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The complex world of regulators

Independent and continued evaluation of statutory regulatory agencies is necessary and important for feedback to regulators and Parliament

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In many countries, statutory regulatory authorities (SRAs) are now an important organisational mechanism for the state. The departure from the separation of legislative, executive, and adjudicatory branches, by concentrating them into one agency (the SRA), is an important change from the traditional working of government. While SRAs have added value in many respects, they also face questions of accountability and excessive concentration of power.

When such an unusual organisation is set into motion in the body politic and body economic, it is important to be self-aware about how well it is working. Evaluating SRAs is, however, difficult.

In normal times, regulators are criticised for over-regulation, with calls for a hands-off approach. In difficult times, they are pilloried for under-regulation and for sleeping at the wheel. There is a tendency to extrapolate from one publicised regulatory failure to over-broad claims about the overall performance of the SRA. Officials at SRAs constantly seek more power and have a bias in favour of making excessive claims. They suffer from applause by regulated persons and scepticism from the broader community. The achievements of the SRA that do not make headlines, in terms of laying foundations for economic growth or avoiding crises, tend to get ignored.

In 2001, a Joint Parliamentary Committee (JPC) was set up to investigate the stock market crisis of March/April 2001. The report of the JPC presented to Parliament in December 2002 said that "regulators have been found wanting and they do not instil confidence in the investor". The years from the creation of the Securities and Exchange Board of India in 1992 till 2001 were actually a golden age in terms of momentous reforms and laying the foundations of a modern financial market system. This did not attract much public attention as it did not visibly impact the life of the average person. The reprimand of the JPC was, however, the stuff of newspaper headlines.

How can the working of SRAs be better assessed, so as to establish feedback loops through which their working can be improved? In 2013, the Financial Sector Legislative Reforms Commission (FSLRC) recommended a formal mechanism to evaluate regulators through a review committee comprising only non-executive members of the regulator's governing board. The Committee on Reforming the Regulatory Environment for Doing Business in India (2013) recommended that each regulator should undertake self-evaluation once in three years, and place its conclusions in the public domain for informed discussion and debate.

Such performance evaluation can be quite complex. Regulators generally do not have much direct output: Their services are inputs to outputs of the regulated entities and markets. Their performance is affected by several external factors, many of which are beyond their control, and their efforts may take years to have visible outcomes. The data required to make the evaluation may not be easily available. The best skills available in the Indian knowledge ecosystem may not have the capacity to evaluate regulators. The domains in which the diverse regulators operate have many unique features. A systematic strategy of regulatory evaluation can be organised around three groups of parameters: Governance, process, and outcomes.

And then, we turn to the mechanics. How should this be done? *Nemo judex in causa sua*, or nobody should judge their own cause, applies for state agencies. There is a principal-agent relationship between the legislature and the SRA, and the principal should assess the working of the SRA through mechanisms that are distinct and separate from the SRA. One natural line of attack is performance audits by the Comptroller and Auditor General of India (CAG).

Around 22 years ago, after some attempts to audit the Telecom Regulatory Authority of India and some state electricity regulators, the CAG issued guidelines on the audit of regulatory bodies. Essentially the guidelines say that the audit should be within the sphere of the provisions made in the relevant statutes. While the CAG needs to build out the full capabilities to do performance audit of regulators, so far, those capabilities and processes have not emerged. In the present Indian landscape, the natural alternative is to turn to non-partisan research organisations.

For this, a logical option is to establish an assessment cycle where the terms of reference of the evaluation is discussed with the relevant parliamentary standing committee, an external research organisation is given the task of performing the evaluation, and the report is taken back to the parliamentary standing committee. This emphasises the agency relationship between the parliament and the regulator, and feeds into amendments to the law which are required for many reforms of regulators.

One part of the regulatory evaluation consists of examining the actions of the regulator over a stated time period. The second part of evaluation consists of anonymous perception measurement in regulated persons. A private organisation needs to conduct a fully anonymised survey, which measures how regulated persons view the processes and outcomes of the regulator.

The parliament and regulators have begun to respond to this gap in the evolving landscape of regulation in India. An important milestone here is the law on India's most recent financial sector SRA. The International Financial Services Centres Authority Act, 2019, requires the authority to constitute a Performance Review Committee to review its performance annually. Similarly, the rules made under the Insolvency and Bankruptcy Code (2016), governing another young regulator — the Insolvency and Bankruptcy Board of India (IBBI) — have this provision. The rules require that the IBBI carry out an assessment of its effectiveness and efficiency in terms of its objectives and mandate, keeping in view its resources, duties and powers, and an assessment of performance of its governing board and publish this evaluation in its annual reports.

Over the past year, the IBBI has become the first Indian SRA to have commissioned an independent evaluation of its regulatory role as envisaged in the law. In doing this, it has set a benchmark for other SRAs to commission similar regulatory performance evaluations by external academic/ research bodies. The resulting documents have helped the leadership of IBBI think about its strategic road map for strengthening the IBBI. This constitutes an important milestone in the emergence of state capacity in regulation in India.

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