

# High performance regulators: The issues

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# Regulators

- Instead of public sector production or a government scheme, regulation is often a sensible path: A private industry actually does the production, but their behaviour is modified through regulations
- Many regulators have come up in India, at both Union government and state government
- Many areas of concern about their performance

## Three solutions that are not

**Firefighting on one problem at a time** We think FSSAI went wrong on Maggi noodles, we put in time and trouble to fight with this one problem.

**Appointments process** When the institution is weak, we think we will overcome this by hiring a hero. Sad is the land that needs a hero.

**Objections to mindset/culture** Percy Mistry's law: Mindset is endogenous to organisation design. Let's go deeper and find the actionable solutions.

Why are intelligent people coming up with the wrong answer?

The key tool for progress is process improvements. High performance organisations deliver results through organisation design

# Part I

## Elements of a high performance regulator

# Components

- 1 Clarity of purpose
- 2 Role and composition of the board
- 3 Legislative process
- 4 Executive process
- 5 Judicial process
- 6 Reporting, accountability
- 7 The role of the department

# E1: Clarity of purpose

- Each agency must have clarity of purpose
- There can only be accountability if there is clarity of purpose.

# E1: Indian examples

- TRAI: Fair clarity on objective
- RBI: An improbable mix of conflicting functions.
- IBBI: Good clarity on objective

## E2: Role and composition of the board

### Functions of the board

- 1 Initiate and approve all law
- 2 Design the organisation: organogram, processes
- 3 Establish targets, run the budget process
- 4 Hold the management accountable.

### Composition

- 1 1 chairman + 2 executive board members
- 2 1 representative of the parent department
- 3 5 independent board members.



## E2: Indian experiences

- None of the boards in India are properly structured.
- SEBI: The role and function of the board is fairly good, but there are loopholes.
- RBI: The composition of the board is good but it has no role.
- IBBI: A failure on board structure.

## E3: Legislative process

- 1 All law should be only one legal instrument: “a regulation”
- 2 All regulations should only commence from an instruction from the board
- 3 The management must make a documentation packet:
  - 1 What is the problem we seek to solve?
  - 2 Is it a market failure?
  - 3 What's the proposed intervention?
  - 4 Does the proposed intervention address the claimed market failure?
  - 5 Cost benefit analysis: Do the benefits outweigh the cost? Was there an alternative intervention which would get the job done at a lower cost to society?
  - 6 The draft regulation
- 4 Put this packet for public comment for  $\approx$  a month
- 5 Management must respond to all the ideas from the public
- 6 Go back to the board for a discussion
- 7 Board approves the final regulation for release
- 8 3 years later, a post-mortem.

## E3: Indian experience

- TRAI has a fairly good regulation making process
- AERA is also okay
- All the others are pretty bad.
- *Regulatory responsiveness in India: A normative and empirical framework for assessment*, Anirudh Burman, Bhargavi Zaveri, October 2016.
- Supreme Court on TRAI and calls dropped regulation.

## E4: Executive process

- Licensing, investigation, prosecution
- Formal procedures for all these
- Analogy : Criminal procedure code, Police Acts.
- Denying a license imposes harm upon the applicant: requires a reasoned order and possibility of appeal.

## E4: Indian experience

- All being done pretty badly.
- SC on coal has implications for licensing by all parts of the Indian State
- *Payment bank entry process considered inconsistent with the rule of law*, Shubho Roy and Ajay Shah, September 2015.

## E5: Judicial process

- The accused should get an SCN and an opportunity to present his facts
- A small hearing where a neutral person hears the prosecution and the accused
- A reasoned order
- Fairness in punishments
- Possibility of appeal: Tribunal and then SC.

## A peculiar problem in India

- Elsewhere in the world, regulators fuse legislative and executive powers
- In India we have placed judicial powers also
- This is an extreme violation of the separation of powers doctrine
- This makes it even harder for us to build sound regulators in India
- FSLRC solution – a separate vertical headed by an Administrative Law Member.

## E5: Indian experience

- All being done pretty badly.
- At SEBI: The use of 'ex parte orders' to jump steps: punishment without trial
- Highly inconsistent punishments
- SAT works pretty well, even though the processes are bad
- At RBI: No due process, no reasoned order, no appeal.
- IBBI: separate vertical has been implemented.



## E6: Reporting, accountability

- Operational metrics must be reported, that are under the control of the management
- A target-setting process to make an improvement every year
- Linked to the budget process.
- This also requires functional thinking about the budget.

## E6: Indian experience

- Not being done.

## E7: The role of the department

- 1 Give regulators the requisite authority in the law
- 2 Appoint all the members of the board
- 3 Use your membership on the board to be a full blown board member: participate in regulation-making, budget-making, targets, performance, organogram, process manuals.
- 4 Stay out of executive and judicial functions.
- 5 Do not entertain complaints from private persons about executive and judicial actions of the agency
- 6 Department is the Principal. Must constantly ask how the Principal-Agent relationship is working, constantly modify the contract (i.e. the law), and modify the work given to different agents.

See: *Ministry vs. regulator: How to draw the lines*, October 2016.

## E7: Indian experience

- The department asks for favours on executive and judicial functions
- And cedes power on all the other things
- A notion of turf arises.

# Recapitulate: Components of a high performance regulatory organisation

- 1 Clarity of purpose
- 2 Role and composition of the board
- 3 Legislative process
- 4 Executive process
- 5 Judicial process
- 6 Reporting, accountability
- 7 The role of the department

# Major developments in the Indian story on regulators

- Justice Srikrishna, *Financial Sector Legislative Reforms Commission* (FSLRC)
- Has drafted *version 1.1 of the Indian Financial Code*.
- Has 140 sections which setup a regulator – useful for all laws that setup regulators
- MOF has created an '*FSLRC Handbook*' for voluntary adoption of good governance practices by regulators until the IFC is enacted. And a *MIS procedure for tracking compliance*.
- Present state of implementation is roughly 0.
- MCA *Working Group on establishment of IBBI*, chaired by Ravi Narain, on the processes of setting up a new regulator.
- Skills regulator, early stages at Ministry of Skills.

Thank you.

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