Regulatory Approaches, Models and Tools Quick Guide

REGULATORY PRACTICE ESSENTIALS

At a glance

Regulators are responsible for effective regulatory outcomes, managing their resources efficiently and being accountable to the public. Having an approach helps them to prioritise their efforts while managing finite resources.

What are regulatory approaches, models and tools?

Approaches are a set of principles and objectives that guide the way a regulator carries out its work. Approaches are based on one or more models tailored to a regulatory system, context and challenges.

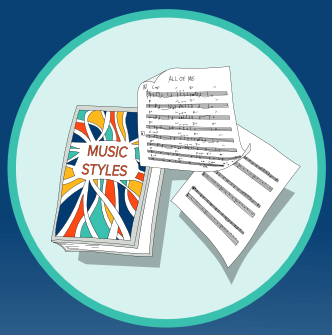
Models are theories developed by experienced practitioners and researchers that guide thinking about regulation. They explore the challenges regulators face and seek ways of understanding and resolving them. Models help regulators think carefully about their work, role and how to achieve their objectives.

Tools are the practical methods that people doing regulatory work use to do their job. Regulators create, adapt and use tools to align with their approach.

Ministry for Regulation
Te Manatū Waeture

Regulation is like performing in an orchestra

People who do regulatory work play a part in delivering something complex, purposeful and for the public benefit.



Regulatory models are like musical styles: classical, jazz, rock. They're developed by experts and used by regulatory leaders to think about how the whole system works together. They offer broad guidance.

Regulatory approaches are like the conductors; they decide how to apply the models based on context, audience and purpose. Regulators might blend responsive and risk-based models to suit the environment and objectives. Approaches are set by regulatory leaders and used by regulated parties to understand the priorities and what to expect.

Regulatory tools are like instruments. These are the practical methods used by regulators to deliver the approach in real-world situations.

What are approaches?

Approaches are a set of principles and objectives that guide the way a regulator carries out its work. Approaches are based on one or more models tailored to a regulatory system, context and challenges.

Approaches, models and tools are connected. When choosing their approach regulators look to models about regulation. Once they decide on an approach they use tools to put their approach into practice.

Regulatory models

Regulatory models are theories developed by experienced practitioners and researchers that guide thinking about regulation. They explore the challenges regulators face and seek ways of understanding and resolving them. Models help regulators to think carefully about their work, role and how to achieve their objectives.

Models evolve to reflect trends and issues in the political, social and economic environment. Each model has strengths and weaknesses and is more effective in some contexts than others. In practice regulators often use one or more models when developing their approach.

Models help regulators understand how the different functions in their system work together. They can build understanding of how other regulators are responding to similar environmental factors.

Models can be grouped into themes that reflect how they evolved.

These are:

a. **Responsive, smart and really responsive regulation:** These models focus on regulators responding to a regulated party's behaviour and willingness to comply.

b. **Problem based and risk-based regulation:** These models focus on the regulatory risk or problems that need to be solved.

Responsive, smart and really responsive regulation

Responsive Regulation

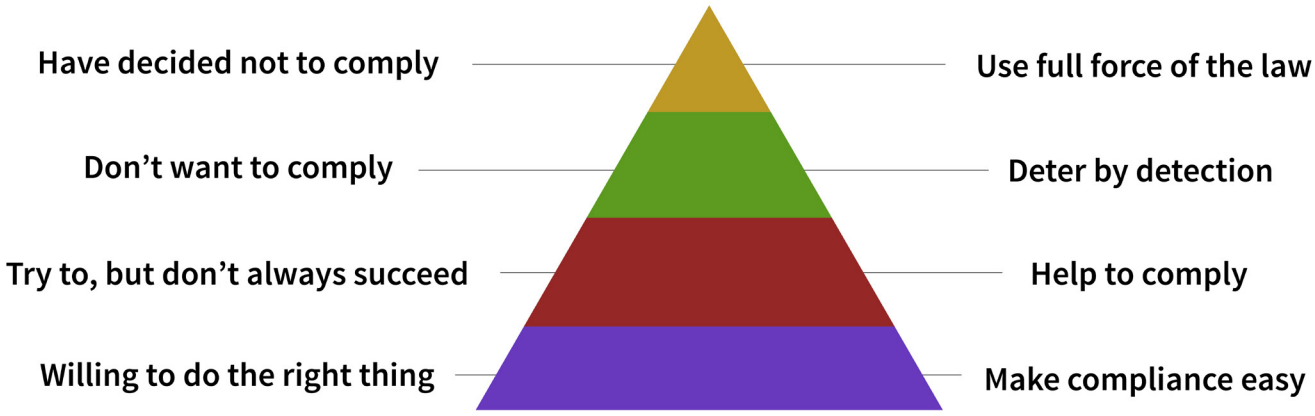
Ian Ayers and John Braithwaite (1992)

The responsive regulation model outlines a range of responses that align with regulated parties' willingness and ability to comply. When they use this model regulators use cooperative measures to achieve compliance escalating to stronger enforcement where needed. This ensures their responses are proportionate, flexible and effective. The Braithwaite pyramid (also known as the compliance or enforcement pyramid or triangle), featured on the following page, shows the different tools regulators use to achieve compliance.

At the base of the pyramid regulators focus on making compliance easy through education, guidance and user-friendly processes. At the next level are those willing to comply if it benefits them. The regulator uses persuasion tools such as targeted education and incentives for this group. For those who resist compliance regulators escalate their response using warnings, fines and other legal penalties.

The pyramid is not a rigid sequence. Regulators intervene at a higher level where non-compliance is serious or there is risk of harm. When compliance is achieved their responses move back down the pyramid. Having strong sanctions at the top signals the regulator's willingness to act and encourages compliance at lower levels.

Braithwaite pyramid



The pros and cons: Responsive regulation is logical and easy to understand.

However, some regulators don't have the regulatory powers to intervene at all levels on the pyramid. There may be barriers to using powers such as time, cost and the degree of public interest. Some responses have unintended consequences, for example, a threat of prosecution may limit people speaking up to report incidents.

This model assumes that regulators have an accurate understanding of regulated parties and the regulatory environment. In practice they may not have a full view nor have the resources to know and assess all the parties they regulate.

Smart Regulation

Gunningham and Grabosky and Sinclair (1998)

Smart regulation builds on the foundations of responsive regulation and the Braithwaite pyramid. Smart regulation recognises that regulators don't act alone. Other groups such as industry bodies, non-government organisations, businesses and international organisations influence regulated parties. These groups use tools such as education, information, peer pressure, rules or standards to encourage people to comply.

In this model part of the regulators' role is to be a facilitator. They use tools that work in tandem with these other groups. They escalate responses up the pyramid where needed filling in any gaps and links between the layers rather than duplicating responses. For example, a professional association may have a code of conduct and educate members to encourage compliance. Where a regulated party does not comply the regulator intervenes with warnings, fines and legal penalties.

The pros and cons: Smart regulation recognises other groups and their tools work alongside the regulator to influence behaviour. It enables the regulator to be 'smart' about the way it uses resources and tools.

In practice smart regulation takes time to implement and co-ordinate. The tools the regulator uses may work against the tools of other groups. The regulator may not have the range of tools needed to fill the gaps or the information they need.

Really responsive regulation

Julia Black and Robert Baldwin (2008)

Really responsive regulation recognises an even wider regulatory environment. By thinking about how this influences behaviour, regulators can really adapt their response.

Regulators should consider:

1. **Regulated parties:** Many factors influence regulated parties' behaviour and willingness to comply. For businesses these may be pressure to be profitable, pressure from competitors, their reputation, whether they see the law and regulators as fair.

2. **Regulators:** Organisational structure, culture and resources impact the way regulators work. Factors outside their organisation such as political influence and overlapping systems have an impact.
3. **Regulatory tools and strategies:** Problems arise when a regulator uses different responses in similar circumstances or when different regulators in the same system use conflicting responses.
4. **Performance of the regulatory system:** Regulators need a culture of learning, good evaluation tools and effective leadership within their organisation for the system to work well
5. **Changes in the regulatory system:** A really responsive regulator is aware and responsive to change. Changes may be new risks, developing markets and technologies, changing political and public expectations.

When regulators have a view of these elements they get a picture of everyone's motivations to act in certain ways. This leads to better decisions about the way regulators respond.

The pros and cons: This model reduces blind spots and surprises for the regulator making it well-suited to complex and evolving challenges. It helps them to consider the role of their own culture in difficult regulatory issues.

Really responsive regulation can be costly and difficult to maintain. More than other models it relies on transparency and being able to adapt. Despite these challenges, when applied well, this model helps regulators stay agile, informed and effective.

Problem based or risk-based regulation

Problem-based regulation

This model requires regulators to select a problem and put resources into solving it. Malcolm Sparrow (2000) said that regulators should pick important problems and solve them by managing the risk. The next step is to report on how well they solved the problem.

This model focuses on developing responses that are tailored to addressing a problem. It differs from responsive regulation which focuses on the regulated party or uniform responses.

Risk-based regulation

Christopher Hood (1980s–2001) and Michael Power (1997); Malcolm Sparrow (2000)

Risk-based regulation focuses on identifying and prioritising the greatest risks of harm. The regulator targets resources to the highest areas of risk.

Identify and assess risk: Regulators identify and study the risk of harm or danger to the public, environment or economic stability. They develop a framework for assessing and scoring risks usually based on the degree of the potential harm and the probability of it occurring. They use intelligence i.e. they collect, collate and analyse information to gain a deep understanding of the risk.

Allocate resources: Once they clearly understand the risk regulators put their effort and resources into designing solutions that modify or reduce the risk and support better outcomes.

Sparrow compares risk-based regulation with knots. When you try to unravel a knot (the risk of harm) you study the knot carefully to see how the strands are woven (assess the risk). You form a plan to work out how to take the knot apart (or reduce the risk of harm happening).

Keeping an eye on the horizon: Just like knots, when regulators reduce the risk of harm, new risks (or knots) may arise. This may be due to changes in technology, product development, changes in public expectations and government priorities. Regulators need to keep watching for new problems or risks. They need to be flexible and adapt where they put their efforts to address these.

The pros and cons: When regulators proactively target risk they prevent harm before it occurs. In the long term this has the greatest benefit to society and costs less. It helps to reduce inefficiency by placing less effort into problems that create less harm to the public or the environment.

In practice a risk-based model poses several challenges.

Risks can be difficult to assess and the causes of harm can be complex and hard to predict. Regulators need reliable and valid intelligence which may not always be available. There is also a risk that visible or politically charged issues attract more attention even if other, less prominent risks pose greater harm.

Risks are events that might occur in the future. When they don't occur it can be difficult to show this was the result of the regulator's actions. When regulators focus attention on the greatest risk, less urgent, but still important problems could be missed.

Other regulatory models

There are many other regulatory models. These are used more often internationally. Some apply to designing regulatory systems while others focus on the practical work that regulators do.

- **Meta-regulation or management-based regulation:** Regulators require businesses to develop internal systems to manage risks rather than relying on external rules. The regulator assesses these systems for design and use.
- **Outcome-based cooperative regulation:** Regulators set desired outcomes, for example, lower environmental impact and give regulated parties flexibility on how to achieve them. The regulator measures whether outcomes are achieved.
- **Command and control regulation:** This model focuses on using strict rules for how the regulated party will act. This leaves little room for flexibility. Given there is often high risk there are high penalties.
- **Performance-based regulation:** Regulators set performance goals rather than detailed rules. This allows regulated parties to innovate while achieving desired results. Regulated parties are rewarded for good performance with lower requirements, for example, less auditing.
- **Principles-based regulation:** Regulators provide high-level principles that regulated parties must follow. This allows for flexibility and innovation. It also requires strong enforcement tools and good judgement.

Why do we need approaches?

Approaches help regulators to:

- **Be transparent:** Communicating their approach builds a reputation for being honest. It gives clarity on their priorities which builds trust and shared understanding with the public.
- **Be accountable:** Taking responsibility for their decision-making builds a reputation for being ethical and reliable. It supports regulated parties to challenge the process which leads to improvements.

- **Communicate expectations:** Clarifying roles and responsibilities of those in the regulatory system helps regulated parties know what's expected of them and what they can expect from the regulator.
- **Focus their resources:** Targets their finite resources where they will have the intended impact. Approaches help regulators organise their people, resources and processes. They provide a structure for regulatory decision-making and compliance.

Choosing an approach

Regulators may select one or more models or integrate several models to create the right approach for the context. Regulators who manage several regulatory systems within their organisation may have different approaches for each system. When choosing an approach regulators need a deep understanding of their regulatory environment. They think about the system and its objectives, the culture they wish to promote, the degree of potential harm and how likely it may occur. They consider their finite resources and the range of tools they can use. They think about regulated parties and how easy is it to reach them.

For example, systems that manage high risk of harm such as threats to life, public safety or environmental damage are more likely to adopt a risk-based approach. A really responsive approach is used where regulators work closely with regulated parties or need to stay alert to changes in the regulatory environment.

Most regulators in New Zealand choose an approach that draws on several models. For example, both risk-based and responsive. This means they accept some areas of non-compliance have less risk and do not move up the pyramid to enforcement every time.

When a regulator changes their approach they make policy and practice changes that align with the new approach. For example, it may lead to new information systems, changes in licensing or the way it organises its people.

VADE (Voluntary, Assisted, Directed, Enforced) is an approach often used in New Zealand. It builds on the responsive regulation model. VADE outlines engagement tools that align with compliance behaviour. It moves from education and guidance to assisted support on to warnings and finally penalties for serious breaches. This approach ensures proportionate responses.

Regulatory tools

Tools are the practical methods that people doing regulatory work use to do their job.
Regulators have a range of tools such as an investigation, reporting or compliance and enforcement tools used to deliver their functions.

However, tools have another story to tell. They reflect an approach adopted by the regulator. For example, advisory or warning letters are a common tool. How and when they are used depends on the approach.

- A **responsive regulator** tailors their tools to the behaviour of the regulated party. An inspector might issue a warning letter to a regulated party who they assessed as unwilling to comply. The letter escalates the response from an inspection to a warning. If the regulated party responds well the regulator moves their response down the pyramid.
- A **risk-based** regulator uses audit trends or complaints data to identify a pattern of risk for a group of regulated parties. The regulator will send letters to the group to remind them about the law. These letters are intended to prevent harm before it occurs.

What you can do to learn more about approaches, models and tools

- Talk to your manager about the regulatory tools your team uses. Can you identify the approach?
- Learn from senior colleagues about how approaches and tools shape decision-making in your regulatory system.
- Review your organisation's compliance and enforcement strategies.
- Explore approaches other regulators use. Read information on their websites about their approaches and tools. Can you identify the models they have used when choosing their approach?
- Reflect on your work – What tools do you use? What's missing from your toolkit? When could you apply different tools and what support would help?

Resources

↗ An international conversation with Professor Julia Black. Ministry for Regulation Te Manatū Waeture (Feb 2024) (You Tube, 53 mins)

↗ A conversation about responsive regulation. Ministry for Regulation Te Manatū Waeture (Sept 2022) (You Tube, 56 mins)

↗ Responsive regulation. John Braithwaite (2016)

↗ Responsive regulation in practice, a review of the international academic literature. Victoria University of Wellington. Professor Jereon van der Heijden (July 2020)

↗ Tools we use to regulate (VADE model). New Zealand Petroleum and Minerals, Ministry of Business, Innovation and Employment Hīkina Whakatutuki (Nov 2022)

Got questions? Get in touch

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