

THE PARADOX OF REGULATION



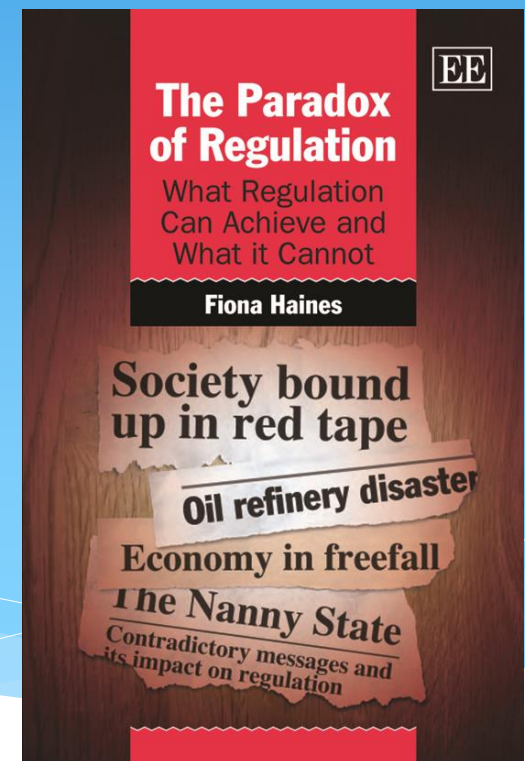
THE UNIVERSITY OF
MELBOURNE

What regulation can achieve and what it cannot

Professor Fiona Haines

School of Social and Political Sciences

University of Melbourne



Never Again!

- * I want to finish by reading the words of the commissioners, with which the Government is in complete agreement: **“The lessons from the Pike River tragedy must not be forgotten. New Zealand needs to take urgent legislative, structural and attitudinal changes if future tragedies are to be avoided. Government, industry and the workers need to work together. That would be the best way to show respect for the 29 men who never returned home on 19 November 2010, and for their loved ones**
- * *Hon CHRISTOPHER FINLAYSON (Acting Minister of Labour) Nov 6 2012* http://www.parliament.nz/en-NZ/PB/Debates/Debates/8/2/a/50HansD_20121106_00000008-Urgent-Debates-Pike-River-Mine-Disaster.htm

The pursuit of 'good regulation' begins

*but:

- * what is understood as good regulation?
- * how does it emerge?
- * and what does it target?

Good regulation: How much?

* Less:

- * “Like a smouldering fire the Liberals let the deregulation agenda in this country lie dormant for most of their eleven years in office. I intend to re-ignite it.” Lindsay Tanner
Former Finance Minister (ALP),

* More:

- * “She was a born-again deregulator” (Darien Fenton (NZ Labour) criticising Kate Wilkinson, NZ Nationals)
- * “... it is extremely clear that it is the failure of the regulatory regime, of the Government as regulator—it is the failure of deregulation—that has led to a situation where this company, Pike River Coal, could take those catastrophic risks.” (Kevin Hague NZ Greens)

Good regulation: by whom?

- * The state

- * “this is not the time to fire the police force...” (Alfred E. Kahn following the Savings and Loans Crisis)

- * The market

- * “... even an imperfect market produces better results than arrogant experts and grasping bureaucrats”, (GW Bush former US president)

- * Or in between:

- * ... we also need a robust analysis of the social-democratic approach to properly regulated markets and the proper role of the state, ... Kevin Rudd, as former Australian PM

Good regulation is

- * An oxymoron
 - * public choice economists
- * “light handed” subjected to a “survival of the fittest” reform process
 - * view from regulatory reform bureaucracies
- * Effective and tough minded, flexible but just
 - * Regulation academia
- * Regulation is partly scientific/technical (or problem solving) but largely political:
 - * In design
 - * In its goals

How does ‘good regulation’ emerge? (targeted at what?)

- * Focused on an “undesirable risk” in the wake of adverse events:
 - * Explosions, fires
 - * Deaths, diseases
 - * Terrorist attacks
 - * Financial meltdown
 - * Global warming?...
- * Perception that regulation acts like a ‘surgical bombing raid’
 - * removing the ‘risk’ whilst maintaining the reward

But what is risk?

- * Risk not singular:

- * **Actuarial risk**

- * Impact and probability of the realization of *a given category of risk outside of the self*. Understood as a ‘Technical/scientific’ risk problem
- * Dominant form of risk as understood by ideas behind “smart regulation”

- * **Socio-cultural risk**

- * Concerns individuals have about their society and their identity (Durkheim).
 - * Recognition of interdependence
- * Risk given significance and meaning by society itself (Douglas)
 - * Risk is not calculable in the same manner as actuarial risk, but categories tied in to social order

- * **Political risk**

- * (Habermas) Arises when governments fail in their core activities of:
 - * promoting entrepreneurial activity (keeping the economy going)
 - * Providing conditions for capitalism to flourish
 - * Reassurance (making people feel safe)
- * *Two elements in tension with one another*

But:

- * Each risk is ‘ideal typical’
 - * With a different focal concern
 - * Subject to a risk assessment
 - * that may be more or less accurate
 - * and subject to systemic distortions
- * Should *not* be conflated
 - * Are both independent and interdependent
- * Political risk dominant
 - * Frames the response
 - * Shapes the perception of risk
 - * To place the government as protector

Reform Paradox: Longford

- * Victoria – the regulator’s nirvana
 - * Meta-regulation: Safety case ‘+’
 - * In the context of the failure of Industrial Manslaughter
- * NT – proportional to risk?
 - * But heavily dependent on industry being both responsible and knowledgeable
- * NSW
 - * Little or no political risk attached to doing anything about MHF regulation
 - * Debates in parliament largely around ‘red tape’ and ‘terrorism’ – and pit bulls
 - * Little support for the regulator
 - * and the regulatory regime divided
 - * Lots of committees, lots of ‘problem solving’ but few resources and little action

Reform Paradox: 9/11 at ports and airports

- * Do it yesterday!
 - * “(There is) the constant need to amend the legislation and regulations. **I mean, if industry thinks its bad [complying with regulations], try writing the damn stuff**”
- * Pleasing the Minister
 - * **at the end of the day the public servants aim: what’s the Minister’s reaction going to be to this?** And I guess I don’t really care if for my friends in tax (or) if the treasurer said this is a crummy proposal or this is a ridiculous method of regulating this ...
- * “We started a new empire”

Reform Paradox: Finance ASIC/APRA.

- * Confidence ‘reassurance’ critical in financial regulation
 - * *Perception* drove ‘success’
 - * Reform designed to reinstate trust and confidence
 - * Transparency/accountability/independent oversight emphasis in CLERP 9
- * But regulators not the only influence:
 - * ‘...pressures from shareholders and financial markets for performance... are overwhelmingly strong’ John Palmer 2002
- * Leading to pushback
 - * Three years have passed (since HIH) and now we’re still implementing or trying to implement change in relation to that, but the climate’s changed ...
 - * Demand for ‘certainty’ by industry
- * Prudential regulation supported/protected by public interest mandate (protect the policyholders)
 - * Requirement for premiums to cover payouts (‘de-financialisation’)

Implementation Paradox: Major hazards (Vic)

- * Good implementation requires communication – but communication is a *social* activity:
 - * I'll sit in the meeting and the site manager would just go bang, bang, bang! But being part of the process and knowing some (of the acronyms) you could actually get a gist of what they're going. But sometimes you sit back and go, "I didn't understand a word you said" and just bide your time and it's obviously above what we need to know. (21, p7)
- * Showing up ignorance makes you unpopular – with everyone!

Implementation Paradox: Security

- * Implementing measures to fight the last war
 - * Development of an always unstable narrative
 - * Consistent increase in demands for security in line with political expectations
- * And keeping the airlines flying
 - * Creating a 'sense' of security
 - * “... **even the palisade (high security) fencing will only stop people for about ten minutes.**” (45, p28)
 - * Screening and cargo
- * Always patchy implementation
 - * “(small airport) has got a security system and **they’ve actually left a spot where you can climb up onto a step and skirt around a piece of steel to get in, because otherwise you can’t get off the airport.**” (47, p9)
- * Powerful regulations! Can use keep out troublemakers e.g.:
 - * Unions
 - * Meddlesome politicians

Implementation Paradox: Financial collapse

- * As a result of change in accounting standards (AIFRS)
- * Assets come:
 - * As a result of that our assets went from \$40m to \$180m ... It looked like we grew our business overnight by \$130m...
- * Assets go...
 - * Counting every nut and bolt a waste of time... **“5% of our equipment in the stores are big ticket items worth, worth about 80% of the costs, yet, [the auditors] were telling us, you have to count everything. So we’re counting these little washers worth a dollar each, 50 cents each and we’re going – hang on, this is crazy!”**
- * And assets shift in time and place (Hedging)
 - * We’ve reached agreement with our board given where the Australian dollar is, where the oil price is, we thought hedging was a good idea, so we’ve hedged a particular layer of risk, which we haven’t in the past.... We’ve engaged [accounting firm] to help us account for it appropriately. So it’s significant dollars, but again there are only zeros at the end of the numbers. **Once the processes are in place, whether you’re talking two million or a twenty million [it’s fairly straightforward]. At the moment I think we’ve got a hundred million of a particular currency. But again they’re only numbers.** (44, p24)
- * A set of financial accounts:
 - * Result from ‘craft’ activity
 - * **are only ever an approximation of company value – a “best guess”**
 - * Close connection between actuarial and socio-cultural risk in finance

Never again becomes Oh No!

- * Reform paradox
- * The 'master risk' is political
 - * Keep the economy going,
 - * Managed by listening to business, modifying demands
 - * make people feel safe (socio-cultural)
 - * Temptation to go for symbolic change
 - * Criminalisation
 - * Quick fix solutions
 - * Use of 'policy based' evidence
 - * Deflect attention onto a different 'problem'
 - * – terrorists, asylum seekers – in the case of MHFs in NSW deal with the pit bull terrier problem
- * Actuarial risk is expendable

Compliance Paradox

- * Compliance also requires dealing with all three risks
 - * Reducing the (actuarial) hazard
 - * Engendering respect for co-workers, managers (addressing socio-cultural concerns).
 - * Attuned to sense of order in the workplace
- * Dealing with legitimacy risks to the business
 - * Profitability
 - * Reassurance (of the market, of other stakeholders and workers)
- * For 'agency' based actuarial risks 'confidence' of consumers (travellers, investors) critical
 - * So compliance measures on the ground must reassure – but reassurance does not mean they are effective
- * Powerful regulation can be used as a weapon in a local political war as much as a method to reduce an actuarial risk

The paradox of actuarial risk – the limits of instrumentalism

- * Actuarial risks are the ‘problem’ regulators are asked to solve
- * Focus on narrowing, defining
 - * RIS cost benefit/costs to competition
- * Can be powerful – and effective
- * But tight definition without commitment can invite:
 - * Tick and flick
 - * Gaming responses
- * ‘Solution’ is to move to performance standards, broad definition etc but:
 - * Political risk management requires risk *taking*
 - * red (or green?) tape’ pushback
- * Broader institutional change may be required – rather than a ‘surgical bombing raid.’

Never Again?

- * Regulation *can* be critical to the reduction of risk but
 - * It must work at an actuarial, socio-cultural **and** political level
- * In understanding where it can be successful
 - * Content matters
 - * Context matters
 - * Generic prescriptions have their limitations
- * Regulation can promise more than it can deliver
 - * Bit like surgical bombing raids
 - * That gloss over the need for more wide ranging reform

Thank you

***Questions?**



THE UNIVERSITY OF
MELBOURNE