patchy. For example, two key Cabinet papers on initiatives to improve regulatory performance (Regulatory Systems papers one and two) only report on consultation that occurred within Government, without mentioning any consultation or engagement with the public. And the questions on evaluation and review in the Treasury Guidance for the Regulatory Systems Report (New Zealand Treasury, 2013c, p. 10) do not focus on how departments consult with the public about the impacts of legislation and regulation.

On the other hand, considerable public consultation has been undertaken during specific reviews (for example, the process leading to the vehicle licensing reforms).

Given that consultation can lead to more robust approaches to managing and improving the stock of regulation, it should be a key feature of the Government’s approach. (Chapter 8 examines effective consultation and engagement in more detail.)

**Prioritisation**

The stock of regulation is so large that it is important to focus evaluation where the payoff is expected to be largest. The Treasury (2013h) has “speculated” that New Zealand might have perhaps 200 core regulatory regimes, and that 100 of these “warrant regular monitoring/reporting and better periodic review/maintenance” (p. 16). With so many possible candidates for review, criteria for filtering them are needed. The Government used the following criteria to choose its regulatory review programme in 2009:

- regulations that are most in need of a review, based on the likely impact on productivity;
- election commitments;
- advice from officials; and
- feedback received from the public (Cabinet Office 2009b).

The following criteria, slightly amended from those that the Australian and New Zealand Commissions suggested in a recent inquiry into trans-Tasman economic relations, could be used to update the Government’s 2009 criteria and to target reviews where they would deliver the highest return on investment:
• width of reach (number of entities and/or value of activity affected);
• depth of reach (the extent to which entities are affected);
• information that the issue is critical for stakeholders; and
• any other information that a regulation is imposing large costs (APC & NZPC, 2012).

With such a large stock of regulation, and so many options for improving the way it is managed, it is important to continue using a process to focus review effort where it is most valuable:

**Capability**

As noted earlier, evaluating regulatory regimes is a skilled job. Given the focus on decentralising responsibility for reviews to portfolio agencies, these agencies will need staff with evaluation skills. The burden on these staff can be reduced by effective prioritisation of the evaluation agenda. However, even after this has happened, the workload is likely to be large. And given that the evaluation agenda has only recently been established, it is likely that skills in this area are not widespread. The Government has noted that capability in this area is limited, and may need to devote additional resources to improving it.

<table>
<thead>
<tr>
<th>R15.4</th>
<th>The Treasury should continue to monitor approaches to evaluation used in other countries, while implementing the current evaluation agenda, building an approach that:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• ensures that the scale and scope of evaluations is proportionate to the monetised impacts of regulation;</td>
<td></td>
</tr>
<tr>
<td>• provides transparent reporting of the Government’s strategy, work programme and progress in achieving performance targets;</td>
<td></td>
</tr>
<tr>
<td>• clearly defines responsibility for managing the stock of regulation;</td>
<td></td>
</tr>
<tr>
<td>• is based on consultation with those affected by regulation;</td>
<td></td>
</tr>
<tr>
<td>• is driven by a need to prioritise effort where the payoff is expected to be largest; and</td>
<td></td>
</tr>
<tr>
<td>• is adequately resourced, so that people with the capabilities to undertake effective evaluations can implement it.</td>
<td></td>
</tr>
</tbody>
</table>
16 Making it happen

Key points
- The regulatory management system is a large and important part of New Zealand’s policy infrastructure. This report has reviewed the components of the system and found system-wide deficiencies in each of them. New Zealand’s system cannot be described as broken, but it is “muddling through”. There is considerable scope to get more, and much better, performance from the system, with significant benefits for the New Zealand economy and the wellbeing of New Zealanders.
- To move the regulatory management system to the next level of performance requires, for example:
  - energetic and focused leadership from within the Cabinet;
  - re-focusing effort to improve the system from the front end of regulation (the decision-making process), towards organisational design, implementation, monitoring and review;
  - stronger encouragement and support for regulators to fulfil their stewardship obligations; and
  - better understanding by departmental monitors of regulators about the monitoring role, and increased importance attached to the monitoring role.
- The Commission is proposing 43 recommendations to improve the system. Implementing the recommendations would require a strategic and focused approach. This chapter provides suggestions about how these recommendations could be embedded in the system, by strengthening existing institutions and creating an environment in which the recommendations will have most effect.
- Having a Minister responsible for the regulatory management system is essential. The Minister’s responsibilities should include:
  - defining the overall objective of the regulatory management system and bringing focus and attention to it;
  - strategic prioritisation of effort across the regulatory system;
  - specifying and allocating tasks for improving the system; and
  - promoting continuous improvement in regulatory design and practice.
- Effective institutional support for the Minister is needed, and initiatives must be resourced adequately.
- Stronger and more focused mechanisms to encourage continuous improvement, not just a one-off lift in performance, should become permanent features of the regulatory management system.

16.1 Introduction
This report has demonstrated that New Zealand has a large and complex regulatory sector, comprising, according to the Treasury, possibly as many as 200 regulatory regimes (New Zealand Treasury, 2013h, p. 16). Regulation touches the lives of New Zealanders in many ways, even though most people would rarely give them a passing thought. Regulation also affects the costs and competitiveness of businesses and sometimes even their right to operate. As such, it goes to the core of personal rights and freedoms, social
cohesion, and business dynamics and efficiency. While there is surprisingly little information about the overall regulatory system and its effects (Chapter 3), the processes for introducing, implementing, enforcing and reviewing regulation are profoundly significant for the wellbeing of New Zealanders.

When people think about regulation, they tend to think about their interactions with a particular regulator or regulation. Yet, these are only components of a much larger system. An analogy may help to make this clearer. Most people would understand that there is an education “system”, even though they will only deal with a particular school. Yet behind that school is a system that determines or influences the national curriculum, school funding, qualification and training requirements for teachers, and so on.

The same applies to regulation. While most people interact with specific regulators or regulations, behind them sits a “regulatory management system” that determines or influences the processes that must be followed before a new regulation is introduced, the scope of regulators’ powers, requirements for consultation, whether and how regulations need reviewing to ensure that they remain fit-for-purpose, and so on.

This system is a key part of New Zealand’s policy infrastructure and should be seen, for example, as no less significant than the systems behind taxation and government spending. Regulation is one of the main instruments through which governments achieve social, environmental and economic objectives. However, regulation also imposes burdens that need to be controlled, and poor implementation can undermine its effectiveness in achieving outcomes and its credibility. This means that having a regulatory management system that encourages up-to-date focused regulation, is directed at genuine problems that only regulation can solve, is implemented well, and does not impose any unnecessary burdens, is one key way that governments can meet the aspirations of New Zealanders. Other countries have long recognised the importance of their regulatory management systems. For example, since the 1990s the Organisation for Economic Co-operation and Development (OECD) has been developing policy tools to capture the notion of quality in regulatory management (Jacobzone & Miguet, 2007).

New Zealand has introduced improvements to the regulatory management system. The introduction of the Regulatory Impact Assessment (RIA) process in the late 1990s is an important example. And there has been a subsequent strengthening of the process by successive governments. This work is, however, incomplete. Every chapter in this report has identified weaknesses in particular parts of the regulatory management system and has suggested ways to fix them. Table 16.1 demonstrates this, by providing a brief synopsis of the system-wide improvements outlined in each chapter.

To move the regulatory management system to the next level of performance:

- the Cabinet needs to show energetic and focused leadership, based on the premise that the regulatory management system is a key part of New Zealand’s policy infrastructure, combined with more transparent processes from both Ministers and agencies;
- more attention should be paid to organisational design, implementation, monitoring and review;
- regulators need stronger encouragement and support to fulfil their stewardship obligations – the system should rely less on goodwill and the sense of professional duty and more on exposing Boards and chief executives to performance expectations and incentives commensurate with the Government’s stated objectives;
- departmental monitors of regulators need a better understanding of their role, and the importance attached to the monitoring role needs to increase; and
- agencies with key roles in ensuring the system functions well must be funded adequately.

This report is largely pitched at the level of the regulatory management system, rather than at individual regulators or regulations. It looks at broader system-wide issues, rather than seeing how they play out for individual regulators, and provides guidance that will help in designing new regulatory regimes and in improving the operation of existing regulatory regimes.
The Commission is proposing 43 recommendations. Implementing them would require a strategic and focused approach. This chapter provides suggestions about how these recommendations could be...
embedded in New Zealand’s regulatory management system by strengthening existing institutions and creating an environment in which the recommendations will have most effect.

The following features would facilitate the implementation of recommendations and encourage continuous improvement:

- clear definition of roles and responsibilities, particularly of the minister responsible for stewardship of the regulatory management system (Section 16.2);
- effective institutions to support the minister (Section 16.3);
- adequate resourcing to support the implementation of initiatives to improve the system (Section 16.4);
- strengthened and more focused incentives to encourage the completion of tasks (Section 16.5); and
- building the necessary capabilities across the regulatory management system (Section 16.6).

### 16.2 Clear roles and responsibilities

A theme of the report has been that roles and responsibilities must be clearly defined. This applies equally to responsibility for the regulatory management system. Virtually every minister interacts with this system and most are responsible for some part of it. This begs the question of who is responsible for the overall system.

Table 16.2 illustrates why this is an important issue. It provides one example from each chapter of a task that, if undertaken, would strengthen the regulatory system as a whole. Unless there is a single point of accountability with a system wide-perspective, improvements that are designed to affect the system overall are unlikely to be implemented effectively. A portfolio minister who is responsible for a particular regulatory regime would not have the responsibility, authority, or system-wide perspective to ensure that such tasks are carried out. As the OECD suggests,

… governments should consider assigning a specific Minister with political responsibility for maintaining and improving the operation of the whole-of-government policy on regulatory quality and to provide leadership and oversight of the regulatory governance process. (OECD, 2012a, rec. 1.6)

In 2008, 24 OECD jurisdictions reported that their governments had assigned responsibility for promoting government-wide progress on regulatory reform to a specific minister (OECD, 2012a, p. 23). A single point of accountability – a minister with responsibility for the regulatory system – has significant advantages. This Minister would be required to take a whole-of-government approach to regulatory policy, rather than one that comes from a sectoral perspective, and a whole-of-system view of how to improve the system, rather than ad hoc improvements to current initiatives in part of the system.

### Table 16.2 Examples of system-wide tasks arising from report

<table>
<thead>
<tr>
<th>Chapter title</th>
<th>Example of a task to be allocated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Understanding the regulatory system</td>
<td>Oversee implementation of standardised reporting.</td>
</tr>
<tr>
<td>Role clarity</td>
<td>Ensure the Cabinet Manual and State Services Commission guidance are updated to reflect expectations for greater use of exposure drafts, and the obligation on new regulators to publish interpretations of their mandate.</td>
</tr>
<tr>
<td>Regulatory independence and institutional form</td>
<td>Identify mechanisms to ensure greater consistency in the allocation of material between primary legislation and other legislative instruments in government bills.</td>
</tr>
<tr>
<td>Governance, decision rights and discretion</td>
<td>Update guidance on the appointment of board members to Crown entities, and induction material for new board members.</td>
</tr>
</tbody>
</table>
Responsibilities of the minister

The Minister for Finance is currently responsible for managing the regulatory system. It is common internationally for this responsibility to be assigned to a senior minister.

Previously, the regulatory portfolio has been held by ministers outside Cabinet. However, assigning the responsibility to a senior Cabinet minister has significant advantages, as seniority provides:

- the ability to take a whole-of-government perspective;
- the capacity to maintain the Government’s focus on improving the system;
- the authority to ensure that initiatives are implemented; and
- access to the information required to develop and implement policy.

The specific responsibilities of the minister in regard to the regulatory management system have not been published. The Commission (drawing on Victorian Competition and Efficiency Commission (VCEC) 2011, Chapter 2, and OECD, 2012a) considers that there are four key responsibilities

Identifying an integrated policy for regulatory management

Chapter 4 pointed out that regulatory regimes with clear objectives are more likely to enjoy high levels of compliance and credibility, although achieving clarity is not straightforward. This also applies to the
regulatory management system overall. This is illustrated by the APEC-OECD integrated checklist on regulatory reform, which states that

… the point of departure is to ask whether a regulatory reform policy exists. Such a policy often takes the form of a statement setting out principles to govern regulatory reform which provides strong guidance and benchmarks for action by officials, and also sets out what the public can expect from government regarding regulation. (OECD, 2005, p.5)

The regulatory management system, as an overarching set of governance and institutional arrangements, does not, by itself, achieve the Government’s regulatory objectives. Rather, its role is to be an enabler of good performance by the regulatory regimes that operate within the system. The overall policy objective for the system could be expressed in different ways. The Commission sets out one possible approach below, which it puts forward as a starting point for discussion (Box 16.1):

**Box 16.1  Possible high-level regulatory management policy**

The Government seeks a regulatory management system that enables and encourages the effective and efficient operation of the regulatory regimes that operate within that system. The Government is seeking a system that is at all times fit for purpose for achieving the Government’s regulatory objectives without imposing an unnecessary regulatory burden. The system should be focused on continuous improvement and consistency with best practice principles of regulation.

**Strategic prioritisation of effort across the regulatory system**

With the primary objective of the regulatory management system defined, the minister’s second responsibility is to lead a process for establishing the strategic priorities for improving – when necessary – different components of the system. There needs to be periodic diagnosis of performance at the system level, followed by the development of strategy and the allocation of effort to achieve these priorities.

For example, it is common overseas for an *ex ante* evaluation of regulations through a Regulatory Impact Statement (RIS) to be given more attention than an *ex post* evaluation. This seems also to be the case in New Zealand. A major strategic choice for the Government is whether to allocate more resources to improving *ex post* evaluation, and indeed the Government is moving in this direction (Chapter 15). Examples of other broad priorities are focusing on reducing the compliance costs of regulation, or on developing the organisational capability of regulators.

Once major priorities have been determined, a detailed programme for implementing specific initiatives to deliver them should be developed and kept current. This is likely to be an iterative process that involves collecting extra evidence, monitoring the outcomes of initiatives, identifying barriers to progress and considering how to overcome them and, where necessary, finding a place for initiatives in the Government’s legislative programme. This will require a strong ongoing commitment from the minister with responsibility for regulatory management, with appropriate departmental support (see below).

**Task definition and allocation**

Many different institutions could be involved in delivering this large number of tasks, including portfolio Ministers, the Treasury, the State Services Commission (SSC), the Auditor-General, departments responsible for monitoring regulators or establishing regulatory regimes, regulators, and the Compliance Common Capability Programme (CCCP).

An important role for the minister would be to ensure that tasks the Government accepts are specified precisely and accountabilities for delivering them are allocated appropriately:

The assignment of specific responsibilities for aspects of reform and the creation of a framework for accountability are essential for the success of the programme. (OECD, 2005, p. 6)

A particularly important feature of assigning responsibilities is that there is clarity about the respective responsibilities of the minister responsible for regulatory management and the portfolio Ministers who are responsible for specific regulatory regimes. Often, portfolio Ministers are responsible for implementing
initiatives that are driven from the centre. Part of the role of the minister responsible for regulatory management is following up to ensure that allocated tasks have been completed. This task will only be feasible if the respective responsibilities of different ministers are clear, and if the minister responsible for the overall regulatory system holds a senior position in Cabinet.

Assigning responsibilities will likely be influenced by factors such as existing strengths, capabilities and resources; fit with existing functions; and ensuring that the independence of independent regulators is not compromised (VCEC, 2011, p.22).

Promoting regulatory policy
Ensuring the quality of the regulatory structure is a “dynamic and permanent role of governments and Parliaments” (OECD, 2012a). Maintaining support for improving systems, however, requires sustained effort. The recommendations in this report, if accepted, would take some years to implement. Indeed, system improvement never ends; it is a continuous process. Some changes may be opposed by those who feel they might be adversely affected. Other changes involve “machinery-of-government” issues, which usually have a low public profile. These issues can easily slip down the Government’s agenda, particularly when they are crowded out by episodes of perceived regulatory failure that create pressure for an immediate response, even if this is not consistent with the long-term direction of regulatory policy.

In this inhospitable environment, a key function of the minister responsible for regulatory management would be to identify opportunities for system-wide improvements and to be a champion for implementing them, while preventing this process of continuous improvement from being derailed by short-term responses to regulatory failures. The Minister will need to make this case to different audiences, including:

- Parliament;
- Ministerial colleagues, who have their own priorities that may seem more pressing;
- departments responsible for overseeing regulators;
- regulators;
- other institutions that can support continuous improvement of the system, such as the Auditor-General and the Regulations Review Committee; and
- those affected by regulation, who in practice are represented by industry associations or community groups.

The most effective approach to communication will vary between these audiences. However, a useful foundation document would be a statement that sets out the Government’s medium-term objective for the regulatory management system, its strategic priorities, and work programme. The Government’s 2009 Statement on Regulation: Better Regulation, Less Regulation, which has now been replaced, was an early example. It set out the Government’s two key commitments at a high level and set out how the Government intended to deliver on these commitments. This could provide a framework to build on when crafting a future statement on regulation. The approach in fiscal policy, where the government is required to publish a strategy report that sets out long-term objectives, short-term intentions towards meeting these objectives, and then reports regularly on its progress, provides another example.

An equivalent statement for regulation would promote continuous improvement by:

- becoming a vehicle for the Government to report on progress and issues not yet covered;
- motivating stakeholders to monitor progress and lobby the Government to complete the issues that remain;
- providing strategic direction for those who have been allocated tasks to improve the regulatory system; and
- becoming the basis for a living document that could be refreshed as circumstances change.
The Government should publish the responsibilities of the minister responsible for regulatory management. These responsibilities could include:

- defining the overall objective of the regulatory management system;
- prioritising effort across the regulatory system;
- specifying and allocating tasks for improving the system; and
- promoting regulatory policy and the case for continuous improvement in regulatory design and practice.

The minister with responsibility for regulatory management should publish a strategy report that sets out the medium-term objectives that the Government is seeking to achieve through the regulatory management system, its strategic prioritisation of effort for achieving these objectives, and its work programme. The Minister should report regularly on progress towards delivering this work programme, and update the statement as necessary.

### 16.3 Effective institutions to support the minister and the functioning of the system

The minister responsible for regulatory management needs departmental support to carry out the roles identified above. Table 16.3 identifies nine functions that are involved in providing this support.

<table>
<thead>
<tr>
<th>Functions</th>
<th>Who currently does this?</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Stocktake and evaluation of the state of the regulatory management system.</td>
<td>Treasury</td>
</tr>
<tr>
<td>2. Advice on medium-term strategic objectives for the regulatory system.</td>
<td>Treasury</td>
</tr>
<tr>
<td>3. Provision of support and expertise to other agencies on regulatory design, when required.</td>
<td>-</td>
</tr>
<tr>
<td>4. Advice on priorities for regime review, and monitoring of progress on previously-agreed reviews.</td>
<td>Treasury</td>
</tr>
<tr>
<td>5. Advice/thought leadership on regulatory practice.</td>
<td>CCCP (informally)</td>
</tr>
<tr>
<td>6. Assessments of the adequacy of the monitoring of departmental regulators.</td>
<td>PIF reviews are beginning to do this</td>
</tr>
<tr>
<td>7. Analysis of standardised performance data from regulators, and advice on implications.</td>
<td>-</td>
</tr>
<tr>
<td>8. Advice on the current state and needs of the regulatory workforce.</td>
<td>CCCP (informally)</td>
</tr>
</tbody>
</table>
### Functions and Who Currently Does This?

<table>
<thead>
<tr>
<th>Functions</th>
<th>Who Currently Does This</th>
</tr>
</thead>
<tbody>
<tr>
<td>9. Assessment of the quality of significant proposals for new regulation, and oversight of the internal quality assessment processes that departments use.</td>
<td>Treasury</td>
</tr>
</tbody>
</table>

This table suggests that the arrangements for two functions are informal and that no agency is currently formally responsible for:

- providing technical assistance or expert advice to departments developing new regimes (Function 3);
- assessing the adequacy of the monitoring of departmental regulators (Function 6); and
- analysing standardised performance data from regulators, and providing advice about its implications (Function 7).

**Q16.1 Are there other functions for which a minister responsible for regulatory management would need support?**

Responsibility for the functions in Table 16.3 should be assigned. There are some synergies between them. For example, a department that builds up their understanding of regulatory best practice would gain insights into the requirements of the regulatory workforce. This suggests a benefit in co-locating some of the functions.

In 2008 almost all OECD countries had a specialised regulatory oversight body, undertaking at least some of the functions identified in Table 16.3. However, there are different views about where these functions should be located within government (Box 16.2).

**Box 16.2 OECD insights about the location of regulatory management functions**

**OECD 2010**

Many countries have difficulty determining the best location for a central unit, if they are trying to establish one. Possible locations which have been tested include the centre of government (prime minister’s office or equivalent), enterprise ministry, finance ministry, justice ministry, and home affairs ministry. This is very country specific, reflecting traditions and the relative weight given, for example, to the economic or legal context for regulatory policy. In countries with a long regulatory management tradition, location may vary over time (for example between the centre of government and the enterprise ministry).

The differences also reveal a more fundamental issue: regulatory management affects a wide range of ministries and does not have an automatic “home” (as does, for example, fiscal policy). One or two countries have set up units made up of secondees from key ministries. This appears to be a very promising approach. There are advantages and disadvantages to a single location. For example, centres of government are often reluctant to take on substantive tasks that may compromise their key function of arbitration and strategic management; finance ministries may be too engaged in other parts of their portfolio to pay enough attention to regulatory management (although they are important because of their power); and enterprise ministries are closer to their clients than to centres of government, but may lack authority over other ministries. (pp. 70-71)

**OECD 2011**

The OECD cite Cordova-Novion and Jacobzone (2011), who analyse the key factors contributing to success of regulatory oversight, including the mandate, powers, structure, location, resources and coordination mechanisms. The findings are set out below.

- Oversight bodies are generally located close to core executive functions: either at the centre of government itself, or as part of central ministries. Despite significant institutional heterogeneity, a key issue for success is the existence of a structured unit or dedicated secretariat. It can be set up within the executive, or as a council/committee as part of an arms'
Table 16.4 presents five possible options for New Zealand and summarises their advantages and disadvantages. Possible locations for a support agency for the minister with responsibility for regulatory management include the Treasury, the Ministry of Business, Innovation and Employment (MBIE), the State Services Commission (SSC), or a new independent agency.

Alternatively, a networked approach could be taken, with the Treasury having the key oversight role, but with the SSC being assigned responsibility for parts of it. The participation of the SSC would reflect its statutory role to “promote strategies and practices concerning government workforce capacity and capability” (relevant to Function 8 in table 16.3) and to provide advice about “the allocation and transfer of functions and powers … and the establishment, amalgamation, and disestablishment of agencies” (relevant to Function 3 in table 16.3). And, as discussed in Chapter 14, the State Services Commissioner has a number of wider roles, which strongly suggests it should be an active participant in the regulatory management system.

However, as discussed in Chapter 14, it is clear from material collected from both inquiry participants and external parties that the SSC is not currently playing a major role in regulatory affairs.

Table 16.4 Possible locations of a support agency for the minister with responsibility for regulatory management

<table>
<thead>
<tr>
<th>Possible location</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
</table>
| The Treasury     | • Already plays a role in regulatory management.  
                  | • Can take economy-wide perspective. | • Many competing priorities could mean that regulation struggles for attention.  
                  |                                       | • Does not have expertise in some regulatory hot spots (such as workforce capability). |
| MBIE             | • Department oversees many regulators.  
<pre><code>              | • Well placed to understand industry’s needs. | • May not take a community-wide perspective. |
</code></pre>
<p>| SSC              | • Has expertise in relation to governance and capability. | • Does not have expertise in other regulatory issues. |</p>
<table>
<thead>
<tr>
<th>Possible location</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent agency</td>
<td>• New agency could provide sharper focus and be more open to innovation.</td>
<td>• Additional cost.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• If independent, capacity to advise minister is not clear.</td>
</tr>
<tr>
<td>Networked approach</td>
<td>• Combines the knowledge and skills of different agencies.</td>
<td>• Can lead to accountability problems unless roles and responsibilities are specified precisely.</td>
</tr>
</tbody>
</table>

The Commission intends to discuss options for improving the advice provided to the minister responsible for regulatory management in more detail in the final report.

16.4 Adequate resourcing

In addition to the additional costs of a potentially larger regulatory oversight agency, there would also be costs involved in implementing particular recommendations. Some indication of the size of these costs is given by two RISs prepared by the Treasury’s Regulatory Quality Team (New Zealand Treasury, 2011b; 2013h), which assessed packages of options for encouraging better quality regulation. These packages included options such as increased disclosure, guidance and support to departments from the Parliamentary Counsel Office and Treasury, tighter RIA requirements, enhanced roles for Select Committees, enhanced reporting requirements, and investigating the possibility of a new Office of Parliament to review the performance of existing regulatory regimes. As there is considerable difference between the scope of the packages, their estimated costs vary widely – between $0.85 million and $15 million a year. (At the upper end, about $5 million of the $15 million package would be spent creating a new Office of Parliament.)

Some of the options in these packages overlap with suggestions made in this report. The Commission has not yet quantified the costs of its recommendations. Without adequate resourcing, implementation is unlikely to be effective. The Commission intends to provide more information about the cost of its recommendations in the final report.

16.5 Strengthening and aligning incentives with regulatory objectives

How well initiatives are implemented will be influenced by the strength of the motivations of those who are accountable for implementing them. The possibility that a change will lead to better outcomes provides some motivation for implementation. However, the report has identified other ways to motivate those operating within the regulatory management system. Table 16.5 groups them into five broad categories and lists the recommendations that fit within each category.

Importantly, the Commission is proposing that these mechanisms would become permanent features of the regulatory management system. This means that they would encourage continuous improvement, not just a one-off lift in the system’s performance.

The Commission’s proposals would place some extra burdens on external reviewers (such as the Office of the Auditor-General and the Regulations Review Committee of Parliament), and on the SSC. However, the
Commission considers that these organisations will be an important part of any plan to improve how the regulatory management system operates.

### Table 16.5  Mechanisms for motivating change

<table>
<thead>
<tr>
<th>Type of incentive</th>
<th>Examples</th>
<th>Comment</th>
<th>Relevant recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expectations</td>
<td>Expectations that departments will review the stock of legislation or comply with cost recovery guidelines.</td>
<td>Can be a powerful incentive if expectations come from an authoritative source (such as the Cabinet.) But may be weakened if there is no follow up for non-performance.</td>
<td>15.2</td>
</tr>
<tr>
<td>Legislative requirement</td>
<td>Legal requirement to review the operation of legislation/regulation.</td>
<td>Non-compliance can have serious consequences. May not be appropriate when flexibility is needed.</td>
<td>15.3</td>
</tr>
<tr>
<td>Professional</td>
<td>Linking executive agreements to achieving Cabinet expectations about regulation review.</td>
<td>Effectiveness depends on having the capacity to specify clear performance measures, and on avoiding too many obligations.</td>
<td>14.2, 15.2</td>
</tr>
<tr>
<td>Transparency</td>
<td>Improved performance reporting. Regular presentation of a progress report by the minister responsible for regulatory management.</td>
<td>Can be very powerful, when people can be held accountable for achieving clearly-defined performance measures.</td>
<td>13.4</td>
</tr>
<tr>
<td>External review</td>
<td>Widening the grounds on which the Regulations Review Committee can disallow a regulation.</td>
<td>Provides an independent perspective, but would require new expertise.</td>
<td>12.6, 13.3, 13.5</td>
</tr>
</tbody>
</table>

### 16.6 Building up capabilities

The report has identified the contribution of organisational capability (Chapter 12), workforce capability (Chapter 13) and organisational culture (Chapter 7) to the effective administration and enforcement of regulation. It has also pointed to a shift in emphasis towards the evaluation of how well regulation is working (Chapter 15). This shift will not be successful unless there are people with the skills to undertake evaluation. Capabilities will also need to be developed in relation to the design of regulatory systems in departments:

Building and maintaining capacity must be seen as a crucial element for a successful regulatory management system. (OECD, 2005, p. 10)

One of the responsibilities of the minister responsible for regulatory management would be to ensure that system-wide initiatives to improve the regulatory management system are backed up by developing necessary skills across the regulatory system.

### 16.7 Conclusion

The regulatory management system is a large and important part of New Zealand’s policy infrastructure. This report has reviewed the components of the system and has found system-wide deficiencies in each of them. New Zealand’s system cannot be described as broken, but it is “muddling through”. There is
considerable scope to get more, and much better, performance out of the system, with significant benefits for the wellbeing of New Zealanders.

The approach suggested in this chapter would concentrate attention on the role and contribution of the system to the wellbeing of New Zealanders and encourage a more strategic approach to initiatives aimed at improving it. It would:

- sharpen the accountabilities of those who have important roles to perform in improving the system;
- redirect effort to improve the system to where it can yield the highest dividends;
- increase the attention devoted to improving organisational and workforce capability; and
- build in mechanisms to encourage continuous improvement of the system, to keep it current.

New Zealand is not so well off that it can afford to settle for second best in its foundational systems. Indeed, given the disadvantages of small scale and isolation, New Zealand needs to excel in such matters if it is to meet its aspiration to deliver first-class living standards to all New Zealanders. Achieving this will require focus, enthusiasm, capability and strong political support.
Summary of questions

Chapter 3 – Understanding the regulatory system

Q3.1 Are there other or different elements of regulator design, practice or impact that should be reported upon?

Q3.2 Are there factors that would make the benefits of reporting at a regime level, rather than an agency level, outweigh the costs of doing so?

Chapter 5 – Regulatory independence and institutional form

Q5.1 How can the role of the Regulations Review Committee be strengthened, if regulators are delegated greater regulation-making powers?

Chapter 7 – Regulator culture and leadership

Q7.1 What factors are contributing to poor communication within regulatory bodies? Are these factors cultural or procedural in nature? What actions or approaches could be put in place to reduce barriers to internal communication?

Chapter 8 – Consultation and engagement

Q8.1 Are there any examples of legislative rigidity that may prevent regulators from using participatory processes and/or making decisions that would benefit both consumers and regulated parties? What evidence is there of this? What lessons could be learnt from these examples?

Q8.2 Are there examples of consultation provisions that are working well, or alternatively, not as well as they should? What factors contribute to a consultation provisions working well/poorly?

Chapter 9 – The Treaty of Waitangi in regulatory design and practice

Q9.1 Would an overarching Treaty clause in an appropriate statute (separate from the jurisdiction the Treaty of Waitangi Act 1975 confers on the Waitangi Tribunal to investigate actions inconsistent with Treaty principles), that signals the Crown’s intent with respect to the principles of the Treaty of Waitangi, improve the operation of regulatory regimes in New Zealand?

Chapter 10 – Decision review

Q10.1 What evidence exists for the effectiveness of internal review of regulatory decisions?

Q10.2 How effective are the Legislation Advisory Committee’s guidelines on appeal and review in influencing policy-makers in the design of new regulatory regimes?
Q10.3 Is there a need for greater specialisation among the judiciary to hear cases relating to complex areas of regulation? What approaches might be effective to develop greater expertise among the judiciary in these areas?

Q10.4 What benefits and risks are there in providing for alternative dispute resolution mechanisms as a way of reviewing regulatory decisions?

Chapter 11 – Regulator practice

Q11.1 Do recent developments in the theoretical literature, suggesting that in designing and implementing regulatory regimes, there needs to be a focus on:

- the behaviour, attitudes and cultures of regulatory actors, including those of the regulator;
- the dynamics of the regulated environment in which regulated parties and regulator operate, and the institutional setting of the regulatory regime;
- the logics of the regulatory tools and strategies used;
- the performance of the regime over time, and
- changes in each of the above factors;

offer a way forward for improving both the design and operation of New Zealand’s regulatory regimes?

Chapter 13 – Funding regulators

Q13.1 Are there clear and legally accepted definitions of fees and levies in New Zealand? If not, does this matter? Are there issues that are specific to either fees or levies that the Commission needs to consider?

Q13.2 Would there be net benefits from imposing a general obligation on regulatory agencies to consult before fees or levies are introduced or amended?

Q13.3 Do surpluses and deficits on memorandum accounts signify a problem? If so, are there worthwhile options to address the problem?

Chapter 14 – Accountability and performance monitoring

Q14.1 Are there other questions or characteristics that a monitoring approach for Crown entity regulators should include?

Chapter 15 – System-wide regulatory review

Q15.1 What would be the advantages and disadvantages of increasing the role of Parliament in scrutinising how the stock of regulation is managed? If Parliament’s role should increase, what approach should be used to achieve it?
Chapter 16 – Making it happen

Q16.1 Are there other functions for which a minister responsible for regulatory management would need support?

Q16.2 Which is the best location for a support agency for a minister with responsibility for the regulatory management system?
## Findings and recommendations

The full set of findings and recommendations from the report are below.

### Chapter 3 – Understanding the regulatory system

#### Findings

| F3.1 | Maps and groupings are valuable as a way to understand regulatory regimes and agencies, but mainly as a first step in a more detailed analysis. For most regimes, further disaggregation is likely to be needed to gain a full understanding of their dynamics, relationships and differences. |
| F3.2 | No single set of categories will support all avenues of analysis into how regulatory regimes perform. A range of frameworks can be applied that answer different questions and lead to different combinations of agencies and regimes. |
| F3.3 | The lack of regular and detailed reporting on the state of New Zealand regulators and regulation is a key gap in the current regulatory management system. The lack of data on regulatory activity compares poorly with fiscal management processes. Those processes promote informed and focused public debate on fiscal policy, encourage governments to focus their actions, and enable comparisons between different areas of the public sector. |
| F3.4 | More comprehensive and comparable information should be collected on the activities and impacts of New Zealand regulators. Such information could help offset barriers to identifying and making systemic improvements to regulatory practice. In particular, it could:  
- help designers of regulation compare and contrast regulatory approaches and features;  
- help regulators identify better practice among their peers that might be adopted in their own operations; and  
- be used to identify trends or patterns in implementing regulation or the performance of regulators. |
| F3.5 | The information collected from regulators should allow analysis of the structure, efficiency, effectiveness, responsiveness, scope of activity, burden of activity on regulated parties, and transparency and accountability of New Zealand regulators. |
| F3.6 | Standardised reporting could be formally integrated into Treasury’s regulatory management systems. In particular, the results could be used to find any parts of the regulatory system that need improving, and underpin policies to make those improvements. |
| F3.7 | Although reporting at the level of individual regulatory regimes might allow more sophisticated analysis of design and practice features, at this stage the Commission is not convinced that these benefits would outweigh the costs to larger departments of disaggregating performance data down to regime level. |
Recommendations

R3.1 Standardised reporting requirements for agency annual reports should be used to collect data on regulator activity. The Treasury and the State Services Commission, as the central agencies responsible for the public sector accountability framework, should be responsible for developing these standardised requirements.

R3.2 At the end of each financial year, the Treasury should collect and analyse performance data from the annual reports of regulators, and produce a public report outlining key features and trends.

R3.3 The Treasury and the State Services Commission should work with relevant departments to ensure that all regulators not captured by the Public Finance or Crown Entities Acts comply with the new standardised reporting requirements for their annual reports.

Chapter 4 – Role clarity

Findings

F4.1 Many firms that the Commission surveyed saw contradictory or incompatible regimes and regulators poorly managing duplicated compliance requirements as issues in New Zealand.

F4.2 “Deemed-to-comply” systems can let regulatory regimes adapt to changes in technology or shocks. They also permit different firms to find the compliance approach that best suits them. This lets regimes more effectively cover industries where the capability varies.

F4.3 Legislative frameworks that keep the number of objectives and conflicts to the lowest possible number and provide a clear hierarchy of objectives help to support regulators in making consistent and predictable decisions.

F4.4 Before new regulatory functions are allocated to an existing agency, policymakers must assess that the mission of the agency is compatible with the objectives of the new regime, and whether the new functions will get sufficient resource and attention.

F4.5 Regulator involvement in providing strategic policy advice is important for effective regulatory outcomes. Strategic policy should be developed so that it taps the experience of regulators and provides a dispassionate assessment of the issue. To ensure this balanced assessment, regulators should not have the sole or main responsibility for reviewing underpinning frameworks.

F4.6 Creating separate bodies so that one body is responsible for making rules and the other for enforcing them can have benefits, such as greater transparency, probity and good decisions. Even so, whether structural separation creates net benefits will depend very much on the details of the regulatory regime. Combinations of other regulatory design options (such as clearer regulatory objectives, stronger reporting and consultation obligations) may provide equivalent benefits, with lower costs and less disruption.
Cooperative arrangements like Memoranda of Understanding play an important role in managing regulatory overlaps. To be most effective, they should be reviewed regularly, be publicly available, provide clear guidance to regulated firms and individuals, and be empowered by legislation.

Regulatory exemptions can help manage overlaps between regimes, and allow regimes to adapt to changing business practice and circumstances. Principles or criteria guiding the use of exemptions should be included in legislation, and regulators should publish their reasons for granting exemptions.

**Recommendations**

**R4.1** The Cabinet Manual should be amended to set a general expectation that exposure drafts will be published and consulted on before introducing into Parliament legislation that creates new regulatory regimes or significantly amends existing regimes.

**R4.2** The next version of the State Services Commission’s guidance on machinery of government issues should set an expectation that, where a new regulatory regime is established, the entity responsible for implementing the regime should have a legislative obligation to publish a statement that explains its interpretation of its mandate, to consult on that statement, and keep it up to date.

**Chapter 5 – Regulatory independence and institutional form**

**Findings**

**F5.1** Designers of regulatory regimes must carefully assess the arguments for and against regulator independence. Arguments for political control must be weighed against the benefits of providing a credible long-term commitment to an impartial and stable regulatory environment.

**F5.2** For most regulatory regimes, the arguments for providing more independent regulation will be stronger than the arguments for less independent regulation.

**F5.3** To be effective, an expert regulator must operate within institutional arrangements that let it assess risks objectively and manage risks.

**F5.4** “Independence” is multi-faceted and covers significantly more than formal legal designation, including:

- the ability to adjust the regulatory settings and rules (regulation independence);
- the ability to undertake functions without interference (operational independence);
- funding arrangements that protect the regulator from external pressure (budgetary independence); and
- formal distance from the executive and security of tenure for governors and senior management (institutional independence).
<table>
<thead>
<tr>
<th>F5.5</th>
<th>Regulators often have to work with legislative regimes that are outdated or not fit-for-purpose. For example, regulators in transport sectors have to oversee outdated rules due to an inflexible legislative framework.</th>
</tr>
</thead>
<tbody>
<tr>
<td>F5.6</td>
<td>There is inconsistent allocation of legislative provisions between primary legislation and types of secondary legislation in regulatory regimes. There is evidence that existing mechanisms to promote greater consistency are ineffective.</td>
</tr>
<tr>
<td>F5.7</td>
<td>There is scope for the greater use of delegating authority to make secondary legislation to regulators, subject to appropriate controls, to ensure regulation can keep pace with technological and other developments. Designers of regulatory regimes need to consider what regulation-making powers can be delegated to the regulator, particularly in areas subject to technological or other changes, in order to future-proof the regime.</td>
</tr>
<tr>
<td>F5.8</td>
<td>Political pressures to intervene in the decisions of independent regulators are inevitable from time to time. Providing transparent mechanisms for political intervention in the decisions of independent regulators is preferable to wholesale regulatory reform designed to resolve political frustrations. It can also strengthen a regulator’s ability to withstand informal political pressure.</td>
</tr>
<tr>
<td>F5.9</td>
<td>Designers need to plan for how to manage the political imperatives to intervene in regulatory decisions. Whether direct powers of intervention are provided or not, designers should seek to ensure:</td>
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<td>• intervention is infrequent</td>
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<td>• intervention does not set precedents for future intervention</td>
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<td>• the regulator's authority is not undermined</td>
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<td>• intervention does not encourage regulated parties to work around the regulator</td>
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<td>• there is transparency in the intervention.</td>
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<td>F5.10</td>
<td>Government has regulatory and funding levers over many public services. Funding arrangements may permit faster enforcement action, but can be less useful for raising performance across the whole system in the absence of substantial failures, or for revealing information to consumers about relative performance. Designers of regulatory regimes to assure quality in public services need to consider how they expect the funding and regulatory levers will be exercised to manage performance issues across the whole system. They also need to ensure that regulatory requirements are appropriate for publicly-funded and privately-funded services.</td>
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<td>F5.11</td>
<td>The expectation that departmental agencies will operate with a high degree of autonomy is dependent on agreements between ministers and between chief executives, rather than any legal protections associated with this institutional form.</td>
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<td>F5.12</td>
<td>Government has indicated a desire to relocate some regulatory functions from Crown entities to departmental agencies. By itself, this would serve to reduce the formal operational independence with which those functions are undertaken. As a result, government will need to review any functions that are transferred to consider whether they should be undertaken in a statutorily independent way.</td>
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There is the potential for confusion about the accountability arrangements of departmental agencies, and the respective roles and responsibilities of:

- the minister responsible for the departmental agency;
- the minister responsible for the host department;
- the chief executive of the departmental agency; and
- the chief executive of the host department.

The legal differences between the types of Crown entities – the appointment and removal of board members, and ministerial powers of direction – do not in practice differentiate them, because the removal of board members and the issuing of formal ministerial directions to boards has almost never occurred.

The choice of institutional form will be important as much in terms of what it signals around expected levels of agency independence, as for the legal protections associated with particular agency forms.

Ministers and the founding governors and leaders of new agencies need to pay particular attention to the norms and cultures established around independence, in terms of the relationships between them, and the agency’s operations.

Regulation designed to prevent low-frequency, high-consequence (catastrophic) events is less likely to suffer from loss of focus or institutional support over time if located in stand-alone agencies.

Coherence problems between executive functions cannot be resolved by co-locating those functions alone. Designers of regulatory regimes need to identify what personal and professional relationships are key to the effective operation of a regulatory regime, and assess which of those relationships are best managed within an organisation and which are amenable to management between organisations. This should inform decisions around the location of regulatory functions.

While there can be benefits to structural changes in regulatory agencies, they can take time to emerge, and will often be disruptive to the smooth operation of regulatory regimes in the interim.

**Recommendations**

**R5.1** The Ministry of Transport should consider in its review of the Civil Aviation Act 1990 how the legislative regime can be flexible enough to take advantage of ongoing technological developments that could provide safety and efficiency gains. Subsequent reviews by the Ministry of Transport should consider how the other legislative regimes in transport can be made more flexible, taking into account the differences between the transport sectors.

**R5.2** The Minister for Regulatory Reform should coordinate a principle-based review of regulatory legislation to ensure greater consistency in allocation of legislation material between primary legislation and types of secondary legislation.
The Minister for Regulatory Reform should consider stronger mechanisms to ensure greater consistency in the allocating material between primary legislation and types of secondary legislation, either by elaborating departments’ Disclosure requirements for government legislation, empowering Parliamentary Counsel to provide stronger guidance, or some other mechanism.

The Minister of State Services should review agreements between ministers to establish and allocate functions to departmental agencies to ensure that respective roles, responsibilities and accountabilities are clear.

The State Services Commissioner should approve agreements between the chief executives of host departments and departmental agencies to ensure that respective roles, responsibilities and accountabilities are clear, and that there are appropriate formalities in place to preserve the independent exercise of statutorily independent powers.

Updated State Services Commission guidance on machinery of government choices should discuss the practical benefits, costs and risks associated with allocating functions to a department or stand-alone agency, as well as the accountability and governance considerations.

Plans and strategies for undertaking structural change involving regulatory functions should explicitly discuss how the effective operation of those functions will be maintained during the change.

Chapter 6 – Governance, decision rights and discretion

Findings

There is evidence of confusion around the role that some members of Crown entity boards with industry backgrounds are expected to play.

There is good SSC guidance on managing conflicts of interest for members of Crown entity boards.

Board members of Crown entities should not be appointed to act as representatives of external groups. Regardless of the backgrounds, experiences and prior or ongoing associations that make them valuable as members, their duty should always be to ensure the entity acts in a manner consistent with its statutory objectives and functions, and not as the representative or agent of any external group. The exception is where co-management arrangements are expressly intended.

The variety of internal governance arrangements and allocation of decision-making rights in regulators appears to be ad hoc rather than based on sound governance principles.
Designers of regulatory regimes should avoid allocating regulatory decision-making powers to ministers avoided unless good reasons are established. Decisions where ministerial decision making is likely to be appropriate include decisions with:

- significant value judgements, involving trade-offs that are not readily amenable to analysis
- significant fiscal implications, or which are integral to a government’s economic strategy.

In practice, the distinction between single-member and multi-member decision making is not always sharp. Colleagues/staff are likely to inform the views of individual decision makers.

In designing new regulatory regimes, it is most appropriate to vest significant regulatory decision-making powers in multi-member bodies, unless there are good reasons not to. But a range of day-to-day administrative decisions are more appropriately vested in individuals.

Designers of new regulatory regimes need to consider providing for the internal review of day-to-day administrative decisions which are taken by individuals.

There is extensive delegation of regulatory decisions within New Zealand regulatory regimes. In practice decisions are taken by a range of compliance staff, managers, chief executives, boards and ministers.

Designers of regulatory regimes need to consider the capabilities required to take regulatory decisions in specifying the nature of decisions regulators need to take, assigning decision rights, and providing for delegation.

Administrative discretion is a feature of many regulatory regimes. Principle-based or outcome-based regulatory regimes inherently involve the exercise of discretion, as do risk-based approaches to implementing regulation.

There is a range of legal constraints on the exercise of discretionary decisions. In particular, there are strong protections where those decisions intrude on the civil and political rights enshrined in the New Zealand Bill of Rights Act 1990. However, New Zealand is unusual in not acknowledging or protecting property rights.

Institutional and cultural constraints on the exercise of discretionary power support legal constraints by promoting ethical decision making.

Recommendations

The effectiveness of a part-time board comprised of participants in the regulated sector (as in the Financial Markets Authority) should be reviewed by the State Services Commission before its wider application to other sectors of regulation.
The State Services Commission’s guidance about appointing board members to Crown entities and its induction material for new board members provide good information on the duties of members. But it should update these documents to emphasise that members are not appointed and should not act as the representative or agent of any external group.

All regulators should publish and maintain up-to-date information about their regulatory decision making processes, including timelines and the information or principles that inform their regulatory decisions.

Chapter 7 – Regulator culture and leadership

Findings

The espoused values of new regulators may be “aspirational” rather than deeply engrained and widely accepted. This means such values may not actually reflect the beliefs of those working within the organisation or be reflected in their actions.

The culture that emerges within a new regulatory agency will be influenced by (1) the beliefs, values and assumptions of its founding leaders; (2) the experiences of members of the organisation as it matures; and (3) the injection of new beliefs, values and assumptions through new members.

When looking to improve the performance of a regulator, it is vital to understand whether what is required is a change in regulatory practice within a given culture, or a change in culture. This requires targeted analysis of the culture within a regulatory agency and the institutional factors that impact the way it operates.

Good internal communication is a catalyst for developing a culture of organisational learning. Yet central government regulatory workers are significantly less likely than non-regulatory workers to believe that there is good communication within their organisation.

With some exceptions, New Zealand regulators do not appear to have a strong culture of learning from experience.

There is evidence of a risk-averse culture within some New Zealand regulators. It is important to understand whether this culture has emerged as an appropriate and efficient response to the nature of the harm being managed or as a means of protecting the reputation of the regulatory body (or its employees).

The likelihood that systemic failures in regulatory regimes will go unchecked is higher when regulators have poor internal communication, lack the ability to learn from experience and have professional subcultures that are resistant to change.

The way in which a regulator engages with stakeholders is often perceived as a “window” to the organisation’s culture. In making such assertions, it is important to assess whether the quality of engagement is driven by the regulator’s deeply held values and beliefs, or whether it is driven by some other factor – such as the legislative environment or available resources.
A common understanding of the purpose and mission of a group is the first step in developing a common culture. While Chief Executives believe corporate culture is influencing the behaviour of frontline staff, central government regulatory workers do not perceive that senior managers communicate a clear organisational mission.

Government can “seed” the culture of a new regulatory agency by appointing founding leaders who have values, beliefs and experiences that are consistent with its vision of the “ideal” culture. However, selecting the “right people” does not guarantee that the “right” culture will emerge – the actions of founding leaders are the key embedding mechanism.

When establishing a new regulator, it is important to have founding leaders in place from the start of the organisation. This will provide the leader with the opportunity to influence the cultural foundations of the organisation. The use of “interim leaders” is to be avoided where possible.

While legislative provision can codify required actions, they do not guarantee that a regulator will develop deeply held values around the importance of those actions.

Monitoring bodies and central agencies can use formal and informal mechanisms to reinforce favourable cultures in new regulatory bodies.

There is disagreement in the academic literature around the extent and pace at which embedded cultures can actually change. This debate reaffirms the importance of promoting an “appropriate” culture from the inception of a regulatory body.

Chapter 8 – Consultation and engagement

Findings

The “regulatory relationship” is influenced by both the nature of the regulation and the characteristics of regulated parties and beneficiaries. When designing new regulatory regimes, careful thought must be given to the relationships that should exist between the regulator, regulated parties and those who are the beneficiaries of regulation.

In general, the greater the level of public participation the more critical it becomes that there is a common understanding of the scope for stakeholders to influence regulatory decisions. Failure to do so can undermine public confidence in engagement processes and in the competence of the regulator.

When developing engagement strategies, regulators need to examine both the fairness and proficiency of alternative mechanisms. Both proficiency and fairness are influenced by the manner in which mechanisms are implemented.

New Zealand common law, such as case law, contains a number of important principles that affect how and when regulators have an obligation to consult and what constitutes proper consultation.
Inquiry participants have raised concerns around the current engagement practices of some New Zealand regulators. These include insufficient time for engagement, a perception that regulators enter engagement with predetermined views and concerns that some regulators lack the capacity to engage affectively. The Commission has also heard positive feedback around the approaches adopted by some regulators – notably NZTA and the EPA.

Of the more than 50 Acts examined as part of the Commission’s inquiry, over half contain some form of consultation requirement.

Statutory consultation requirements are potentially most useful when:

- there is a likelihood that failure to consult would breach natural justice principles – for example regulation involves a significant use of the State’s coercive powers that could impair the civil liberty, livelihood or property rights of individuals;
- regulators have wide discretionary rule-making powers that involve making judgements about what is in the public interest;
- there are social equity reasons for specifying the consultation processes that should be followed for a specific group - for example where the affected group may not have the resources or capacity to effectively participate in a conventional consultation process;
- the affected community holds information on trade-offs and technical issues necessary for the regulator to make sound decisions.

While a precise definition of the Crown is lacking, it is accepted as being the Executive arm of government.

Those involved in designing and implementing regulatory regimes should understand how their actions or inactions are consistent with Treaty principles.

The courts interpret references to Treaty principles in legislation in a way that is consistent with the purpose of the relevant Act. In the event of a breach, the courts will likely issue a declaration that the proposed decision or action should be delayed so as to establish a process to respect the relevant Māori interest or right.

That Parliament will legislate in accordance with the principles of the Treaty, and will appropriately apply the principles on issues of relevance to Māori, means the courts can, depending on the context, require that an agent of the Crown have regard to the principles of the Treaty, even if there is no specific Treaty clause. The scope and strength of these “statutory interpretation rights” are, however, minimal. The court only takes them into account if the law to be applied in a given situation is ambiguous.

The Waitangi Tribunal has a wide mandate to consider any breach by the Crown and its agents. While it does not have decision-making functions with respect to its findings, its opinions carry considerable weight with the courts.
References to Treaty principles can be found in statutes in which Māori have strong iwi and hapū relationships. There does not appear to be a consistent description of the application of Treaty principles in statutes. Statutes with references to Treaty principles often contain regulatory provisions and create obligations on a range of parties that are not the Crown.

The priority to be given to references to Treaty principles in legislation depends on the wording of the clause and its status in the context of the statute.

There are incentives on officials advising on the content of bills and on Māori to include Treaty clauses in legislation, especially where Māori have clear interests, such as in legislation regulating the use of physical resources. Yet the incentives are different. Māori are incentivised because legislative provision is a mechanism they can use to enforce their rights through the courts if needed. Officials are incentivised to set minimum requirements in legislation that define the Crown’s obligations.

Whether a Treaty clause should be included in legislation requires careful judgement. It requires the careful balancing on a case-by-case basis of key considerations relating to the regulatory area, and the likely impact on Māori, other stakeholders, and the Crown.

The quality of guidance to help apply Treaty principles could be improved. None of the guidance reviewed was considered so bad that it would not add value to stakeholders, and overall the guidance promoted best practice over simple legal compliance. Even so, there was a significant difference between the best and worst examples. Only one example had sections specifically targeted to different stakeholder groups. Some guidance was misleading or inaccurate.

The framework for assessing guidance material could be used as a tool to help regulatory agencies develop guidance about applying Treaty principles in their area of regulation.

The EPA does not limit its role to ensuring that applicants comply with regulatory standards before an application is approved. Applicants are helped in preparing their applications and the EPA also helps those impacted by applications. Conflicts of interest are minimised because the application process is open, transparent and public.

The EPA discharges its Treaty responsibilities under its legislation and the Acts it administers within a net-benefit, decision-making approach.

Members of the Māori Advisory Committee are the guardians of good process, ensuring Māori have adequate opportunity to contribute their views, and that decision makers can use the consultation process to get the information they need.

The permanent and formal structure of the Māori National Network has meant that capability and trust has been built, and this is realising benefits. Te Herenga has increasingly been relied on to accurately and effectively bring the views of Māori to the table on their behalf.
Māori have additional steps and costs to incur when developing submissions, but care needs to be taken when considering funding, having regard to the capability of respective stakeholders and the importance of their perspectives, and ensuring funding is directly related to gaining those perspectives. Regulators need to monitor these expenses carefully.

Providing guidance for applicants and other stakeholders about navigating the process is considered a core part of the EPA’s role as a regulator.

Open and timely communication, accessibility, a balanced approach, pro-activity and a culture of respect and understanding must, to a large extent, be credited to the work and attitude of the EPA’s staff and its leadership.

The arrangements adopted by the EPA are a model that has brought the EPA positive change and support from stakeholders. In designing institutional arrangements, processes and practices to incorporate Treaty principles into their work, regulators should focus on their own regulatory responsibilities and functions, and the capabilities, capacity and incentives of their stakeholders.

An important lesson from the EPA’s experience for other regulators is that the investment in developing good relationships pays off in the form of reduced cost on all parties involved in the application process, while improving the quality of engagement and the resulting decisions. It has achieved buy-in to the success of the EPA approach and a shared commitment to making it work. When decisions go against stakeholders, those decisions are now more readily accepted and are less likely to be contested.

Chapter 10 – Decision review

Findings

In New Zealand there is significant overlap between the scope of judicial review and appeal in practice.

Judicial review in New Zealand is much wider in scope than in Australia, and can include greater scrutiny of the merits of decisions.

Courts will generally defer to the decisions of expert regulators of highly complex or technical areas. In these areas of regulation, there is still a clear distinction between judicial review and appeals, and judicial review is less likely to scrutinise the substantive merits of decisions.

In general, legislation establishing regulatory regimes does provide access to merits review of regulatory decisions.

In areas of complex or highly technical regulation, access to merits review or the scope of appeal provided is often limited.

It will generally be inappropriate to provide for appeals of ministerial decisions.
| F10.7 | Access to judicial review should be approached in a non-instrumental way. Judicial review is an important constitutional check on the power of the Executive, and is available to citizens as of right. |
| F10.8 | Access to appeal (or merits review) should be available where it is likely to improve the quality of regulation, in terms of the objectives of the regulatory regime, taking into account the costs of providing it. |
| F10.9 | The Commission has found no evidence to suggest that judicial review is an ineffective method of challenging regulators’ decisions, and ensuring they act in proper, lawful, and reasonable ways. |
| F10.10 | An absence of merits review increases the likelihood that aggrieved parties will seek recourse outside the legal system. In particular, it will encourage special pleading to politicians. |
| F10.11 | Merits review does not offer additional safeguards to ensure decision makers followed good processes, beyond those offered by judicial review. |
| F10.12 | The broad scope of judicial review in New Zealand means that the availability of merits review would not provide significantly stronger incentives on regulators to make correct decisions than is provided by access to judicial review alone. |
| F10.13 | Providing access to merits review may not always promote the objectives of a regulatory regime. |
| F10.14 | Designers of new regulatory regimes need to consider whether to provide access to merits review. In areas of highly complex, technical regulation, designers need to critically assess whether the appellate body has the institutional capability, compared to the decision maker at first instance, to improve the quality of decisions in terms of Parliament’s objectives for the regulatory regime. They also need to take into account the costs and uncertainty created by providing access to merits review. |
| F10.15 | There is no reason to believe that the incidence or complexity of appeals in areas of highly complex or technical regulation will inevitably decline over time. |
| F10.16 | In appeals of highly complex or technical regulation, providing the court with opportunities to directly question experts, in a non-adversarial setting, can assist in understanding the issues under appeal. |
| F10.17 | Providing courts or tribunals discretion over the admissibility of new evidence is likely to be more efficient than providing for appeals based on a frozen record. |
| F10.18 | Foreign expertise can play a valuable role in bringing expertise to merits review of highly complex and technical regulatory regimes. |
**Recommendations**

**R10.1** The Officers of Parliament Committee should review the adequacy of funding for the Office of the Ombudsman to undertake its statutory functions to a high standard.

**R10.2** Where courts interpret legislation in ways that significantly alter a regulator’s understanding of their mandate, the department responsible for the regime should review that aspect of the legislation. Its review should ascertain whether the courts’ interpretation undermines Parliament’s objectives in establishing the regulatory regime, and whether legislative amendment is desirable.

**Chapter 11 – Regulator practice**

**Findings**

**F11.1** Twenty years of *responsive regulation* in practice has demonstrated that institutional impediments have posed enormous challenges to the real-world implementation of the enforcement pyramid.

**F11.2** Putting risk-based regulation into practice poses considerable challenges for regulators. Adopting a risk-based approach to regulation requires the regulator to:

- deal with uncertainty about risk;
- operate in a political and public environment where there may be very different perceptions of risk and a poor understanding of what it means for the regulator to take a risk-based approach;
- make risk assessments and decide how to allocate its resources; and
- decide what approach it will take to enforcement once a risk assessment has been made.

**F11.3** A risk-based regulatory approach does not necessarily solve the issue of what risks to prioritise, how to deploy regulator resources, or what enforcement strategy to use.

**F11.4** Official guidance on regulator practice emphasises risk-based approaches as desirable, but also endorses responsive regulatory strategies.

**F11.5** Few of the regulators that responded to the Commission’s request for information applied the same level of compliance monitoring to all regulated entities. Most prioritised their efforts in some way, and in many cases regulators applied more than one criterion in judging where and when to monitor.

**F11.6** The strategies of the regulatory agencies examined by the Commission consider both the severity of the harm caused by compliance breaches and the attitude/behaviour of those causing breaches when allocating resources and taking action. However, they differ in how far they prioritise reducing harm or maximising compliance, and the extent to which the two objectives are integrated or treated separately.
There is evidence that some regulatory agencies are demonstrating elements of the really responsive regulatory approach in their compliance and enforcement strategies, especially the willingness of agencies to consciously consider the behaviour and attitude of regulated parties, institutional settings and the logic of regulatory tools, and changes in these factors, when taking enforcement action.

Many of the issues and challenges identified in the literature play out in New Zealand, including:

- difficulties assessing and targeting risk;
- conflicting compliance approaches;
- insufficient or inappropriate enforcement tools;
- the costs and timeliness of prosecutions; and
- the ability of regulators to learn from experience and respond to change.

In summary, regulators often struggle with putting risk-based approaches to regulation into practice, and there are challenges in applying enforcement tools.

The perception that regulators do not take opportunities to improve performance, do not learn from mistakes and successes, and are inflexible in the face of changes in priorities, suggests that New Zealand regulators are insufficiently attentive to two of the five key factors of really responsive regulation – performance over time and response to changes in the regulated environment.

Recommendations

Formal recognition of regulator forums or networks could offset the barriers to sharing good practices through:

- partial government funding (for example, 3-5 years) for regulator networks, tied to a business case and performance measures;
- revisions to Cabinet’s *Expectations for Regulatory Stewardship*, to clarify that regulatory agencies should seek to raise their own and the sector’s performance by sharing experiences and participating in communities of practice; and
- active monitoring by the Treasury and portfolio departments (for Crown entities) of regulator participation in communities of practice and other activities to share experiences.

To encourage the production of guidance material of practical use to regulators, one performance measure of the 3-5 year funding contract should be take-up and use of the guidance material produced.
Chapter 12 – Workforce capability

Findings

F12.1 Regulators need staff who, as a group, combine generic and specific competencies, including specific technical expertise, personal competencies such as communication skills, and an understanding of the compliance role and the role of the regulator. Gaps in these competencies can undermine the credibility of regulation and the achievement of regulatory outcomes. The precise mix of competencies needed is likely to vary between regulators and even within a regulator at different times. It is management’s responsibility to identify the required mix of competencies and ensure staff have, or can develop, these competencies.

F12.2 There is limited information about qualifications held by the workforce in the compliance sector. The proportion currently enrolled in training for qualifications appears to be small.

F12.3 The approach to developing the competencies of the people who work in regulatory roles is constructive and wide-ranging. However, the approach is evolving and sector participants consider there is room to improve.

Recommendations

R12.1 Regulators should:
- focus on recruiting and retaining staff with the appropriate industry knowledge and mix of enforcement, investigative and communication competencies;
- provide appropriate training and written guidance for staff, and monitor regulator practices for consistency with this guidance;
- facilitate opportunities for staff to improve their understanding of the regulated environment, business practices and the nature and magnitude of the compliance costs their engagement imposes on business; and
- implement cooperative arrangements with other regulators that facilitate the sharing of knowledge and resources.

R12.2 That the Compliance Common Capability Programme uses its review of the organisation’s future shape, direction and resourcing to:
- identify gaps in the current organisational framework and explain why it is in the best position to fill some of them;
- set out its specific roles as either a provider of training services or an adviser; and
- explain the issues about which it would provide advice, and how it would ensure that its advice is broadly based from across the regulatory sector.

R12.3 The Skills Organisation should coordinate effort to identify skill levels and gaps across the compliance sector and assess the adequacy of current programmes to fill those gaps.
Appropriate groups of regulators should encourage forums aimed at sharing good practice among the regulatory workforce.

That The Skills Organisation, as the accreditor of training providers, should seek both to maintain quality and consistent standards of provision, and to promote diversity and competition.

Regulators’ performance in developing staff should be reviewed, either as part of the Performance Improvement Framework process or through commissioned reviews modelled on that process.

Chapter 13 – Funding regulators

Findings

Organisational responsibility for advising, implementing and scrutinising funding arrangements has been established, and guidelines offer regulators and advisors guidance on how to approach funding issues. However, the two sets of guidelines cover similar issues in different ways. There is no general requirement for ex post evaluation of the impact of cost recovery and little published evidence about how well funding arrangements are working.

While in principle there can be benefits from regulators being at least partially funded through cost recovery, case-by-case assessment is required to secure these benefits in practice.

The Commission’s survey of businesses, and submissions to the inquiry, indicate concern in the business community about:

- the quality of the consultation that takes place before regulatory fees or levies are introduced;
- weak constraints on the level of charges, including limited transparency about how they are determined; and
- the structure of charges.
The funding frameworks in other selected countries are similar to New Zealand in that they:

- set out efficiency and, to a lesser extent, equity as the main objectives of cost recovery;
- require consent, usually of a minister or Parliament, before a fee or levy is introduced;
- are based on a distinction between cost recovery and taxation; and
- provide guidance material.

There are, however, examples in other jurisdictions of:

- more rigorous consultation and impact assessment requirements before fees are introduced;
- stricter requirements for performance standards and reporting against those standards when new fees are introduced;
- penalties for failing to achieve the standards; and
- more detailed advice about how to implement cost recovery.

It is desirable that regulators, as they develop improved performance reporting frameworks, use these frameworks to measure the cost of delivering regulatory services and report this information publicly.

**Recommendations**

**R13.1** The Government should publish its cost recovery policy, covering issues such as:

- policy objectives;
- guidance about how to make trade-offs should objectives conflict;
- when cost recovery may be appropriate;
- consultation requirements before implementation;
- how and when arrangements are to be reviewed and by whom; and
- responsibility for ensuring compliance with the policy.

**R13.2** Portfolio ministers should be responsible for ensuring that agencies within their portfolio have complied with the Government’s cost recovery policy. Chief executives of agencies proposing a new or amended fee or levy for regulatory services should be required to certify through an appropriate mechanism that their agency has made adequate use of the Treasury guidelines.

**R13.3** The grounds on which the Regulations Review Committee can disallow a regulation should include that the regulator in developing and implementing a fee or levy has had inadequate regard for the economic framework set out in the Government’s guidelines for setting charges in the public sector.
R13.4 The Auditor-General should introduce an enhanced programme of audits of regulators’ compliance with Government cost-recovery guidelines.

R13.5 Portfolio reviews undertaken within the Performance Improvement Framework, and/or the Regulatory Systems Reports prepared under the expectations for regulatory stewardship, should review and report on the adequacy of the approaches to cost recovery of regulators within each portfolio.

R13.6 The Government and Auditor-General should review the Treasury’s Guidelines for Setting Charges in the Public Sector and the Auditor-General’s Charging Fees for public sector goods and services, to ensure that the guidelines reflect current knowledge about when and how to implement cost recovery.

Users of the guidelines (whether the two sets of guidelines continue or are combined) should:

- only have to go to one place for advice on any issue;
- not receive conflicting advice from the guidelines; and
- be clearly informed about the scope of the entities and charges that the guidelines cover.

R13.7 The Government, when it reviews New Zealand’s cost recovery guidelines, should seek to collaborate with the review of the cost recovery guidelines currently being undertaken in Australia.

R13.8 That the Government consider whether those agencies that set or amend fees or levies can access adequate advice and experience from other agencies and departments.

Chapter 14 – Accountability and performance monitoring

Findings

F14.1 Most, but not all, regulators are subject to the Official Information Act.

F14.2 Accountability is a necessary but insufficient condition for better performance.

F14.3 Key tasks for monitors of regulators are:

- providing assurance to ministers that regulators have robust risk identification and assessment processes; and
- assessing the ongoing fitness-for-purpose of regulatory regimes.

F14.4 Regulator chief executives surveyed by the Commission did not consider that central agencies played a significant role in holding their agency’s regulatory functions to account.

F14.5 Departmental monitoring of regulators is weak and departments are not contributing enough to regulatory quality and performance.
Recommendations

R14.1 The State Services Commission and the Treasury should update guidance for ministers and departments on monitoring Crown entities to:

- provide more detail on the issues that monitoring departments and ministers should look for in reviewing the performance of Crown entity regulators;
- clearly express the importance of monitoring departments having the deep sectoral knowledge necessary to understand the regulator’s operating environment; and
- place more emphasis on vigilance and free and frank advice from monitoring departments.

R14.2 The Treasury and the State Services Commission should work with monitoring departments to:

- define common and richer performance measures for regulator Crown entity monitoring;
- update performance information in accountability documents around monitoring in time for the 2015/16 financial year; and
- reflect the new measures in the performance agreements and reviews of departmental chief executives.

R14.3 Departments responsible for monitoring regulator Crown entities should develop and maintain explicit statements of their monitoring roles and responsibilities. In doing so, departments should regularly review whether the monitoring relationship:

- gives ministers the assurance they need about risk identification and management;
- allows departments to accurately assess the performance of regulators; and
- promotes substantive dialogue with entities about the fitness-for-purpose of the regime.

R14.4 The performance of departmental regulators should be strengthened by:

- the Treasury publishing the findings from the Regulatory System Report about departmental stewardship activities;
- the State Services Commission (SSC) developing explicit measures for regulatory performance in chief executive performance agreements and annual expectations letters; and
- SSC using PIF and Treasury surveillance information about departmental regulatory performance in reviewing the performance of chief executives.
Chapter 15 – System-wide regulatory review

Findings

F15.1 The New Zealand Government is implementing a suite of initiatives to improve the management of the stock of legislation and regulation. It does not use many of the approaches to system-wide evaluation of regulatory regimes that are used in other countries, some of which have been identified as involving low effort and potentially low/high return in those countries.

Recommendations

R15.1 The Government should publish an overarching strategy that sets out how it will improve the management of the stock of regulation. The strategy should explain how specific initiatives fit within it, and should describe how successful implementation of the strategy will be measured and how it will benefit the community.

R15.2 The performance of departments, in satisfying Cabinet’s expectations that they keep current the regulatory regimes they are responsible for, should be strengthened by:

- the Treasury publishing the findings from the Regulatory System Report about departmental stewardship activities;
- the State Services Commission (SSC) developing explicit measures for regulatory performance in chief executive performance agreements and annual expectations letters; and
- the SSC using both the Performance Improvement Framework and Treasury surveillance information about departmental regulatory performance in reviewing how chief executives perform.

R15.3 Departments should explain their plans for monitoring, evaluation and review in their papers for the Cabinet Legislation Committee seeking agreement to introduce new legislation. The Treasury should amend the “Disclosure requirements for government legislation” to make this expectation clear. Departments’ plans should be proportional to the significance of the regulation.

R15.4 The Treasury should continue to monitor approaches to evaluation used in other countries, while implementing the current evaluation agenda, building an approach that:

- ensures that the scale and scope of evaluations is proportionate to the monetised impacts of regulation;
- provides transparent reporting of the Government’s strategy, work programme and progress in achieving performance targets;
- clearly defines responsibility for managing the stock of regulation;
- is based on consultation with those affected by regulation;
- is driven by a need to prioritise effort where the payoff is expected to be largest; and
- is adequately resourced, so that people with the capabilities to undertake effective evaluations can implement it.
Chapter 16 – Making it happen

Recommendations

R16.1 The Government should publish the responsibilities of the minister responsible for regulatory management. These responsibilities could include:

- defining the overall objective of the regulatory management system;
- prioritising effort across the regulatory system;
- specifying and allocating tasks for improving the system; and
- promoting regulatory policy and the case for continuous improvement in regulatory design and practice.

R16.2 The minister with responsibility for regulatory management should publish a strategy report that sets out the medium-term objectives that the Government is seeking to achieve through the regulatory management system, its strategic prioritisation of effort for achieving these objectives, and its work programme. The minister should report regularly on progress towards delivering this work programme, and update the statement as necessary.
## Appendix A  Public consultation

### Submissions

<table>
<thead>
<tr>
<th>INDIVIDUAL OR ORGANISATION</th>
<th>SUBMISSION NUMBER</th>
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<tbody>
<tr>
<td>Air New Zealand</td>
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<tr>
<td>Alan Marshall</td>
<td>002</td>
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<td>Aviation New Zealand</td>
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<td>Commerce Commission</td>
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<td>Environmental Protection Authority</td>
<td>020</td>
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<td>Federated Farmers of New Zealand</td>
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<td>Foodstuffs (NZ) Ltd</td>
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<td>Genesis Energy</td>
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<td>InternetNZ</td>
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<td>KLR Investments</td>
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<td>Mighty River Power</td>
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<td>Ministry of Business, Innovation and Employment</td>
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<td>Ministry of Transport</td>
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<td>Molly Melhuish</td>
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<td>Mortlock Consultants Limited</td>
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<td>New Zealand Council of Trade Unions</td>
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<td>New Zealand Customs Service</td>
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<td>New Zealand Food and Grocery Council</td>
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<td>New Zealand Public Service Association</td>
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Appendix A Public consultation

Physicians and Scientists for Global Responsibility 003
PowerCo 014
Reserve Bank of New Zealand 009
Tasman District Council 001
Telecom New Zealand Limited 041
Transpower 032
TrustPower 007
Vector 029
Vodafone New Zealand Limited 046
Wellington Electricity Lines Limited 017

Engagement meetings

INDIVIDUAL OR ORGANISATION
Age Concern New Zealand
Air New Zealand
AMI Insurance
ANZ Banking Group (NZ)
Bank of New Zealand
Brent Layton
Buddle Findlay
Buddy Mikaere
BusinessNZ
Carter Holt Harvey
CERT Systems
Chorus
Civil Aviation Authority of New Zealand
Claire Matthews
Commerce Commission
Compliance Common Capability Programme - Steering Group
Consumer New Zealand
Crown Law Office
David Goddard QC
David Tripe, Centre for Banking Studies, Massey University
Dean Knight, Faculty of Law, Victoria University of Wellington
Department of Internal Affairs
Derek Gill
Education Review Office
Electricity Authority
Electricity Networks Association
Environmental Protection Authority
Federated Farmers of New Zealand
Financial Markets Authority
Financial Services Council of New Zealand
Financial Services Federation
Fitch (Hong Kong) Ltd
IAG New Zealand Limited
Inland Revenue
Insurance Council of New Zealand
James Ataria  
Law Commission  
Major Electricity Users’ Group  
Malibu Hamilton  
Maree Pene  
Maria Bartlett  
Maritime New Zealand  
Medsafe  
Mighty River Power  
Ministry for Primary Industries  
Ministry of Business, Innovation and Employment  
Ministry of Business, Innovation and Employment - Small Business Development  
Ministry of Health  
Ministry of Justice  
Ministry of Transport  
Molly Melhuish  
Mortlock Consultants Limited  
New Zealand Association of Credit Unions  
New Zealand Automobile Association  
New Zealand Banker’s Association  
New Zealand Council of Trade Unions  
New Zealand Law Foundation  
New Zealand Public Service Association  
New Zealand Transport Agency  
New Zealand Treasury  
NZI  
Office of the Auditor-General New Zealand  
Office of the Clerk of Representatives  
Payments NZ  
Professor David Round  
Professor Edgar Schein  
Professor Lew Evans  
Professor Philip A Joseph  
Public Law Committee of the Wellington District Law Society  
Reserve Bank of New Zealand  
Richard Hill  
Russell McVeagh  
School of Management, Victoria University of Wellington  
Simon Power  
Sir Michael Cullen  
Standard & Poor’s Rating Services  
State Insurance  
State Services Commission  
Te Puni Kōkiri  
Television New Zealand  
The Skills Organisation  
Tim Hale  
Tipene Wilson  
Tower Insurance
Transpower
Tuatara Breweries
Vector
Victoria University of Wellington
Vodafone New Zealand Limited
Waikato Regional Council
Webb Henderson
Westpac
Appendix B  Applying the Treaty principles guidance framework

Table B.1  Assessment of 10 documents against the Treaty principles guidance framework

<table>
<thead>
<tr>
<th>Document</th>
<th>Assessment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Best practice guidelines: Tangata whenua effects assessment – a roadmap for undertaking a Cultural Impact Assessment (CIA) under HSNO 1996¹</td>
<td>The good&lt;br&gt;It is very positive that the ERMA (now part of the Environmental Protection Authority) commissioned guidance to help applicants (under the HSNO) collect the information needed for ERMA to be able to assess the applicant’s proposal. Organisations don’t always place a high priority on helping regulated entities to navigate the process, instead viewing their role as simply enforcing compliance.&lt;br&gt;The guidance appears comprehensive. It covers the purpose of the relevant legislation and related guidance, the key Māori interests and how they are to be identified. Contemporary thinking is identified, but the guidance lets itself down a little by dwelling too long on how undeveloped it is, at the risk of users losing confidence in the approach outlined.&lt;br&gt;While identifying the legal basis for the guidance, best practice beyond the legal standards is promoted.&lt;br&gt;Excessive prescription is avoided.</td>
</tr>
<tr>
<td>Consultants prepared this guidance for the Environmental Risk Management Authority (ERMA). The guidance was to help applicants prepare a CIA under the Hazardous Substances &amp; New Organism Act (HSNO).</td>
<td>The not so good&lt;br&gt;The guidance could easily have been made more accessible. In particular, Māori terms should have been defined, and the reference to “various pieces of legislation” appears lazy.&lt;br&gt;There could have been more guidance on how best to engage with Māori, how best to prevent/resolve differences of view between the applicant and Māori, and the implications and options for the claimant if differences are not resolved.&lt;br&gt;Curiously, the document appears written for the benefit of Māori with an interest in the application, rather than the applicants themselves, which is confusing in places (such as the 2nd half of page 3). It may have been better to provide separate guidance for applicants and for Māori with an interest in applications.&lt;br&gt;The guidance is confusing in places (the discussion of economic values, Treaty principles, and the way the material is structured appears to allow for double counting of impacts). Also, it isn’t always clear about the different categories of impacts. The guidance would have benefited from a worked example.&lt;br&gt;In places the document is internally inconsistent. For example, it is described as a cultural impact assessment, yet culture is only one of four categories of impacts covered. It discusses quadruple bottom line reporting, and in places is consistent with this approach, but then provides a table with two additional categories (relationships and the Treaty). In the introduction it is described as being for applicants, yet the footnote on the same page says the guidelines are to assist applicants, tangata whenua and advisors.&lt;br&gt;Discussion of Treaty principles appears incorrect. Applicants are expected to consider whether Treaty principles are “impacted by the proposed application, and if so how?” This is unreasonable. The principles apply to Māori and the Crown – the applicant will usually be neither. It is ERMA and affected Māori, not the applicant that should judge whether the application, if approved, would impact Treaty principles. Rather, the guidance should have tried to more precisely articulate the nature of Treaty principles from the regulator’s point of view. The applicant and Māori would have found this more useful.</td>
</tr>
</tbody>
</table>

¹Consultants prepared this guidance for the Environmental Risk Management Authority (ERMA).
Appendix B Applying the Treaty principles guidance framework

There are few links to additional information and no link/contact for applicants or Māori if they are finding it hard to apply the guidance.

The unsure
It is unclear:
- whether there is a review process for the guidance and, if so, whether stakeholders are able to input to that process; and
- how well the guidance is promoted.

Summary and assessment
The guidance is a positive initiative and will provide some help to applicants and Māori potentially impacted by an application. It is pleasing that its focus is mostly “best practice” rather than legal compliance. It is reasonably comprehensive, although there are likely gaps for the average applicant.

The guidance could easily have been improved at little cost. Perhaps ERMA should have done this, with the resulting document then being more closely associated with ERMA rather than the consultants (Repo Consultancy Ltd). In particular; a worked example, a glossary of Māori terms, a guide to effective engagement with Māori and links to assistance in applying the guidance would have added to its value. The requirement imposed on applicants by the guidelines with respect to Treaty principles appears a significant and inappropriate burden.

Assessment: “Passable”
### Document

| The Treaty, the guidance is very good. However, given its stated purpose “This guide has been prepared as a resource for policy analysts who are called upon to formulate policy advice on the application of the Treaty Principles”, it falls short. In getting to the end of the document, one is left feeling a significant opportunity has been missed – for the Executive to define in broad terms what it believes the relationship between Māori and the Crown should be, and the impact this should have on the policy development process. |
| Assessment: “Good” |

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**Guidelines for Cultural Safety, the Treaty of Waitangi and Māori Health in Nursing Education and Practice**

The Nursing Council of New Zealand prepared this guidance.

The purpose of the guidelines is to provide a framework for training providers to follow when training nurses on cultural safety, Treaty principles and Māori health. The guidance must be viewed in the context of the process surrounding its use. For example, entities are audited against the guidance.

It is interesting to note that the guidance pre-dates the New Zealand Public Health and Disability Act 2000, which introduced Treaty principles into the health sector.

### The good

- The guidance appears to be comprehensive in the breadth of material covered, at least in part because it is strongly principle based. It is also strongly focused on best practice (and focused on outcomes), with no reference to managing legal risk.

- The material covered in the guidance is clearly linked to the relevant statutes.

- The guidance has been updated several times, and appears well publicised and accessible.

- Appropriately, the relevance of the Treaty approach is extended to the treatment of non-Māori cultures by nurses.

### The not so good

- The interface between Treaty principles and cultural sensitivity is unclear. For example, what does the Treaty require in the treatment of patients that isn’t provided for by appropriately applying cultural sensitivity? In this sense, the model appears a little “forced”, inconsistent and unnecessarily repetitive in places.

- Also, some of the Treaty messages appear more suited for health providers than for nursing students, for example, “enabling Māori autonomy and authority over health”.

- In spite of numerous reviews, there are some inaccuracies. For example, the guidance incorrectly claims the Court of Appeal decided in “1975 that both versions of the Treaty were legal.” And “As Crown agents, nurses have an obligation to honour the principles of the Treaty…” also appears suspect.

- In places the guidance appears to border on opinion. For example, no evidence is cited to support the statement that poor relative Māori health status is the result of the loss of cultural beliefs and practices and the Māori language.

### The unsure

- The guidance is very high level and abstract. Because education providers implement the guidance, it is unclear how well the principles are being explained, illustrated with best practice examples, and generally being made relevant to nursing students.

- Similarly, how the audits are performed ultimately determines whether the principles are able to operate as they should (enabling different approaches to achieving the learning objectives).

### Summary and assessment

It is pleasing that the guidance takes a strongly “best practice approach” in preference to legalistic. Also, the spill-over relevance of a Treaty-oriented approach to other cultures is outlined (cultural sensitivity), although the relationship between the two concepts is not always clear. This detracts from the quality of the guidance. The impact of the guidance depends greatly on how well education providers apply it, which is uncertain, although some confidence can be had in that the function is audited.

Assessment: “Good”
<table>
<thead>
<tr>
<th>Document</th>
<th>Assessment</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Zealand Coastal Policy Statement 2010 Guidance note Policy 2: The Treaty of Waitangi, tangata whenua and Māori heritage⁴</td>
<td>The guidance is comprehensive, working systematically through the stages needed for local government to appropriately implement the policy, summarising and linking to the main legislative provisions. Many other links to additional information and guidance are also provided. No errors were picked up, and the document appeared logically consistent and relevant to planners and others, including Māori with an interest in ensuring their interests and rights are taken into account in the planning process. Although prescriptive legal standards were appropriately highlighted, the guidance itself appeared to avoid excessive prescription, and focuses nicely on encouraging best practice beyond the legal requirements. The guidance made very good use of examples, including links to real life practices. The document appeared reasonably well promoted and accessible. Past reviews and their findings were evidenced, suggesting the guidance is a living document. <strong>Summary and assessment</strong> The guidance appears an excellent aid for helping local government meet and exceed their legal obligations with respect to Māori interests, without being excessively prescriptive (an important feature in this case because of the differing capabilities and interest of the stakeholders). Māori, too, should benefit from having their legal rights so clearly laid out, and in certain cases should be able to use the guidance to help drive better performance across local government. <strong>Assessment: “Excellent”</strong></td>
</tr>
<tr>
<td>Guidelines for Consulting with Tangata Whenua on the RMA: An Update on Case Law⁵</td>
<td><strong>The good</strong> The guidance appears comprehensive, logically consistent, is well laid out and appears professional. No errors were detected. It is relatively current (2010), and is an update of earlier documents. While the focus was clearly legal, being a review of the relevant case law, in places it also encouraged best practice. There was also a good balance of core principles, illustrated with real examples. Both good and bad practices were illustrated. The document flowed well (logically) and good summaries were provided at the start of each section, helping to make it more accessible. The guidance was easy to find. <strong>The not so good</strong> It would have been even more useful had there been more links/references to related material/topics across government – not just to court cases and MFE material. More discussion of best practice would have been good, that is, as a strategy for managing legal risk and to achieve better outcomes, and perhaps within the wider context of the purpose of the RMA and impacts assessments. <strong>Summary and assessment</strong> The guidance material is very good and would be a useful aid to the range of stakeholders involved in the Resource Management consents process. More links to and discussion of a wider context may have improved usefulness at minimal cost. <strong>Assessment: “Very good”</strong></td>
</tr>
</tbody>
</table>
### Document

**Guidelines for Cultural Assessment – Māori Under the Intellectual Disability (Compulsory Care and Rehabilitation) Act 2003**

The 2004 guidelines update earlier guidelines promulgated in 1995. Interestingly, the earlier guidelines pre-date the 2003 Act, which incorporated Treaty principles into legislation for the mental health sector. The purpose of the guidelines is to facilitate a cultural experience for Māori under the Act consistent with supporting their recovery.

#### The good
- The guidelines seek to encourage best practice, while appropriately evidencing the legal basis for the guidelines.
- The guidelines appear appropriately principle based.
- The flow of the document appears logical.

#### The not so good
- There are no links to other material or a contact person in the event further advice is needed. For example, the commentary on confidentiality appears inadequate and should perhaps link to more comprehensive advice. Further, “resolving issues in the final report” perhaps warrants more discussion.
- The guidance doesn’t have the professional polish of some of the other guidance material reviewed. In particular, the second part of Appendix 2 is bordering on incomprehensible, and reads in places as an incomplete policy proposal.

#### The unsure
- It is not clear the guidance would be of tremendous value to the range of stakeholders identified (a number of mental health professionals, a specialist in tikanga, and whānau). It is possible their needs would have been better met by providing a range of guidance products (for example, a pamphlet for the patient/whānau, a formal document for the health professionals, and another for the specialist in tikanga focusing on expectations and boundaries). It is possible other, more targeted material is available.

#### Summary and assessment
- The guidance material appears broadly appropriate for its purpose, but lets itself down in places through unprofessional drafting and little coverage of some topics. Links to other material would have made the document more useful.

**Assessment: “Good”**

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**Good practice guidelines for working with tangata whenua and Māori organisations: Consolidating our learnings**

Garth Harmsworth (an employee of Landcare Research) prepared this document for Landcare Research. The document is “… intended to improve race relations in New Zealand …”, and to improve Māori participation in resource management planning and policy.

#### The good
- The document provides a very strong foundation to the guidelines, in particular the need for greater Māori involvement in resource management, the legal context, international developments, and the current direction of travel. The document also has a very useful section that outlines differences in perspectives between local government and Māori.
- The guidance is strongly orientated towards best practice (consistent with meeting the purposes of the relevant legislation) in preference to simply meeting legal obligations. It is appropriately principle based, and well illustrated with good and bad real-life examples.
- Extensive referencing gives the document a strong sense of credibility.
- The explicit acknowledgement of the importance of other stakeholders, and the targeting of their interests and perceptions was a welcome addition to this form of guidance.

For the most part, the document is well crafted, although at times it appeared to stray into an academic piece rather than guidance.

#### The not so good
- The structure/organisation of the document is not always clear, for example, the inclusion of an interesting but perhaps out-of-context section on Local Government New Zealand views within the legislative framework section.

After an impressive build-up with numerous strong insights, the guidance falls a
little flat. The one page of dot points in particular is repetitive and not well organised. In contrast, the consultation guideline from the Auckland Regional Council (Appendix 2) is very good. Also, the guidance would have benefited from links to other key documents/guidance.

The recommendations and conclusion at the end of the document appear to be directed to at least two different audiences – the government and local authorities. This is confusing. In reality, the key themes appeared appropriate also for Māori and other stakeholders. With little effort, useful recommendations could have been distilled from the document for these groups too.

The Treaty was discussed, but not in a way that would provide strong direction to decision makers.

Summary and assessment
The document at times appeared to be an academic piece, advocacy, and guidance. This was confusing. Regrettably, the guidance aspect appeared to be the weakest part. That said, excellent insights and perspectives were woven through the document that would be of great value to a wide range of stakeholder interests. Clearly the author has extensive practical experience working with Māori and other groups.

Assessment: “Good”

Guidance on the Marine and Coastal (Takutai Moana) Act 2011

The Ministry of Justice has prepared this guidance to facilitate and clarify the status and impact of claims under the Marine and Coastal (Takutai Moana) Act 2011.

The good
This guidance material is excellent. It is the only guidance reviewed that has sections specifically targeted to different stakeholder groups (Māori claimants, local authorities and business). This, together with intelligent use of links, a logical flow, a flow chart to bring all the material together, a frequently asked questions section, and the omission of any advocacy sections has made the document very easy to navigate and assimilate.

The document has been professionally prepared and presented, appears comprehensive and free of errors. Links to other material and a named contact for enquiries adds to the likely value of the document.

The guidance is current. Applications under the Act are possible only up to 2017, so it is unlikely to need further review/updating.

For what the guidance is – an aid to understanding of the Marine and Coastal (Takutai Moana) Act 2011, it appears to strike an appropriate balance between prescription and principle-based standards. Similarly, the guidance itself appears “best practice” rather than the behaviours being encouraged. Within this context, it would have been interesting to review the related guidance for officials in implementing the Act against the best practice criteria.

The unsure
There is likely to be guidance for officials on their discharging their responsibilities under the Act. It is not known what the quality of this guidance might be.

Although the Act has a Treaty clause, there is no mention of it in the guidance. It would be interesting to know the reason for this – this is a notable contrast with other guidance documents reviewed.

Summary and assessment
The guidance is excellent and would be likely to add significant value to applicants under the Act while also being useful to other stakeholders with an interest in claims.

Assessment: “Excellent”

Nga Ara Tohutohu Rangahau

The good
The purpose of these guidelines is to improve research by the Ministry of Social Development (MSD) and its contractors where that research requires input from Māori.

The origins of the guidelines include problems with past research involving Māori and the importance of good research on Māori to meet MSD’s objectives. There is no explicit reference to the statutes under which MSD operates (that is, the guidelines are not legalistic).

The framework used appears logical, robust and complete, principles are used in preference to prescriptive standards, and no errors were identified.

There are good links to additional information and resources across the government and non-government sector. Ministry contacts are identified for further information.

The guidance could have been shortened considerably by cutting back on the repetition, and by using the services of a good editor.

The document would have benefited from the use of more examples to illustrate the principles.

In places the guidance appeared excessively aspirational. For example, in most cases it will not be possible (or even sensible) for contractors to have secured the support of Māori before being awarded a research contract by MSD.

The guidelines do not appear complete, despite them being nearly 10 years old. For example, the ethics guidelines intended to guide engagement with Māori are “forthcoming”.

The guidance does not appear to be current, one example being the contacts identified.

The guidance material appears fit for purpose and has comprehensive links to other material. But it lets itself down by being repetitive and not including real-life examples to bring the theory to life.

Assessment: “Good”

The rational for the guidance is clearly articulated.

The guidance is professional, clear and succinct. It covers what needs to be covered for a high-level document (key principles, and a link to further reading).

While the disclosure requirements are prescriptive, the guidance is principles based.

The new disclosure requirements are being trialled before they become legislative requirements. Within this context, it is appropriate to see Treasury contacts identified for clarification, and to see feedback on how the guidance works.

The references are almost exclusively legal. It would have been useful to reference some of the normative guidance available to encourage best practice.

The required disclosure is new. It is not clear how effective the guidance will be; for example, whether officials will resort to a pro forma response along the lines of legal advice was sought. Success will depend on the attitude of officials and the extent of effective monitoring and comment by interested stakeholders. For example, it was found that stakeholder monitoring and review of Regulatory Impact Statements was by itself insufficient to generate the quality improvements sought by government.


The Treaty guidance is a subset of the wider disclosure statement guidance for officials. The existing administrative disclosure statements are intended to become legislative requirements after a trial period and review. The Treaty guidance is an aid to officials answering the question “What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi?” Answering this question promotes accountability of officials to ministers and other stakeholders.
It is also an opportunity for officials to share information on their approach to promoting compliance with Treaty principles. Also, the guidance invites officials to identify impacts of the respective bill on the rights and interests of Māori, and the steps taken to determine if those effects are consistent with the principles of the Treaty. What appears to have been omitted is whether the bill is actually deemed to be consistent with Treaty principles, and, if not, where it is not and what has been done as a consequence. After review, this may be a logical next step for the requirements and guidance.

Summary and assessment

The guidance appears broadly appropriate for helping officials think about whether a bill is consistent with Treaty principles, although it is perhaps a little legalistic in its focus, at the expense of a wider and more aspirational approach.

Assessment: “Good”

Notes:

11. www.treasury.govt.nz/publications/guidance/regulatory/disclosurestatements
# Appendix C  Stocktake of appeals provided for in regulatory legislation

<table>
<thead>
<tr>
<th>Legislation</th>
<th>Specific legislative provision</th>
<th>Initial decision maker</th>
<th>Type of appeal</th>
<th>Appeal body</th>
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<tbody>
<tr>
<td>Animal Products Act 1999</td>
<td>Section 154: appeal against making of or refusal to make compliance order</td>
<td>District Court</td>
<td>Re-hearing</td>
<td>High Court</td>
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<tr>
<td>Animal Welfare Act 1999</td>
<td>Section 143: appeal against decision on enforcement order</td>
<td>District Court</td>
<td>Re-hearing</td>
<td>High Court</td>
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<tr>
<td></td>
<td>Appeal against criminal convictions (pursuant to Crimes Act)</td>
<td>District Court</td>
<td>Re-hearing</td>
<td>High Court</td>
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<tr>
<td>Anti-Money Laundering and Countering Financing of Terrorism Act 2009</td>
<td>No appeal rights</td>
<td></td>
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<tr>
<td>Atomic Energy Act 1945</td>
<td>No appeal rights</td>
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<tr>
<td>Auditor Regulation Act 2011</td>
<td>Section 24: appeal against decision about licensing and related matters</td>
<td>Accredited body or FMA</td>
<td>Re-hearing</td>
<td>District Court</td>
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<td></td>
<td>Section 31: appeal against decision concerning registration of a firm.</td>
<td>Accredited body or FMA</td>
<td>Re-hearing</td>
<td>District Court</td>
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<td>Building Societies Act 1965</td>
<td>Section 16: appeal against refusal to register the rules</td>
<td>Registrar</td>
<td>Re-hearing</td>
<td>High Court</td>
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<td>Section 122C: appeal against refusal to disclose information under s 122B</td>
<td>Any person</td>
<td>Re-hearing</td>
<td>High Court</td>
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<td>Section 124: appeal against suspension or cancellation of registration</td>
<td>Registrar</td>
<td>Re-hearing</td>
<td>High Court</td>
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<td>Biosecurity Act 1993</td>
<td>Section 154EL appeal against compliance order</td>
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<td>Re-hearing</td>
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<td>Broadcasting Act 1989</td>
<td>Section 8: review of broadcaster's decision on a complaint</td>
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<td>Section 18: appeal against decisions relating to complaints</td>
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<td>Section 330(1): appeal against decision relating to licence as a building practitioner</td>
<td>Registrar of Licences Building Practitioners Board</td>
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<td>Climate Change Response Act 2002</td>
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<td>Commerce Act 1993</td>
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<td>Sections 52Z: right of appeal against Commission input methodology determinations</td>
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<td>Freshwater Fisheries Regulations 1983 (made under authority of Conservation Act 1987)</td>
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<td>Corporations (Investigation and Management) Act 1989</td>
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<td>Energy Efficiency and Conservation Act 2000</td>
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<td>Section 51: appeal against Chief Executive’s review of determination as to quantum and allocation</td>
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<td>Section 8V: appeal against refusal to grant exemption from provisions of Food Hygiene Regulations</td>
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<td>Section 28: landholder/owner can request review of notice to make a firebreak or escape route or remove combustible material</td>
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<td>Rural Fire Mediator</td>
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<td>Section 49: any person upon whom a levy is imposed under specified sections can request the National Rural Fire Officer to appoint a Rural Fire Mediator to review the levy imposed</td>
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<td>Rural Fire Mediator</td>
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<td>Section 52: A Fire Authority may lodge an appeal against the apportionment by the National Rural Fire Officer of firefighting costs in a regional fire emergency</td>
<td>National Rural Fire Officer</td>
<td>The Minister must appoint a person to conduct and determine the review</td>
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<td>Section 65: appeal in relation to a dispute about a levy or determination in ss 45 or 46</td>
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<td>Section 85: any member of a society or any person may object to the proposed amalgamation or transfer of the engagements of a society on certain specified grounds.</td>
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<td>Section 50: complaints about investigations into breach of Code of Health and Disability Services Consumers' Rights</td>
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<td>Section 87A: appeal against conditions of repayment and interest</td>
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<td>Board</td>
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<td>Land Transfer Act 1952</td>
<td>Section 216: review of decision of Registrar</td>
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<td>Land Transfer (Computer Registers and Electronic Lodgement) Amendment Act 2002</td>
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<td>Section 98B: appeal against order prohibiting sale or disposal of vehicle (where person charged with an offence and confiscation of the vehicle is a mandatory sentence)</td>
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<td></td>
<td>Section 101: appeal against suspension of drivers licence</td>
<td>On grounds person was not the driver of the vehicle at the relevant time; or the enforcement officer did not have reasonable grounds of belief as required</td>
<td>Land Transport Agency</td>
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<td>Section 102: appeal against seizure and impoundment of vehicle</td>
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<td>No appeal</td>
<td></td>
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<tr>
<td>Marine Reserve Act 1971</td>
<td>No appeal (except general rights of appeal against criminal offences)</td>
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<tr>
<td>Maritime Security Act 2004</td>
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<td>Section 89: appeal against certain decisions (Minister’s decision to refuse, revoke, or suspend a consent or approval or add conditions under ss 20, 23, 24, or 35; a decision to issue a notice under ss 36(3) or 37(1) or imposition or variation of conditions; a decision of the Medical Review Committee under s 88)</td>
<td>Minister, Medical Review Committee</td>
<td>Can appeal if a relevant requirement of the Act or regulations has not been complied with, or the decision that is the subject of the appeal is unreasonable</td>
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<td>Mental Health (Compulsory Assessment and Treatment) Act 1992</td>
<td>Section 16: review of patient’s condition</td>
<td>Family Court judge if possible; if not a District Court judge, plus medical professionals</td>
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<td>National Parks Act 1980</td>
<td>No appeal</td>
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<tr>
<td>Native Plants Protection Act 1934</td>
<td>No appeal</td>
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<tr>
<td>Legislation</td>
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<td>Overseas Investment Act 2005</td>
<td>No appeal</td>
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<tr>
<td>Ozone Layer Protection Act 1996</td>
<td>No appeal</td>
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<tr>
<td>Primary Products Marketing Act 1953</td>
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<td>Protected Objects Act 1975</td>
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<td>Rating Valuations Act 1998</td>
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<td>Reserve Act 1977</td>
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<tr>
<td>Resource Management Act 1991</td>
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<td>Retirement Villages Act 2003</td>
<td>Section 52: resolution of dispute according to statutory dispute process for certain types of dispute</td>
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<td>Securities Transfer Act 1991</td>
<td>No appeal or review rights</td>
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<td>Shipping Act 1987</td>
<td>No appeal or review rights</td>
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<td>Statistics Act 1975</td>
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<td>Director-General or person appointed by Director-General</td>
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The Productivity Commission aims to provide insightful, well-informed and accessible advice that leads to the best possible improvement in the wellbeing of New Zealanders. We wish to gather ideas, opinions, evidence and information to ensure that our inquiries are well-informed and relevant. The Commission is seeking submissions on the questions, findings and recommendations contained in this report by 8 May 2014.