

NRCoP & ANZSOG present

Professor Martin Lodge: Regulators and Risk Appetite

Guest Speaker: Professor Martin Lodge

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Question 1: On the 'Risks' slide I didn't really understand the consequential difference between catastrophic and systemic risk (or as the slide says system 'legitimacy' and 'survival' risks for the regulatory system itself. Isn't a loss a legitimacy also the metaphorical regulatory 'death'?

Answer

In one case, the system itself (such as schools, hospitals, prisons) might in itself be 'destroyed' by the regulatory system and that would be the 'systemic risk' - the catastrophic risk that the regulator encounters an event that delegitimises the regulatory regime (or just the inspection regime).

Question 2: Martin, are you using 'inspection' as a short-hand for the diversity of regulatory activities and tools? If not, it's a very narrow lens.

Answered online by participants

- I agree - inspection is very narrow view of regulatory tools
- I interpreted it as he was referring assessment of risk
- Perhaps seems to be more assurance rather than inspection (inspection is one way to get assurance, but not the only way)

Any further response

I should have been clearer about this - apologies. Risk-based assessments are across regulatory activities - here I was particularly interested in activities of 'detection' (so the activities that are used to 'find out') and activities of 'behaviour modification' (which is enforcement more generally)

Question 3: Can your organisation manage the risks to the level that have been set?" - interesting question. Surely the idea about risk-based approach is a prioritisation that seeks to manage risks as best as possible, but there's always a possibility of risks being realised. and without crises there are likely to be funding cuts to redirections that subsequently lead to risk realisation (reg pendulum in action)

Answered online by participants

- Moreover, risk isn't necessarily a 'bad'. Sometimes we need to seek or embrace risk to be succeed. It needs to inform decision-making in a dynamic way
- Agree - usually any decision is no decision and not making a decision can be riskier than making the "wrong" decision

Any further response

We might officially prioritise that we are 'risk taking' in some areas of our activities, but lack the financial resources to do so.

Question 4: The mixing of the two types of risk - 1) risks to the regulator and 2) the risk to the public/env that the regulator is set up to manage - is really problematic. A regulator needs to manage both but be really clear which one they are talking about at any one time. (I found the questions hard to answer as they aren't clear re which type they are asking about)

Answered online by participants

- Agree. The risks and impacts are completely different for the regulator and regulated entity. It's hard to look at risk and assess risk appetite without knowing if we are assessing using inwards or outwards lens.

Any further response

These are good points - the main discussion point worth raising was to what extent the risks to oneself are always enjoying priority?

Question 5: What are your tips for demonstrating impact if you focus on 'near misses'?

Answer

The value of 'near miss' is to be able to challenge and reflect on processes and thereby detect vulnerabilities that otherwise might have remained hidden.

Question 6: Risk based approach to regulation often refers to assessment (among other things), attitudes and behaviours. How would you define these attitudes and behaviours? (for the purposes of reporting good/bad ones that may contribute to risk of offending/reoffending). I see in research lots of mention of attitudes and behaviours - but not much in how to define these.

Answer

The idea is to distinguish between 'capacity' and 'motivation' - and one can then have a 2x2 table that might inform ideas as to how to think about regulatees. Motivation links in particular to ideas of 'reactive gaming', capacity points to issues of resources dedicated to particular tasks. Coming to a judgement on these will be a judgement.

Question 7: I have heard it argued that a lot of legislation around pollution and environmental hazards ought be "removed from the books" because compliance with most of what is prescribed is never checked for, so why have legislation for things if compliance is never checked!

This seems unsatisfactory to me, and I may be missing something in how a government should design good legislation.

Any comments on this?

Answered online by participants

- I think a prohibition in legislation itself could be part of the control on behaviour i.e. the fact it is there, and people know about it can influence good behaviour.
- The claim made was that the regulator looks foolish (reputation risk) if they insist on rules that participants in the risk know are never (or most unlikely) to be checked for, and if non-compliance is detected, the regulator is unlikely to proceed with litigation for. (resource constraints etc)

Any further response

It depends on the issue - and some of the regulatory review activities have thought about it: is there 'no point' in these provisions (e.g. no harm) then maybe one may want to think again. However, if harm is potentially there, then ex post measures might be sufficient rather than ex ante inspection.

Question 8: Martin - doesn't a choice to avoid taking on the most litigious regulated party (not quite your words) set the incorrect scene for achieving a greater level of voluntary compliance across the whole regulated parties? Doesn't a risky case hold merit if it clarifies the law for all that are within the system?

Answer

These are the sorts of questions that one will have to ask oneself - what are the wider repercussions on the system from taking any one entity on.

Question 9: A big part of our role as a regulator is to ensure that our duty holders understand and appropriately manage their own risks (specifically risks to safety, and to the environment). Can you comment on examples you've seen where regulators successfully avoid risks as they have been successful in ensuring the duty holder carry the risk?

Answer

The whole idea of 'enforced regulation' is the regulated entities manage themselves. However, that is a separate issue of identifying the risks that the regulator has to manage.

Question 10: Martin, firstly thank you for your discussion. Do you have a definition of 'risk' that can be consistently applied by regulators? I find everyone has a differing application of the term which does not aid in consistency.

Answer

The standard definition would be somewhere around impact and probability of an averse event occurring. However, this assumes that we can calculate those somehow. And of course the question is what to do with emerging and other low-scoring risks.

Question 11: How could an organisation best manage the transition to better/improved risk-based regulation, if currently in an environment that is closer to the 'engine of anxiety' scenario where regulated entities are highly reactive?

Answer

It needs a 'reset' that is partly requiring an emphasis on a regulatory conversation with the sector. This is of course easier said than done, as the 'engines' for the 'engines of anxiety' might not be driven by the organisation itself. Here it might be good to pick some 'success cases' of the sector where a confident engagement with the regulatory framework does lead to successful outcomes (not just in a regulatory sense).

Question 12: I recommended many authorities to act against economic actors on the basis of easy to detect formal non-compliance, assuming that this approach eliminates also many economic actors who trigger high concern non-compliance and thus risk (of products in my case). Was I right? Is there a correlation between formal non-compliance and risk?

Answer

It depends on what the impact/probability of the averse event is that non-compliance is about. And then it is about the type of actors are identified as being non-compliant.

Question 13: What level of resource and sophistication are recommended to be allocated towards 1) Elaborating upon potential Risks 2) 'Game Planning' response

Answer

Any form of 'challenge' to existing ways of working is resource-deflecting from operational activities and might also be seen as potentially challenging leadership priorities. However one organises such reflection activities, they are however important so as to support organisational learning.

Question 14: If the regulator only investigates/prosecutes what it sees as the highest risk cases/incidents/situations, is there a risk that stakeholders who may be participants in the risk learn that as long as they don't transgress too badly, they will go under the radar and be ignore by the regulator with limited resources?

Thus, the most egregious players get named and shamed and punished but a lot of small transgressions get ignored. Yet there may be a "long tail effect" – the cumulative impact of all the small transgressions may be significant over time.

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Answer

That is one of the main problems with risk-based frameworks that are too rigid. It is therefore important to 'mix it up' - have a few 'random' non-risk based inspections, for example. One may want to reconsider ones' framework too if the overall effect of being risk-based is a rise in 'lower level' risks - and as the safety literature would highlight, it is usually the aggregation and incubation of small risks that lead to an averse event.

Question 15: What publications/reading might we consult next?

Answer

A good starting point is this:

Baldwin, R and Black, J (2016) 'Driving priorities in risk-based regulation: what's the problem' Journal of Law and Society, 43(4): 565-95.