POLITICAL AND REGULATORY RISK

Is it a serious problem? Can it be limited?

REPORT OF THE RISK COMMISSION

The Regulatory Policy Institute's Better Government Programme was established to focus on practical proposals for improving accountability and transparency in UK and EU policy and regulatory processes. Consideration of political risk – uncertainty arising from actions or the structure of policy or regulatory processes – falls naturally within that remit and is topical at a time when considerable attention is being paid to risk assessment and management as an integral part of directors' and financiers' duties.

Following discussions with Whitehall departments, we were prompted to consider three questions:

- Does the policy process create political and regulatory risk?
- If so, how does that risk affect corporate strategy and business investment?
- Is that risk avoidable? If not, how can it be mitigated?

We assembled a group of politicians, former officials and Special Advisers, and corporate and City specialists to work with us in assessing the evidence[1]. This report sets out our conclusions.

There was common agreement on four points:

- That risk is largely a function of the level of external confidence in the reliability of the policy process.
- That actual or perceived uncertainty over the governance and outcome of that process is high.
- That, while some witnesses may perhaps have overstated their concerns, such uncertainty has materially reduced corporate efficiency and inhibited or increased the cost of investment.
- And that the scope exists to improve confidence and reduce uncertainty.

However, some members and many witnesses believed that the evidence strongly pointed towards the need more strictly to define the scope for political involvement in the process. Others stressed the importance of maintaining democratic accountability. Some felt that policy and regulatory institutions are to blame for failing to create mechanisms that might offer greater certainty to those affected by their decisions – as several financiers told us, a bad outcome is one they have not forecast. Others suggested that organisations also bear responsibility for the creation of risk if they fail to keep

[1] The Risk Commission was originally assembled under the aegis of the Social Market Foundation. The work was subsequrntly transferred to the RPI

themselves informed of the system's work or do not have adequate risk management strategies. Some believed that we were insufficiently radical in our selection of proposals; others that we were threatening enshrined constitutional conventions. In considering these shades of opinion we have tried to avoid both unworkable compromises and politically partisan or agenda-based reporting.

Most of the 40 recommendations (which, while focusing on the UK, are in the main equally applicable to EU institutions) we make to address those conclusions have been designed with both business and to the wider public in mind since greater transparency and accountability is of broad benefit. They cover three broad areas:

- Stronger and clearer governance protocols to apply to political, administrative and regulatory decision making

- Greater delegation of decisions to expert bodies

- Processes should seek to provide clearer and longer-term signals covering their direction, content and decision-making criteria

Most are technical; a few will stimulate debate because they invite a decision as to whether a change in some terms of engagement is a fair price to pay for an improvement both in confidence in the process and in the public standing of its decision makers. But in each case there is nothing apart from the system's own culture that would prevent it from implementing this package. At the same time, we have sought to highlight the importance of organisations embracing the monitoring and assessment of political and regulatory risk and accepting that it as just as much a governance requirement as is direct financial risk mitigation.

Both Government and the governed can play their part in solving this problem.

We are very grateful to all those who served on the Risk Commission and the many others who contributed evidence. All of them assisted our work greatly in providing both expertise and a barometer of market opinion.

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What is political and regulatory risk?

1. The term "political risk" has been in use for many years, but it is ill-defined, often misunderstood and rarely assessed. It is most usually considered in an international context as referring to the risk associated with doing business in a foreign country but, while there has been considerable debate over the role of the state as policy maker and regulator, in the UK and EU it has focused on deregulation or "better regulation", with little examination of the way in which the policy and regulatory process influences corporate efficiency.

2. There are many contributors to risk arising from the actions (or failure to act) of governments and regulatory bodies:

- Uncertainty over the timing of decisions and other critical announcements ("we had expected a decision by now; something must be wrong…").

> Analysts reported to us that departmental delay in responding to Ofwat's recent water price review proposals influenced their profit forecasts because it was assumed the delay implied that Ministers would amend the recommended price caps.
>
> Lengthy delays before Ministers approved an overhead power line led to the applicant's financiers increasing the package cost by 0.2% because it was suspected that delay implied concern.

- Lack of transparency or misunderstanding of the process – which can lead to incorrect assumptions (for example, in the power line case cited above, the inability to distinguish between a heavy ministerial workload and active political concern led to financiers suspecting the latter).

- Mistaken assumptions ("politicians are likely to distort evidence").

- Imperfect communication – ("we did not know that…") whether through failure by Government effectively to disseminate policy or regulatory information (for example, on implementation dates), misreporting by the media or intermediaries such as trade bodies and consultants, or failure by organisations to take reasonable steps to inform themselves.

- Uncertainty over the way in which powers and duties will be implemented or interpreted ("will/can they act; how will they act?"). This could arise from incomplete guidance, failure to consider the implications of proposals ahead of reaching agreement to act, or poor communication or assimilation of information.

We received several reports of significantly differing interpretations of regulatory requirements by local inspectors of a major enforcement agency. In one case, an inspector's compliance list would have necessitated £4 million more in mitigation costs than had been demanded by another inspector for a near-identical project

Member States had little idea of how the Directive on the Obligation of Carriers to Communicate Passenger Data could technically be implemented when they approved it early in 2004. Airlines and others still do not know which technology they will have to use to obtain and transmit the data or how much it will cost them in IT resource and disruption.

Financial services companies sought clarification on whether the recently introduced Distance Selling Directive applied to their sector. They explained to Departments and their regulator that marketing of a number of new products had to be postponed in the absence of guidance but were only advised by Government to consult their lawyers. As one bank commented, *"do we go to market and risk a fine if we fall on the wrong side of the line or play it safe and lose sales revenue while we wait for Government to make up its mind?"*

An MP reported the example of a butcher in his constituency who did not know whether under recent anti-BSE EU regulation he could sell bones for pets. He contacted Defra, but it was unable to offer guidance.

- Actual or feared unexpected amendments to proposals or procedures ("the independent expert advice has been published, but will Ministers depart from it?")

Several examples were offered to us of costly amendments being proposed by European Parliament rapporteurs shortly before plenary votes following only limited consultation. In each case, the amendments were subsequently reversed by the Commission or Council, but in the interim they increased uncertainty over compliance and investment return.

- Departure from expectations ("we were led to believe that…but now the Minister has changed his mind")

A pharmaceutical company invested significantly in new pack machines on the basis of a decision announced before the 2001 General Election, only to find post-Election that a new Minister reversed the position.

Having been encouraged to do so by the Treasury with the "promise" of a duty incentive to defray some of the cost, oil companies invested in excess of £300 million (and a lot of uncosted time) in introducing sulphur-free fuels. However, the Duty change was put on hold when the Chancellor became worried about the increase in the price of crude and it was only introduced after a three month delay.

- Shifts in policy due to changes in political priorities or pressure from the public, the media, interest groups, or another political organisation.

> "*Britain's biggest casino operators were apoplectic yesterday after the Government made another U-turn over the Gambling Bill, sending share prices crashing. Having already capped the number of mega-casinos with 1,250 slot machines paying unlimited jackpots to just eight, the Government said it would limit expansion of the two smaller classes of casinos by a similar amount.*
>
> *The news sent London Clubs shares down 35 to 103p, Stanley Leisure down 43 to 433p and Rank down 36 to 260p*."
>
> Daily Telegraph 17 December 2004

- Manifesto risk – commitments made or influenced by Party machines without the benefit of a full evidential or consultative process but which incoming governments required to be implemented.

> Before it entered office in 1997, Labour had committed to supporting the proposed EU ban on tobacco advertising. It confirmed that commitment on taking power even though the only official impact assessment had concluded that there was insufficient evidence that a ban would be effective.

The impact of political and regulatory risk

3. Actual or perceived risk creates uncertainty, which can restrict or delay corporate decision making. It can also increase investment cost, reduce share price, influence financial market views on value, inhibit long-term planning and deter strategic options.

4. But some risk is inevitable as public perception and science and technology changes, and its creation can be useful for Government and may in some ways be less damaging than well-signalled, transparent intervention. A former Minister told us that *"fear that Government may intervene (eg salt, junk food) may be beneficial because it might prompt sectors to take self-regulatory action as an alternative to the prospect (real or perceived) of formal regulation"* [2] It may also be beneficial to the governed: later in this report we cite a case in which risk arose through political questioning of scientific advice that beef was safe; had the scientific advice been restrictive, the industry would no doubt have sought political intervention which would have been regarded (by the industry at least) as potentially reducing risk.

> Business, whether publicly or privately owned, needs clarity about the rules of engagement with Government in its widest sense, including legislative and regulatory risk. If the framework is clear, the company is free to concentrate on managing the risks within its own control or sphere of influence, including the delivery of high quality efficient services to customers. And financiers can assess the risk element in the cost of capital at a proper level, rather than allowing for an exaggerated unquantified risk.
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> Sector regulator

5. And risk can arise from the absence of regulation. The Environmental Industries Commission told us that *"The ETS industry has painful experience of investing in developing solutions to environmental problems on the basis of there being a demand for those solutions, only to find weak enforcement means this demand turns out to be more illusion than reality. Deregulation and weakening of enforcement are, therefore, a major risk to our Members' business plans - and a major reason why City investors are cautious of the prospects of the sector."* Another respondent to our survey (see below) commented that *"The absence of intervention can increase risk: offshore gas prices are going through the roof but lack of transparent information from offshore operators makes it difficult to work out why, and that deters new entrants. By intervening to require greater transparency, DTI could reduce their risk."*[3]

How great a problem is it?

6. As we comment above, few attempts have been made to assess the extent to which political and regulatory risk influences markets:

A survey commissioned from the London School of Economics[4] among FT 250 directors revealed that 96 per cent of the sample believed that regulatory risks have increased in recent years and will continue to grow (this broke down as Health & Safety/Environment - 92%; Competition - 84%; financial services - 84%; Data Protection - 80%; company law - 52%; and product safety - 60%).

- In the same year, a survey among a broad range of companies and trade associations, corporate financiers, analysts, fund managers and venture capital bodies by Policy Analysis Group[5] assessed that 74% of the 264 respondents regarded the forecasting of political and regulatory risk as "highly significant", with only eight per cent considering it to be "not very significant". There was a noticeable difference between corporate/trade association and City responses, with the City showing markedly less concern:

	Corporate/trade association (%)	City (%)
Highly significant	88	55
Fairly significant	10	21
Not very significant	2	24

7. In order to examine this area in greater depth, following discussions with the Department of Trade and Industry and Treasury, we established a Risk Commission, inviting Departments, politicians, former officials and Special Advisers, business and City representatives (see Annex 1) to participate.

[3] This was recognised by DTI which negotiated a voluntary scheme for transfer of information, some of which is now published market – see *Offshore Gas Production Information Disclosure*, Ofgem February 2005

[4] *Rethinking Regulatory Risk*, DLA 2002

[5] *Sources of information about risk*, Policy Analysis Group 2002

The impact of information asymmetry

In traded commodity markets it is crucial for market competition and liquidity that all participants have access to relevant information on the background rules and their application. However, there are several examples of the application of regulation which leads to information asymmetries between market participants which both increases risk and reduces competition and liquidity. Three examples about the application of existing legislation spring to mind:

- When Ofgem was considering the Market Abuse Licence Condition, TXU sought "confidential guidance" on its application to the planned closure of a significant portion of its generating capacity. Having received the green light from Ofgem, it bought significant amounts of power prior to the announcement of the closure. Market prices rose significantly after the closures were announced and parties on the other end of the TXU purchases lost significant amounts because of their ignorance of a regulatory decision taken in private and known to only one participant. When challenged on this, Ofgem defended its right to discuss privately how regulation would be applied in practice and was unsympathetic to our arguments that this type of behaviour undermined the traded electricity market.

- The Environment Agency sets annual sulphur limits for power generating companies and individual power stations. These restrictions have a fundamental impact on the running regime of the plants and hence the price of power going forward. Again details of draft "thinking" and decisions on the limits were shared with the generators themselves and not more widely with the market (until at least some much later point in time). There seems little reason not to publish the decisions publicly rather than share the decision only with a subset of participants.

- Ditto recent decisions on rateable values for power stations, where evolving thinking has been shared only with insiders, creating assymmetry in the information available for those considering investment in power station assets (whether new build or via acquisition).

The lesson is that "policy" decisions on how the rules are to be applied should be shared equally with all market participants, who could then take a view individually on the sort of conduct that would or would not be in breach of those rules and/or the likely impact of decisions on market prices or valuations. Some of these issues may be solved as the Freedom of Information Act beds in. However, a presumption in favour of publishing information on evolving thinking on the application and enforcement of rules would be most valuable (not least because it's easier than having to put in requests for information that you might not know you need to know).

Another tangentially related example is the Office for Rail Regulation's announcement in May 2004 that it will consider EWS representations before a formal decision is made on a Competition Act infringement and that the Regulator will "shortly be publishing non confidential versions of this correspondence with EWS". The complaint leading to this decision was prepared in early 2001. To my knowledge ORR has neither reached a final decision nor published the promised correspondence. Our call to ORR to request the correspondence (just for personal interest) went unreturned. It has therefore taken four years to not reach a decision that has remained private. Surely greater transparency and timeliness in this form of enforcement action would help to reduce perceived risk for those seeking to enter the rail-freight sector?

Capital markets commodities regulation director

8. The Commission decided upon the following terms of reference:

To assess the scope for reducing business risk arising from uncertainty over the outcome of UK and EU policy or regulatory processes and decisions

This would involve examination of five areas:

- Defining "political and regulatory risk"

- Assessing the scale of the impact of uncertainty created by political and regulatory risk (real or perceived)

- Setting out options for mitigating those impacts

- Assessing the positive and negative implications (administrative/legal/constitutional) of mitigation proposals

- Implementation options

9. The Commission's work will be explained in the next section, but as a background to its examination of this area, questionnaires were sent to over a thousand retail and investment banks, analysts, fund managers and accountants with the aim of establishing the extent to which risk has been a factor in shaping corporate investment and wider strategy or City investment policy. We received almost four hundred responses, which can be summarised as follows:

- Almost 99 per cent believed that considerations of political/regulatory risk played a significant part in shaping investment and/or corporate strategy (Question 1).

- 63 per cent believed that political and/or regulatory risk considerations had inhibited their investment decisions or forecasts; 48 per cent that they had increased the cost of capital or influenced the structure of corporate finance packages; and 69 per cent that such considerations had inhibited corporate strategy decisions (Question 2).

- The most significant risk factors were regarded as uncertainty over the criteria to be taken into account in making policy or regulatory decisions, uncertainty as to the outcome of policy processes, concern that costs and benefits of policy or regulatory options will not be fairly calculated or balanced, and uncertainty as to whether politicians or regulators will intervene. The least significant were uncertainty as to the timing of regulatory decisions and the risk that technical/specialist evaluation will be amended by regulators (Question 3)

(see Annex 2 for full details)

10. The breakdown of responses by sector reveal perhaps predictable differences in emphasis. Utilities and media companies rated political risks significantly higher than those associated with regulators; companies with major environmental exposure were more concerned than the average about regulatory interpretation; fund managers and analysts were less concerned overall than banks, and retail banks were more concerned than investment banks. Second stage witnesses (see 13. below) suggested that it would be expected that the manager of a large and highly diversified investment fund, for

example, might take a more relaxed approach to risk factors applying to individual holdings constituting a relatively small proportion of the fund than a venture capital house, which might typically focus on fewer investments at any one time and would therefore be subject to greater individual exposure.

Highest average concerns overall	**Lowest average concerns overall**
Transport	Defence
Utilities	Chemicals
High environmental impact companies	Property
Retail banks	Media
Pharmaceuticals	Analysts

11. Some care is needed in reading these results. The response to the first question is not particularly surprising given that those who are concerned might be expected to have a greater desire to respond. And caution should be taken over the weighting in question 3 as judgement can be influenced by strength of feeling about regulators and politicians (some respondents will select lower values across their overall range; others will opt for higher values) and differing levels of familiarity with parts of the system – most utility companies, for example, have very regular contact with their regulator but less liaison with Whitehall or the European Commission.

12. Notwithstanding those caveats, the response to question 2 alone led us to conclude that an undesirable degree of concern existed over the operation of the policy process and that the cost of risk was regarded by Business to be sufficiently significant to justify consideration of mitigation options. And our emphasis on uncertainty in question 3 was designed to stress the distinction between policy or regulatory activity that is predictable and which can be factored in one manner into corporate strategies, share prices, finance charges and suchlike; and less predictable activity, which may impact markets in a different way.

13. As a second stage, we conducted interviews with 26 companies, corporate financiers, fund managers, retail banks, insurance brokers and analysts to seek to establish the ways in which political and regulatory risk is priced into finance packages. From these and further evidence provided by Business Forum members and Policy Analysis Group, we noted that in contrast to generic country risk, where several consultancies and international think tanks have devised numerical rating methodologies, no reliable quantitative scoring technique beyond simple 1-5 ratings has been devised for company or sector exposure (we should distinguish here between risk assessment and calculation of the likely impact of known proposals). That is understandable: the perception of risk will be heavily conditioned by the state of the individual assessor's knowledge (both in terms of intelligence obtained and past experience) and attitude towards policy makers and regulators.

> Let me give you an idea of the way we might approach it. Take Sandler products. At the moment, our imponderables on whether we move into that area look like this: the payback will be over several years and will depend on reaching a sizeable critical mass. We do not know whether Government will impose takeup targets on us, how the FSA will regulate marketing or whether charging caps will change. That level of uncertainty will obviously affect the view we take of opportunity costs.
>
> Financial Services Group

assumed political or legislative commitments might not maintain and, most frequently, that required political or regulatory decisions might overrun assumed or declared timetables. This might typically be evidenced by defensive terms attached to completion guarantees, higher bridging costs and more expensive third party collateral charges.[6]

15. A possible approach to the assessment of such impacts is demonstrated in a December 2003 quantification by Barclays Capital[7] of the benefits of increased information flows to the gas market. It examined the impact of better signals in the areas of increased competition in production and supply, better coordination of outages, benefits from more efficient risk management, improved security of supply, and reduced balancing costs. While the assessment was of market imperfections, the parallel with uncertainty arising from inadequate knowledge of or signals from the policy process is reasonably direct.

16. Barclays Capital estimated a benefit upwards of £265 million a year, the bulk arising from improved risk management. It concluded that the spread between buy/sell prices in the wholesale gas market is a measure of the efficiency of that market, representing the "premium" paid by participants to hedge their deliveries and offtakes in order to stabilise their cash-flows. Highly liquid and efficient markets have very low spreads, which are likely to increase significantly when participants face unmanageable and unknown risks, for example, stemming from the exercise of market power or asymmetric access to demand and supply information. In these circumstances, the spread has to be higher to compensate market participants for the increased trading risks that they bear. Barclays Capital estimated that the release of greater market information could reduce these spreads by bringing them at less liquid times closer to the level of premiums observed when the market is working well. The impact of this alone was estimated to equate to a reduction in risk management premiums of the order of £200 million per annum.

17. The Barclays Capital analysis is, however, a rare example of an attempted systematic calculation of the cost of risk. It was clear that, compared with sophisticated models used for forecasting and assessing financial or conventional insurance risk, mechanisms used by financial institutions for determining and pricing levels of political and regulatory risk are generally crude – largely based on little more than the views they may hold about the way Government works, media coverage and information gained from the target sector. This latter can be misleading, since quoted companies would be expected to seek to diminish risk in the eyes of brokers and fund managers in the interest of maintaining share price. This was seen, for example, in the last Competition Commission review of BAA pricing where many analysts, taking their lead from the principal party, anticipated that BAA would be permitted a more generous charging structure. When the Competition Commission disagreed, BAA's market capitalisation fell by almost a quarter of a billion pounds - an impact that might have been ameliorated if the market had been able to make a more informed decision on the extent to which it should have discounted for risk in advance.

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[6] See *Offshore Gas Production Information Disclosure*, Ofgem, February 2005, p8. However, witnesses told us that the importance of securing or maintaining a long-term relationship with a valued client may lead to some or all risk costs being absorbed by the financier.

[7] *Benefits of greater information release in the UK gas market*, Barclays Capital, December 2003

Risk Commission Survey – selection of qualitative responses to Question 2

"Regulation has inhibited investment decisions through over-ruling of company preferred options especially on maintenance expenditure to keep water bills down in the face of competing/conflicting cost drivers."

"Regulation has created its own risk profile as perceived by investors and lenders which has increased the cost of capital. Likewise Regulation has driven water companies to adopt more risky corporate structures with high leverage in order to reduce the cost of capital through accessing the debt market often to satisfy the needs of equity investors."

"Owing to Regulatory pressures on water companies, notably in terms of efficiency targets and price pressures, they have had to adopt shorter term sub optimal solutions to requirements, prejudicing their need to focus on long term sustainability. "

"Our investment in, for example, metering technology has been inhibited by uncertainty over Ofgem's policy on competition in metering."

"Considerations of regulatory risk do affect the cost of capital in the energy sector."

"It is difficult to prove that these risks have an impact because creating the counter-factual is so difficult. However in our case the big impact is on the timing of investment decisions – the go-ahead to major projects can only be given once there is a reasonable amount of certainty around revenue streams which revolve around regulatory decision timetables."

18. This conclusion was corroborated by the Policy Analysis Group survey, which also assessed sources of risk information:

- All respondents cited newspapers and broadcast media. 44 per cent used media or political monitoring services
- 39 per cent obtained material though on line research (in the case of the City, this excluded the sites of companies being researched). Three years on, we would expect that figure to be considerably higher
- 38 per cent obtained information on sector or individual corporate risk from affected companies
- 47 per cent obtained information through direct contact with Government, regulators or politicians
- Four per cent used external forecasting or analysis services.

(respondents were able to tick more than one box).

19. However, there was a marked split in the PAG results between companies, trade associations and financial institutions, with 90 per cent of City respondents relying on the companies they monitor for political and regulatory information. And whereas 74 per cent

of companies and representative bodies obtained information direct from Government or regulators, only 19 per cent of City institutions did so (this excludes Compliance Officers' dealings with the Financial Services Authority).

20. Although a number of companies have sophisticated political and regulatory risk monitoring and assessment systems in place (and it was noticeable in our interviews and other research that many of those with, for example, three year rolling forecasting and evaluation horizons believed that others – particularly the City – over-reacted to misconstrued risk signals), the survey results suggest that in areas where calculation of risk is for many more art than science, perception is as important as reality. Perception of risk can be fuelled by many unreliable factors: as with other nostra such as "Red Tape" and "Gold Plating", it can be passed from hand to hand and create a climate in which assumptions about the way the policy process is likely to work become accepted almost without question. Nonetheless, even if policy makers and regulators observe the highest standards of governance, if outsiders believe otherwise – whether through imperfect information or prejudice – risk exists.

Risk Commission Survey – selection of qualitative responses to Question 2

"The risks were well illustrated with the investment in a new terminal building at Stansted which opened in 1991 when the Government also decided to scrap traffic distribution rules so that Stansted's opening traffic profile was way down on that expected."

"Uncertainty surrounding the structure of Phase 2 of the EU Emissions Trading Scheme will increase the risks associated with power station investment over the next two years and could cause investment to be deferred."

"Uncertainty concerning interpretation of the Large Combustion Plants Directive by the European Commission will affect investment in coal-fired power stations and their future operating lives, as will interpretation by the Environment Agency of its requirement to apply BAT (Best Available Techniques)."

"Uncertainty created over application of Basel 3 to Fund Managers, treatment of FRS17 deficit for regulatory capital purposes, and the removal of waiver for large exposure exemption for investment firms."

"Uncertainty re HMT's approach to refinancing PFI affects assessment of returns. Political risk premium raises hurdle rate of return and therefore reduces the number of PFI bidders."

"I regard political/regulatory risk as the greatest risk facing our regulated utilities."

"Uncertainty around town planning decisions makes our investment plans uncertain and obliges us to seek higher returns before committing capital."

Limits to the ability to reduce risk

21. Although we cited above an example of Government sowing the seeds of risk in order to encourage alternatives to formal regulation, policy-makers and regulators do not in the main seek to create uncertainty – indeed, many regulators have striven to establish governance principles that offer long term investment signals to their sectors (however, a number of consultees commented on the contrast in this respect with Departments and the European Commission, where there is little emphasis on "approach-based" policy making with the aim of establishing certainty and stability). Perfect foresight aside, there are nonetheless several inhibitions on optimal risk reduction in the policy process:

- Constitutional/democratic: while governments have considered the scope for political withdrawal from elements of decision making, with the most prominent – and successful – recent examples being the delegation of Base Rate setting to the Bank of England's Monetary Policy Committee and the removal of ministerial influence from most competition cases (see 27. below), many people consider that political involvement in the process, whether by Ministers, Parliaments, or councillors is essential in order to guarantee democratic accountability. More pragmatically, while organisations may often seek an environment in which issues are determined only by objective evidence, they may on occasion find it convenient to exploit sources of uncertainty for competitive advantage. Many decisions in Government or by regulators must of necessity be judgemental and cannot depend only on technical evaluation. And political control is often necessary to ensure co-ordination with other areas of government policy, to balance competing priorities or to allow the achievement of stated goals.

- Lack of perfect foresight: events change and policy or regulatory responses to them may be needed. The demand for flexibility applies as much in markets (for example, taking account of new entrants or technology convergence) as within the system. As a sector regulator put it in evidence: "*Giving absolute certainty would freeze statutory and regulatory systems at a moment in time; very soon, they would be addressing the wrong issues. The aim therefore is instead to avoid the arbitrary and abrupt. Rather, we seek the converse: consistency (both in time and as between comparable companies); a measured approach and one where changes are, wherever possible, introduced following full warning and consultation*."

- Business inefficiency: failure to forecast, assess and mitigate risk factors.

- Complete transparency is impossible: knowing what decision will emerge and all the evidence on which it is based is not realistic, so there will always be some scope for doubt over the outcome of a decision-making process.

- Cost: some uncertainties (for example over the timing of decisions) may arise from lack of resource which may inhibit the ability to monitor the process.

22. However, we believe that there is scope to improve confidence in the transparency of the process and reduce uncertainty as to the timing of policy or regulatory actions or the way in which policy and regulation will be implemented and interpreted.

23. Although the safeguard that political control is meant to offer may be important in order to retain democratic accountability, the way it is exercised should perhaps be

reconsidered if confidence in politicians is low.. Parliamentary scrutiny of the governance of Executive or regulatory action can be limited - and has done little to reduce risk: indeed, the uncertain scheduling of the parliamentary process may have increased it. It may be considered that greater confidence in the process, better governance and more meaningful consultation are significant benefits to trade against ministerial power and accountability.

The Risk Commission's programme

24. Against this background, the Commission decided to focus on six work streams:

- Whether it is desirable and possible to remove political influence from decision-making while maintaining accountability; and whether the Impact Assessment process can be developed to reduce uncertainty
- Improving transparency and signals in transposition of EU legislation
- Planning decisions
- Consistency in interpretation and enforcement, taking the Health and Safety Executive and Environment Agency as examples
- Pharmaceutical regulation – initial work as preparation for a sub-study in a follow-up report
- Pensions – initial work as preparation for a sub-study in a follow-up report

25. Commission members were divided into groups to produce initial papers for review by the full Commission.. Background work included interviews with City, business, Government and regulators all of which, in the interest of encouraging respondents, have been treated as non-attributable.

Candidates for political withdrawal/improved impact assessment

26. Political involvement in the policy process does not necessarily increase risk, but because Whitehall and Brussels at present do too little to explain how they will reach or have reached decisions, concerns over the way evidence is balanced are greater than they might be, and the *perception* of risk (which, as we have already concluded, for investment or corporate strategy purposes is much the same as the real thing) is therefore higher than it might be.

27. Government has acknowledged that this can be an issue in certain areas, most significantly in recent years by delegating decision-making responsibility for monetary policy and for most competition decisions to apolitical expert bodies subject to policy frameworks set by Ministers. In doing so, it stressed the undesirable impact of uncertainty and of suspicion over the role of political decision makers. Transferring the management of monetary policy to the Bank in 1997, the Chancellor said:

'Government has a responsibility to the public in setting the objectives of economic policy and that means that the Government rather than the Bank of England must set the targets for monetary policy.

However, as I have repeatedly made clear since 1995, we will only build a fully credible framework for monetary policy if the long-term needs of the economy, not short-term political considerations, guide monetary decision-making. We must remove the suspicion that short-term party political considerations are influencing the setting of interest rates.

As our election manifesto said:

"We will reform the Bank of England to ensure that decision-making on monetary policy is more effective, open, accountable and free from short-term political manipulation."
It has become increasingly clear that the present arrangements for policy-making are not generating the confidence that is necessary. That is one reason why Britain has higher long-term interest rates than most of our major competitors. And the perception that monetary policy decisions have been dominated by short-term political considerations has grown.'[8]

And the 2001 competition policy White Paper justified the withdrawal of Ministers on grounds of risk reduction:

'Ministers will be taken out of the vast majority of monopoly and merger cases, and decisions on day to day cases will be taken by the Competition Commission against a competition-based test. This will increase business certainty.

This change will clarify arrangements and make decision-making more predictable. Business will no longer need to factor in the possibility that decisions will be influenced by political considerations.'[8]

28. In looking to build on that precedent, echoed in many other cases such as the creation of sector regulators and the delegation of powers to public bodies, we concluded that the solutions to the risk challenge are part structural - more transparent and objective processes; part cultural - for example genuine commitment to providing longer-term signals; and part PR - demonstrating good governance - in nature.

29. What does that mean in practice? Structurally, there are three routes that might be examined – political withdrawal, process timetabling (decisions having to be made or stages reached by a certain date and greater clarity over forward planning) and horizon-setting (creating a reasonable expectation that policy frameworks will not be significantly amended for a declared period). The first of these would seem to work best in areas involving price-based regulation or standard-based regulation. Examples might be

- the setting of night movement quotas at airports, currently a four-yearly process where Ministers are the ultimate decision-maker and airline investment strategy may be impacted through uncertainty as to whether technical recommendations will be politically amended in response to the concerns of the public and/or pressure groups. Following the MPC example, Ministers could set parameters and criteria and

[8] Statement by the Chancellor on the central economic objectives of the new Government, 6 May 1997
[8] *A World Class Competition Regime*, DTI 2001, Foreword and para 5.2

then leave the rest of the process to the Civil Aviation Authority. As with the MPC, whose deliberations can be no more forecast than they were when Treasury was able to exercise influence over the Bank of England, actual risk may not be reduced – the CAA might amend its initial proposals in response to consultation (there is a part solution to this: see below) – but perception of risk and confidence in the system may improve

- utility price reviews, where some regulators are required to submit proposals to Ministers but others have to submit to determination by the Competition Commission. Once again, the statutory ministerial guidance (for example, on social or environmental objectives) should be enough, with Ministers playing no further role and with all reviews being handled on a consistent basis, possibly by the regulator without the need to burden another body.[9] In complex technical areas such as these Ministers cannot reasonably be expected to have sufficient expertise to guarantee democratic accountability, but Select Committees' existing power to scrutinise the regulators or the departmental officials responsible for technical determination should be adequate and would be more transparent

- setting environmental standards (for example, engine NOx emissions or noise levels) within the context of broad government-set climate change or air quality objectives.

We recommend that candidates should be drawn up for transfer of decisions within these areas to expert bodies working within ministerially-set limits and criteria.

Why, following the granting of planning permission to a power station, is there a need under the Electricity Act for Ministers, following lengthy technical evaluation, themselves to have to issue a licence to burn gas?

30. The above examples fall under existing regulation. In making new policy or legislation there should be a more fundamental precursor: Ministers should reach a determination on whether the public interest requires them to be the ultimate decision maker, as distinct from the setter of decision-making frameworks within which officials or external expert bodies should work, and should be prepared to justify that role – a position similar to that under the Enterprise Act, which allows Ministers to opt in to an objective process in certain circumstances through serving Intervention Notices on the Competition Commission. Concomitant to this is an assumption of accountability of independent or technical decision makers to Parliament. This is not to suggest that the process should be geared to the needs of business and City – there will always be cases where the price of reducing corporate risk is increased risk to consumers, for example, and the system must balance competing interests – but we believe it is possible to introduce new procedural principles that place Ministers in a clearer position.

31. This approach is consistent with the principles that underpinned the MPC and competition decisions referred to in 27 above. We propose this because

[9] This is consistent with the conclusions of one of the Commission members, Dan Corry, in *The Regulatory State* (IPPR, 2003), where he distinguished between the political setting of policy parameters and regulators' independence of operation within that framework.

- decisions in many areas currently reserved to Ministers are essentially technical in nature

- recourse to Judicial Review is denied to many on grounds of cost and may not be available in cases of non-statutory policy decisions

- prevention of avoidable uncertainty through fear of arbitrariness or political bias is preferable to an ex-post cure

while recognising that there are major policy areas such as resource allocation and the balancing of social, economic and other considerations where it is right that the convention of direct political accountability should be maintained. In many cases, therefore, our proposed approach is still likely to justify retention of political primacy. The important point from a risk standpoint is that the determination should be able to be justified.

32. However, it was felt that this alone might not be sufficient to influence decision-making culture. We believe there should also be a presumption in favour of the publication of research, internal analysis and external advice and that it should be incumbent on the system to explain any apparent departure from it. This would not involve declaring officials' advice to Ministers, but the analysis underpinning it (for example, the Regulatory Impact Unit's examination of draft Impact Assessments) should be placed in the public domain: Freedom of Information may force this anyway. We would expect that such a requirement might initially lead to more guarded, less specific analysis but over time pressure would grow for a greater rigour to be demonstrated. We note and welcome DTI's acceptance of the advice of the Government's Chief Scientific Adviser that the evidence used in policy advice to be subject to peer review, or an appropriate quality assurance process[10].

33. Publishing indicative timescales for decisions or legislative phases is consistent with the popular practice followed by several regulators. It has been argued that policy and regulatory processes do not offer direct parallels and that timetabling could not be introduced as easily into the Whitehall system as in, say, Ofgem. We are not convinced that this is the case but would suggest that the procedure is tested through three pilots spread over different Departments and involving a major policy development exercise, a policy review, and a Bill.

34. A move to more disciplined timetabling will arouse concerns over guillotining. We therefore recommend it subject to the presumption that it should only apply to the parliamentary stage of the process in extremis (we distinguish between pre-legislative scrutiny committees acceptably being set a deadline for reporting and the imposition of a guillotine on debate) and provision would have to be made for changed circumstances or new evidence.

[10] DTI press release, 19 October 2005

Why it is important to explain departures from expert advice

Government is accused of playing politics with food safety

(…)*John Reid, the Health Secretary, and Sir Liam Donaldson, the Government's Chief Medical Officer, are refusing to allow beef from cattle aged more than 30 months back on to dinner plates.*

They are blocking a plan to replace the eight-year-old ban with a new test on every cow before its meat can enter the food chain. The opposition from the Department of Health has angered ministers at (…) *Defra* (…)*.*

They are exasperated because the proposed testing system has been adopted by other European countries and been approved by scientists at the Food Standards Agency, the Government's BSE advisory committee and the European Food Safety Authority.

Yet Mr Reid, Sir Liam and Melanie Johnson, the Public Health Minister, continue to question the robustness of the scientific evidence that would allow people to eat beef from older cattle.

Their stance appears to undermine the scientific risk assessments by the country's leading experts.

(…) *there is now anger and concern that the independent advice is being ignored.* (…) *Meat industry chiefs now fear that the Government's opposition can be explained only by political concerns and the prospect of a general election next year.*(…) *"We just do not understand why they are challenging the opinions of the scientific experts"*.

Times, 27 July 2004

35. Several regulators also give clear signals about decision making structures by consulting upon and publishing annual work plans, which differ from Departments' Annual Reports or five year plans in their emphasis on detailed workstreams and schedules rather than aspirations and outcomes. This could be translated by Government into a regularly updated three year or full-Parliament programme. It has been suggested that the publication of forward legislative programmes would create problems in connection with the annual Queen's Speech. However, such longer-term (say for the life of a Parliament) scheduling could only be indicative and subject to annual confirmation; some Departments already refer to the development of specific legislation in their five year plans; and the proposal is already under consideration[11]. At the very least, UK and EU bodies should adopt the Scottish Executive's practice of posting on its website a schedule giving notice of forthcoming consultations[12].

[11] *The Commons leader now wants to introduce "a strategic approach" to law-making with each department making bids for, and agreeing to, a "three-year plan for legislation" in the same way that they already negotiate budgets with the Treasury* (interview with the Leader of the House, Times, 15 January 2005).

[12] See http://www.scotland.gov.uk/Consultations/Forthcoming

36. Our recommendations have been based on a view that confidence in the policy process is lower than might be desirable. Ministers will have to decide whether giving greater structure to the process is an acceptable price to play for an increase in faith in that process and therefore a reduction in perceived and actual risk. The comparison with judges, whose public standing if much higher, is relevant: like Ministers, judges are kings in their own court; but they have to operate within a clearly recognised code of procedure and evidential requirements and the process of judgement is both visible and justified to all. Our proposals are rooted in a desire to raise trust in political and judicial decision-making to the same level.

In producing advice on food safety and diet, (Food Standards Agency Chairman Sir John Krebs) has stuck to three principles: that the agency should be independent; that it should base its views on scientific evidence; and that it should be open to scrutiny.

"If you are independent, that means being objective and impartial about the evidence and not succumbing to pressure from interest groups, whether they are the food industry, consumer groups, green groups or politicians," says Sir John, who steps down in April to become principal of Jesus College, Oxford.

"If you take that stance, you will inevitably come into conflict with people who have firm beliefs that may be very real to them but not necessarily supported by evidence." The agency's stance on genetically modified food has attracted particular anger from environmentalists. "We have said we are neither pro nor anti-GM," he says. "We will look impartially at the evidence in relation to food safety and assess each case using the best available science, and we will support clear labelling of GM food so that people can choose. That, to me, is a neutral stance.

The National Consumer Council was one of several consumer groups to accuse the agency two years ago of bias in support of GM crops and of failing to address public concerns about their safety. But Deirdre Hutton, who chairs the council, praises Sir John for creating an organisation "that operates with a transparency unheard of in British politics". She has used it as a model to encourage openness at the new European Food Safety Authority, of which she is deputy chair.

Sir John believes that transparency was crucial to rebuilding public trust. The agency's approach stands in contrast with the old Ministry of Agriculture, Fisheries and Food (Maff), where the approach was "decide on the policy, announce it and then defend it".

Three-quarters of the agency's 2,000 staff came from Maff and most of the rest from the Department of Health. Sir John and his first deputy chair, Suzi Leather, a consumer champion, pushed for board meetings on policy to be held in public, a signal to staff that the old era was over. "At the last board meeting, we had 60 to 80 people in the audience and another 700 watching on the internet." Interest groups are also consulted before policies are made - typically by being invited into the agency to talk to officials early in the process.

Financial Times, 10 February 2005

37. Whitehall and Brussels might usefully borrow from DG Competition's Best Practice Guidelines for mergers, where State of Play meetings with the parties (which

can be translated in the policy process into the hearings that regulators hold) are offered within the Merger Regulation timetable to discuss the development of thinking on cases, meaning that assumptions on outcomes can be steadily built up rather than sprung upon affected sectors and their financiers.

38. Examples of horizon-setting are Ofcom's recent Communications Review, with a declared objective to set a clear policy framework to 2010; the Renewables Obligation, where the Government has set out a framework to 2016 with five-yearly reviews; or airports policy, where the review process leading to the recent White Paper assumed a need to set policy to 2030. Once again, much of this is about managing expectations - raising confidence that policy-makers are less likely to tinker with measures in reliance of which investment decisions may have been taken (or that if they do – and inevitably circumstances change over a period of several years – the basis and process for doing so is clearly understood well in advance). One option to encourage greater use of this approach while maintaining flexibility could be

- as part of initial consultation (possibly carried out through an extension of the existing industry/cross-Government fora, comprising small groups of experts drawn from affected sectors[13]), views should be sought on reasonable investment/certainty horizons: these could be quite lengthy in sectors involving either long payback (such as renewables or building the Channel Tunnel Rail Link) or where development and investment processes are slow (aero engine environmental standards are an example); or much shorter where, for example, technology change rapidly outranges policy – for example IT data protection.

- policy or regulation could then be set on a detailed framework basis, with a clear announcement as to the timing of "State of Play" (for example the aviation White Paper's assumptions on airport capacity will be reviewed in 2006) and fundamental (it was known well in advance that BAA's charges will be statutorily re-examined in 2006) reviews. The circumstances in which policy or regulatory intervention might be expected to take place within that timescale would also be clearly set out, although we would assume that there would have to be an Other Things Being Equal exception. The State of Play review would also include ex-post assessment of actual compared with forecast costs and benefits, with the option of subsequent consultation on amendment, strengthening, or relaxation (see 43. below). A decision that change might be required need not conflict with the objective of stability within the horizon timescale since, with rare exceptions, even if “fast track” Regulatory Reform Orders are used that horizon would probably be approached by the time the amendment process had been completed. One benefit of consultation at the State of Play stage is that it may on balance be decided that the investment certainty and other benefits of Do Nothing outweigh those from reducing regulatory costs or improving efficiency.

[13] Government has accepted the desirability of increasing these groups, which currently cover the food, retail, chemicals, vehicles and construction sectors, and of involving them at the outset on issues associated with emerging regulatory proposals: see *Government response to Better Regulation Task Force report on Avoiding Regulatory Creep*, February 2005, response to recommendation 6

Why cannot Whitehall work like this?

In December 2004, the Civil Aviation Authority consulted on its approach to reviewing airport charges, including an indicative schedule. All stakeholders should welcome departmental policy and legislative processes having this level of predictability:

Early 2005: Preliminary airline/airport discussions on the institutional structure for the negotiations and for the development of traffic forecasts, and on the nature and content of the preliminary papers to be prepared by the airports

March 2005: CAA consultation paper on the framework for the negotiations

Spring 2005: Parties comment on the consultation paper; BAA works up preliminary papers, in informal contact with airlines

July 2005: CAA decision document on the framework for negotiations and to which airports it should apply; BAA produces initial position papers

Autumn 2005: CAA consultation paper on issues of regulatory policy for the next reviews

Winter 2005/2006: Parties comment on the consultation paper; MAG begins work on preliminary papers for Manchester Airport review (MAN), in informal contact with airlines; negotiations commence on BAA airports

Spring 2006: CAA issues decision document on issues of regulatory policy for the next reviews; negotiations continue on BAA airports; MAG prepares initial papers for MAN

July 2006: negotiations on BAA airports complete; MAG issues initial papers on MAN

Autumn 2006: CAA consultation draft of its proposed CC reference on BAA; negotiations commence on MAN

Winter 2006/2007: CAA refers package on BAA airports to the Competition Commission (CC); negotiations on MAN continue

Summer 2007: CC reports on BAA airports; negotiations on MAN complete

Autumn 2007: CAA consults on price caps for BAA airports; CAA consults on proposed CC reference on MAN

Winter 2007/2008: CAA decides price caps for BAA airports; CAA sends package on MAN to CC

April 2008: New BAA price caps in force

Summer 2008: CC reports on MAN

Autumn 2008: CAA consults on MAN price cap

Winter 2008/2009: CAA decides MAN price cap

April 2009: new MAN price cap in force

Edited from *Airport Regulation: Looking to the future – learning from the past, CAA 2004*

39. We also considered the relevance of Regulatory Impact Assessment and its Brussels counterpart, Impact Assessment, to the risk agenda. These procedures are important as a way of ensuring that the costs and benefits of proposed policy initiatives are properly evidenced and fairly weighted before a decision is taken and because of the need to create a perception that decisions will be linked to evidence and will not be distorted by more subjective factors without good reason. We felt that their use could be improved to make the system more punctilious about Evidence Based Decision Making.

40. Government reacted to concern over the effectiveness of the RIA process by announcing the establishment of a Better Regulation Executive, with responsibilities including oversight of RIAs and other issues covered in this report such as enforcement. While the move to a BRE with an independent head and non-executive directors is welcome, and the system will want to give the BRE time to prove its worth, we feel that there may be a need for a more radical approach to strengthening of scrutiny mechanisms. A preferable option would be to give the BRE a more independent status (the Office of Fair Trading might be a model) and empower it to undertake Impact Assessments, reach advisory conclusions on proportionality (whether a fair balance has been struck between benefits and burdens) and to scrutinise Departmental, Non Departmental Public Body and regulators' subsequent use of them. This stems from concern that despite the willingness of the Cabinet Office's Regulatory Impact Unit (now part of the new Better Regulation Executive) to adopt improvements to RIA guidance and reports of hard negotiations between the RIU and Departments behind the scenes, visible influence on policy, legislative or regulatory decision making has to date been lacking and surveys by Commission members[14] suggest that, whether justified or not, suspicions about poor or opaque methodologies and of data trimmed (or ignored) to suit conclusions continue to be widespread. We need a system where the owner of a proposal cannot simply, and in private, say no to the BRE or persuade colleagues in the Panel for Regulatory Accountability (see below) that the Government's programme should not be disrupted by evidential queries: the BRE should be given sufficient power to require that the proposal should if necessary fall or its owner renew it with a public explanation.

41. The 2005 Budget announced an enhanced role for the National Audit Office in overseeing the technical evaluation of departments and regulators in reducing the burden to business of administering regulation[15]. NAO will now report to Parliament on departments' performance against their targets for reduction of regulatory burdens and regulators' performance against the Hampton Review's recommendations and principles (see Enforcement and Interpretation below). This role could be further expanded. Less radical than independent status for the Better Regulation Executive would be maintenance of its role during the drafting process but giving the NAO the power to undertake peer review of all RIAs between ministerial sign-off and Council political agreement or, for UK-originating measures, implementation of the policy in question or

[14] See *Accountable Government*, Charles Miller for the SMF Business Forum, 2004
[15] See *Economic and Fiscal Strategy Report*, 3.38

Improving confidence in the process – Ofgem and the Distribution Price Review

The approach taken by Ofgem to this major review has been applied to its smaller-scale policy and regulatory exercises and is also adopted to a greater or lesser extent by other regulators such as Ofwat, Ofcom and the National Lottery Commission. We will therefore set out the broad principles rather than focus only on the DPCR:

- It published a draft Approach Paper, setting out the way in which it proposed that the Review be conducted, and invited views. This allowed affected parties to recommend methodological assumptions and governance principles at the outset
- It held hearings on the Approach Paper and on subsequent consultation papers. Some Departments are starting to adopt this practice
- It allowed affected parties to comment on the methodology to be used for the calculation of costs and benefits
- And it set out a clear timetable for the review, with target dates for every stage

From *Accountable Government*, Charles Miller for the SMF 2004

the parliamentary stages of legislation. In practice, this would involve auditing the implementation and management of the RIA process, assessing compliance against a set of tests such as

- Were experts from likely affected sectors consulted at the outset on alternatives to regulation? Does the RIA explain why the decision was taken to opt for formal regulation?
- Was the methodology for seeking and assessing evidence appropriate to the issue and sector? Were calculations of costs and benefits clearly justified and explained? Were evidence sources balanced?[16]
- Was consultation carried out in compliance with Cabinet Office requirements? Was any departure from recommended timescales adequately explained?
- Was evidence presented to Ministers in such a way that it would be possible for them to reach an informed and balanced decision on proportionality?

42. NAO already annually evaluates the quality of a sample of RIAs and, in contrast to the former RIU, it publishes its assessment and advice on improvement and this additional responsibility would be consistent with NAO's current role, which under the National Audit Act 1983 does not involve questioning the merits of policy objectives but does consider how policy has been designed and implemented. It would be for the

[16] Note that the European Commission has decided to submit impact assesment methodologies to ex ante validation by independent experts (Communication on *Better Regulation for Growth and Jobs in the European Union*, March 2005)

Public Accounts Committee (or Select and joint scrutiny committees) to decide whether to question Ministers or officials in cases where the NAO raised concerns over proportionality. Whichever option is preferred, it will also be important in addition to assessment of planned legislation or regulation to implement the commitment[17] to undertake retrospective review after, say, three years, something that neither Whitehall nor the European Commission carry out systematically.

43. We have proposed that the NAO should only audit governance. If proportionality decisions are to be fully challengeable on the basis that they were not justified by the evidence, the RIA process would either have to become statutory[18], allowing ministerial proportionality decisions to be judicially reviewed (after all, if environmental impact assessments can be challenged, why should not one that the benefits of a legislative proposal outweigh costs?) or the Lords Constitution Committee's proposed Regulatory Appeals Tribunal should be established to cover all cases, whether involving regulators, Departments or NDPBs, which do not currently fall under the jurisdiction of the Competition Commission.[19]

> The fundamental principle of administrative law established in the Wednesbury case that the administrative authority must behave 'reasonably' had a fairly narrow interpretation which subsequent case law has steadily widened. Judicial review may still be risky and expensive for plaintiffs.
>
> But it is a real and very useful constraint on the behaviour of regulators - none of us would wish to be found by the High Court to have been behaving, for example, in any way irrationally. We therefore tend to move carefully and in consultation which, I would hold, adds to regulatory effectiveness in most circumstances.
>
> Sector regulator

44. One advantage of using the NAO, apart from greater independence than the current BRE, is its reporting line to Parliament, which currently does not exercise systematic oversight of governance: the PAC could therefore act as a more democratic, transparent version of the Panel for Regulatory Accountability, which currently meets behind closed doors and does not publish its agenda or output (because of this, the expanded role for the Panel announced in the 2005 Budget may do little to demonstrate its effectiveness). Regardless of whether either of our proposed new structures are accepted, a closer relationship between the PAC and the Better Regulation Commission and Better Regulation Executive, possibly taking the form of an annual performance review, would be welcome. It would also offer the BRC a formal parliamentary forum for setting out its conclusions on regulatory efficiency.

[17] Labour Business Manifesto 2001

[18] A proposal on which the Scottish Parliament's Subordinate Legislation Committee consulted in its *Inquiry into the regulatory framework in Scotland.*

[19] cf note 3. above, para 232. While statutory status for RIAs across the board would be preferable, at the very least it could be progressively introduced through incorporating in new legislation an RIA requirement in respect of decisions made under that Act. This approach was favoured in the Food Standards Act 1999, the Financial Services and Market Act 2000 and the Communications Act 2003.

How accountable is the Panel for Regulatory Accountability?

Mr. Stephen O'Brien: To ask the Minister for the Cabinet Office on how many occasions the Prime Minister's Panel for Regulatory Accountability has met since March; which regulations likely to impose a significant cost to business have been scrutinised by the panel; and which regulatory proposals have been *(a)* rejected and *(b)* delayed by the panel.

Mr. Miliband: We do not disclose information relating to the proceedings of the Cabinet and its committees.

Hansard, 12 January 2005

45. We do not expect that the NAO would have to have to reach a critical judgement on many RIAs because the example of regulators such as the Food Standards Agency which are under a legal obligation to undertake cost:benefit analysis suggests that the fear of legal challenge forces the system to be much more careful about researching and explaining its decisions. Even if RIAs were not given statutory status, the respect in which the National Audit Office is held would act as an incentive on Departments to make it easy for the NAO to provide a clear opinion on RIAs with only minimal scrutiny. Nonethless, NAO would need more staff, but significant resource requirements would be eased if industry/cross-Government fora (see 38. above) were used by Departments to assist with the production of RIAs and then borrowed if necessary by NAO (or by the new body proposed in 40. above) to accelerate its learning curve. Use of these fora would have the further advantage of improving quality and boosting confidence at the departmental stage, reducing the need for lengthy NAO scrutiny, which in most cases could be carried out by reference to unambiguous criteria (as in 41. above). On that basis, and given that some 200 RIAs are produced annually, we estimate an additional staff requirement of well under 50.

46. At present, the NAO is annually sent a few RIAs by the Better Regulation Commission from which it selects a sample for review. However, only some five per cent of RIAs are assessed in this way, a total too small to concern Departments which, if they are to be stimulated to greater punctiliousness over use of RIAs as a genuine tool, will need to assume that there is a much higher chance of their work being audited. As an interim measure, we therefore recommend that around 20% of Assessments should be examined on the checklist basis proposed in 41. above, with a smaller number being subjected to the current depth of review. If BRC's resources would be stretched by this, it might be open to NAO to make a direct selection. Because annual review takes place after the regulation sanctioned by each RIA has been settled, the NAO's work can only seek to influence subsequent conduct, so we see this as a half way house, with the preferable reform enabling NAO to highlight weaknesses in poorly-executed RIAs before the Council or Parliament sets its seal on measures.

47. Our alternative proposal preserves the independence of the Comptroller and Auditor General because RIAs would remain the responsibility of the relevant Department or agency and NAO's work would not question the merits of policy objectives. The proposal also builds on the NAO's existing work in evaluating RIAs in a

way that should raise the profile of impact assessment within Government and improve incentives for Departments to produce higher quality RIAs.

48. Better RIAs do not themselves reduce risk (legal status would, though, for the reason given above); the perception of a commitment to producing them properly might do so through increasing confidence in the process[20].

49. *Accountable Government* commented on the apparent lack of desire by the system to demonstrate that impact assessments work[21]. The NAO's most recent review of RIAs found that four of the ten assessments sampled led to some changes in policy, ranging from minor refinements to the Department deciding not to regulate at all; but there was little communication of cause and effect to affected sectors.[22] Regardless of the above options, greater opportunity should be taken by Whitehall, regulators and EU institutions to increase confidence that impact assessment is genuinely used to inform, rather than to justify conclusions by publicising cases where assessments have clearly influenced decisions. Justice must be seen to be done.

An example of Government showing that impact assessment has influenced its decision making

On 22 July 2004, Consumer Affairs Minister Gerry Sutcliffe announced that proposals to licence estate agents had been dropped in favour of an Ombudsman scheme in the light of assessments that showed licensing to be disproportionately expensive.

50. These proposals would, with relatively minor amendment, be equally applicable at UK and EU levels.

Transposition risk

51. The Commission was also concerned that unnecessary uncertainty surrounds the process of translating Community legislation into national law. We are not referring here to the frequently (and often unjustifiably) reiterated charge of "Gold Plating" but to

- Delays in corporate strategy implementation through organisations (or even governments) not knowing how legislation will be transposed efficiently ahead of the implementation date

- Unresolved uncertainty over the interpretation of often deliberately vague Regulations or Directives; this may leave insufficient time for organisations to adapt

[20] In Brussels, scrutiny of Impact Assessments is handled by the Commission Secretariat-General. However, parts of the process are still not covered by a IA requirement: the increasingly used Conciliation procedure, which operates when the European Parliament, Council and Commission cannot accept each others' legislative amendments, produces compromises with little explanation and no analysis of costs and benefits. While we accept that Conciliation timetables are tight, clarity and accountability are as important at that stage as at any other.

[21] The 2004 Pre Budget Report took this point on board and cited three examples of decisions being changed following consultation – cf PBR para 3.37

[22] Evaluation of Regulatory Impact Assessment Compendium Report 2004-5, NAO, para 19

- Inconsistency in approach across borders affecting organisations with similar operations in several Member States.

52. Three examples of this are set out in 2. above and illustrate the importance of Member States providing a clear explanation *ahead of reaching Common Position in the Council of Ministers* of the scope of national application and of the way they will interpret and apply the measure. Current Cabinet Office guidance to officials[23] is to produce a project plan for transposition no later than adoption of a Common Position by Council. While this may seem reasonable, if plans are produced late in the process (for example, between political agreement and adoption) they may result (as we showed with the passenger information Directive) in Member States agreeing to legislation without knowing how or whether it can cost:effectively be made to work.

53. It may be argued that the complex politics of reaching agreement in Council can on occasion preempt such preparation. We believe that a "shoot now, ask questions later" approach can never be acceptable and that the Council Bureau should seek sight of draft implementation plans before Common Position (and, if significant amendment has taken place in Conciliation, before the Council finally agrees). This may delay the process by one or two months, but that is justified by the benefit in greater certainty that it would bring. We recommend that initial consultation on transposition should become part of the RIA process, with views on costs, benefits and implementation options being invited while proposals are at Working Group stage. Introduction of automatic notification (see 54. below) would allow affected sectors to be kept informed of the implications as negotiating drafts change.

54. At present, public explanation of implementation plans is given at a late stage, in the Explanatory Notes and Transposition Notes that are meant to be produced when legislation is introduced in Parliament, and is poorly disseminated (the Notes are meant to be posted on departmental websites but are difficult to find and few departments have introduced automatic notification systems to make it easier for affected parties to gather information such as this)[24]. While it is probably not possible for TNs to be published earlier given that they are designed to offer a clause by clause commentary on the implementing legislation, the draft implementation plans (covering definitions, the implementation plan and timescale, scope of application, and the basis for any elaboration of the original text) that have to be drawn up for all transposable EU legislation could be posted on line when they are sent to the Council Bureau.

55. The option of simply transposing Directives verbatim has been mooted by some commentators. While this would at least offer cross-border consistency, we do not believe that it would be an effective remedy as thin or unclear legislation only creates a demand for detailed guidance notes, in the absence of which the apparent reduction in

[23] *Transposition Guide: How To Implement European Directives Effectively*, RIU 2005

[24] Automatic notification of announcements, documents and events has been offered by several sector regulators for some time. Its widespread introduction by all Departments, Brussels Directorates-General, regulators and NDPBs would, we believe, make an appreciable contribution to the reduction of risk, particularly among SMEs, by limiting one of its factors – imperfect communication (see para 2. above). Where notification systems exist, they should be well publicised, both direct and through representative bodies, as the existence of this facility is relatively little-known.

Red Tape would in most cases be offset by an increase in risk. The 2004 Pre Budget Report stated that "*Transposition should mirror as closely as possible the original wording of the directive except where there is a clear justification for doing otherwise, having regard to the impact on business and the workability and fit of the legislation in its domestic context*"[25]. It is important that the distinction between elaboration and Gold Plating[26] is understood and observed in that context.

Enforcement and interpretation[27]

56. We concentrated on two bodies, the Health and Safety Executive and Environment Agency. The main risks we identified relate to inconsistency

- between the two regulatory areas
- within each of these regulatory regimes
- between the central and local agents responsible for enforcement. There is a division of responsibility in both cases, with the EA and HSE being responsible for the most serious environmental and occupational health and safety risks and local authorities having responsibility for lesser risks.

57. Inconsistency *between* these areas – where actions required by one may violate the requirements of the other – is being handled in a modest way by inter-agency co-operation. Attempts to follow such a path are presently limited and have encountered some difficulties because of differing legal frameworks and regulatory approaches resulting from them.

58. Inconsistency *within* regimes is typically tackled by guidance, enforcement codes and training. HSE has also recently introduced an internal audit and peer review of regulatory decisions. The establishment of cross-functional teams is used by both agencies to try and foster greater consistency between areas. The use of risk-based methodologies is another example of regulators trying to tackle issues of consistency, these approaches are very well developed in HSE and more recent to EA. But risk-based regulation needs to be handled with some caution. A particular concern is that it may lead to under-enforcement of what are perceived to be low risk areas. And lack of enforcement, or being compliant and seeing others 'get away' with non-compliance, is also a concern of business (cf para 5. above).

[25] Pre Budget Report 2004, 3.39
[26] For a definition see *Transposition Guide – how to implement European directives effectively*, cf Note 21 above.
[27] This section was written before the publication of the Hampton Report in March 2005. Hampton covers this subject in greater detail but echoes several of our recommendations.

> We have experienced considerable inconsistency in the application and interpretation of policy and planning guidance. For example, the Highways Agency centrally may take the view that where traffic flows are disrupted by a service area because of long term roadworks the operator is entitled to a sign saying 'services open as normal' but a regional director can take a contrary view and turnover can fall by 15-20% for the duration of the roadworks.
>
> Food services company

59. But there are a number of fundamental difficulties to consider:

- How much consistency is desirable and what is meant by consistency? Where consistency refers to the application of fairly prescriptive rules across all businesses without any enforcement discretion, larger businesses seem to be particularly unhappy. Indeed, rigid enforcement of prescriptive rules seems to be the type of regulation most cited within the media. Where it refers to consistency in the application of a set of rules or a risk-based approach, SMEs tend to complain as they do not have the regulatory capacity to cope with such a system - which leads to a second difficulty.

- Different types of business want often very different regimes. Larger businesses generally favour more risk-based regimes which may have inherent flexibility over time and across areas, whereas SMEs are known to favour something simpler and more prescriptive.

- Regulators are charged with taking differences in regulatory capacity into account through broadly framed legislative concepts such as ‘reasonably practicable’. They also take varying capabilities into account by being outcome rather than process based so their focus is on consistent outcome rather than uniform process, and by the use of cost:benefit analysis.

- At a national level, greater complaint about political risk is directed to the environmental area than to occupational health and safety for a number of reasons, a significant one being the division of responsibility between DEFRA and the EA – the CBI for example reports being confused about the division of responsibility of each with respect to decision-making. HSE has a greater degree of independence in its operations (as do other agencies such as FSA). This is perhaps a model to commend as it reduces the risk of political interference and bureaucratic confusion and creates an obligation on policy makers to secure agreement with independent agencies on the effectiveness of delivery. If EA had the autonomy of other agencies such as HSE and FSA it could take total responsibility for regulatory policy and implementation, enabling more independent and holistic approaches to environmental regulation and creating greater clarity for business about responsibility and communication.

60. Political risk is at its highest at local level. There are over 400 local authorities with responsibility for aspects of environmental and occupational health and safety enforcement. The possibilities for differential enforcement are numerous – ranging from budget allocation to the views of local councillors. Indeed in some local authorities even action proposals about legal enforcement are brought before a council committee for decision. HSC does have some authority to question local authority health and safety

approaches and has engaged in a deal of work to try and foster consistency through interauthority audits, partnership agreements and training programmes. EA does not have such authority to oversee or monitor local authority enforcement.

> We do find inconsistencies in interpretation between trading standards officers in different authorities. For example if we consult the trading standards officer in our "home authority" and they gave the green light to a promotion or advert and an officer from another authority contacts the company with a complaint or query, the opinion of the officer in our home authority should take precedence; however, this is not always the case and we do run the risk of having to withdraw a promotion because an officer takes a contrary view.
>
> Food services company

61. The potential effects of differential powers to oversee local authority decisions are highlighted by the case of food safety. The Food Standards Agency has relatively strong powers to oversee local authority activities in this area, and there is evidence that this has led to the devotion of much greater authority attention and resources, but at the expense of other environmental health issues (*Hampton*, 2004: 3.41).

62. Some of the solutions to these difficulties may be politically unacceptable to some although that does not mean they are not worthy of mention. Already mentioned is the establishment of the EA as an agency independent from DEFRA. Another possibility is the transfer of regulatory responsibilities from local authorities to the relevant central government agencies. This does not necessarily mean the loss of local sensitivity as HSE and EA both operate a network of regional offices and locally based inspectorates.

63. Other proposals might include:

- Greater inter-agency co-operation is being tried by HSE and EA (see above) but this is not without its limitations. More 'joined up' co-operation is to some extent hampered by different legislative and institutional regimes. This suggests the more radical solutions identified by Hampton, namely greater consolidation of regulatory activities.

- Greater clarity about regulatory goals by the legislature, for instance a statement in legislation about what it is trying to achieve.

- Transparency about enforcement criteria and activity on the part of regulatory agencies. HSE, for example, publishes its guidance to inspectors, much of it on the web. This practice is to be encouraged.

- Greater co-operation between business, government and worker/environmental representatives at the drafting stages of legislation. This could involve fora where these groups could come together to focus on the practical implications of legislative drafting ; and

- Greater co-operation between these groups about pragmatic compliance solutions such as two track compliance schemes (for example, the Licensing of Butchers

Shops Regulations, Scotland[28] where butchers can opt to comply with either a simple prescriptive set of regulations or a more broadly framed risk-based approach).

64. Business should also be taking more responsibility. Greater regard should be given to the voice of those requiring protection and cases where there are simple pragmatic responses to regulation. All those from whom we have took evidence for this section cited examples where business has complained in a knee jerk way about regulation that is not a significant burden.

Planning

65. We looked at options for reducing both uncertainty and cost in the planning process, taking evidence from practitioners, professional bodies and commentators. Constraints were stressed by all witnesses in three areas:

- Technical: a lack of clarity over process; possibly unnecessary regulatory requirements.

- Political: the risk that technical evaluation may be amended at Member-level.

- Resource: lack of staff or poor training has, it was suggested, led to uncertainty over timetables for decisions, an appeals logjam, and an increase in risk though inadequate scope for detailed pre-application discussion, resulting in applications failing to address key concerns and being rejected.

66. There were significant differences both within the Commission and among our witnesses over the desirability of limiting political involvement or of giving a stronger role to regional planning bodies with the aim of seeking greater consistency in application of policy. In seeking to address the constraints that were represented to us while taking those concerns into account, we reached the following conclusions:

- Greater certainty is needed over the availability of development land. The Government, through Local Development Frameworks, is trying to speed up the system. We considered the suggestion that Local Plans should be revised annually, but felt that this was too ambitious to be attainable. Gloucester Council attempted this a few years ago but gave up as it proved impossible to plan for just one year ahead. We therefore recommend that they should simply be monitored on a rolling annual basis, with the possibility of a fast track process (perhaps based on Whitehall consultation timetables) where fine tuning may be needed. Plans should set out areas where capacity is coming on stream and then establish a simplified planning system within those zones.

- Annual monitoring need not be more onerous than at present. Local Development Plans could be shorter if a clear national standards book was produced and much of the detail such as parking standards were moved to local technical manuals that could be debated at the inquiry on the LDP. These manuals would also set out s.106 criteria, possibly moving to a tariff basis to reduce uncertainty (ODPM is proposing

[28] Ref. BRTF 2004: 14

that a range of options, including tariffs, could be considered but a single route would be clearer, and councils are moving toward a tariff-based approach).

- It was suggested to us that several PPGs, PPSs and RPGs are well out of date - for example PPG 4, covering industrial, commercial development and SMEs, was produced ten years ago. They should be updated more regularly to reflect changes in markets and business. PPG 3 (Housing) has been reviewed, but in addition to PPG 4, PPGs 2 (Green Belt), 15 (Historic environment) and 16 (Archaeology) all need to be updated.

- The burden on applicants and planning officers could be reduced through expanding Deemed Consent.

- While there should be no restriction on the right of residents to make representations on planning applications, it was felt that an incentive is needed to discourage activity at the decision-making level that may be considered to be either vexatious or at odds with Evidence-Based Decision Making principles and which may lead to wasted resources through fighting unnecessary appeals or awards of costs against resource-constrained Councils. At the same time, we were conscious of the strain that the current volume of appeals places on the system. We would therefore propose that

  - an authority's unreasonable behaviour or failure to produce evidence should be subject to stricter censure. In order to encourage more careful debate on applications, ODPM should review the procedure for awards where appeals or Local Government Ombudsman determinations not only overturn decisions or censure procedures but award costs against the planning authority – as DoE Circular 8/93 comments, *"The availability of costs awards, on specific application, is intended to bring a greater sense of discipline to all parties involved in planning proceedings."* To this should be added the establishment of an audit trail to show how Councillors voted on planning matters and whether they were acting against officers' advice, with the information published annually as part of the Council's audit report. We believe that this would not prevent proper consideration of planning matters by Councillors but would reduce occurrences of refusal not based on planning merits.

  - where Committees endorse officers' advice and a cost award is made on appeal, such costs should be deducted from any Planning Delivery Grant made to the Authority or from its own resources in the absence of Grant. All planning officers should have performance assessments based on their delivery of advice to Committee, so where an officer recommends refusal and this is overturned on appeal with or without costs, such matters should be subject to the officer's performance review. Where officers consistently perform at a high level (say an 80% and above success rate) they should be eligible for a bonus payment from the Planning Delivery Grant, which should be ring-fenced for this purpose. Clearly, where costs are awarded against a Council where Members follow an officer's advice no such bonus should be payable. This performance data should be published annually to identify poor performance and also recognise good performance from Members and officers.

Cost awards against planning authorities are made in only a minority of cases and only on grounds of unreasonable behaviour[29] causing the claimant to incur unnecessary or wasted expense, but as with Regulatory Impact Assessment (see 38. above) and a range of ministerial decisions under statutory powers, where the prospect of Judicial Review can help to deter departure from evidence-based processes, we believe that the threat of superior action would encourage greater care in decision making (producing full evidence to support refusal of planning permission is a defence against a charge of acting unreasonably) without limiting councillors' right to raise concerns on behalf of their constituents.

- Public consultation should be focused on Community Plans (which cover issues such as mast siting). Consultation on Local Development Frameworks should be restricted to spatial planning issues such as land use – in other words, non-planning items should be excluded from the planning process.

- Greater scope should be offered for the option of dispute resolution ahead of/after the inspector's hearing in order to streamline hearings and reduce the need to appeal. Appeal costs should be loaded as an incentive to settle earlier but Government guidance would be needed on award discretion in order to avoid undue disincentive to appeal (eg individual councillors appealing against a plc's application).

- Call-In should be limited to genuine national projects. Others should be handled regionally. This should not represent a major democratic loss since Ministers have historically almost always agreed with inspectors.

- One option, albeit a possibly controversial one, could be for planning authorities to offer a two tier service under which, in return for higher charges, applications could be fast tracked. This happens already in some authorities through, for example, asking applicants to fund additional planning officers to process large cases such as Heathrow Terminal 5. It is important that governance safeguards are put in place to limit the scope for this to be seen as a charter for developers.

67. However, the issue of resource remains. As one witness told us, "you can make all the procedural or legislative changes that you like, but it's all irrelevant if there are simply not enough people to handle the workload." It was suggested to us that poor pay, image and morale have led to fewer people attending planning courses at university and therefore becoming professional planners. Barely 2,500 people under the age of 30 are members of the Royal Town Planning Institute. When that is contrasted with the 4,500

[29] Unreasonable actions giving rose to a costs award include failure to comply with normal procedural requirements for inquiries or hearings; failure to provide evidence to substantiate reasons for refusing permission; failure to take account of relevant policy statements in Departmental guidance or relevant judicial authority; refusal to discuss an application or provide requested information, refusal of permission for a modified scheme when an earlier appeal decision indicated this would be acceptable and circumstances have not materially changed; failure to carry out reasonable investigations of fact, or to exercise sufficient care, before issuing an enforcement notice; introducing an additional reason for refusal, or abandoning a reason for refusal at a late stage; imposing unnecessary, unreasonable, unenforceable, imprecise or irrelevant conditions; pursuing unreasonable demands or obligations in connection with a grant of permission; failure to renew an extant or recently expired planning permission, without good reason - DoE Circular 8/93.

who are aged between 41 and 50, nearly 4,000 who are aged 51-60, it was difficult not to conclude that under the Planning Service is a demographic time bomb. The Government has introduced a bursary scheme covering 144 places at planning schools across the country but it will be some time before this feeds through. Elsewhere, it has introduced the Planning Delivery Grant - £130m in 2004 and £170m this year, which while a good start still has to overcome the obstacle of attracting young people to the profession. *Planning* magazine estimates the recruitment shortage to be up to 6,000 planners (4,000 standard planners and around 1,800 transport planners) with the bulk of the problem in London and the South East (one third of planning posts in London are either vacant or filled by staff on temporary contracts).

68. This was coupled by our witnesses to shortcomings in training. Concern was expressed over poor understanding by planners and councillors of development economics, which impacts on any negotiations for planning gain. More importantly, 70% of councils have no compulsory training of councillors in planning, which means that developers hold detailed talks at officer level at which an assumption of success may be created but with the risk that their proposals may be rejected by the Planning Committee against advice from the council's own planners. Training should be compulsory for all members who sit on such committees. Small steps have been taken to address this: for example, English Heritage has recently launched its internet-based HELM project which tries to educate on taking account of heritage and architectural issues in the planning process.

> There's the issue of resourcing of local planning authorities. The mobile operators now have systems in place that oversee consultation with LPAs at annual rollout and pre-application stages. Some planning officers are making a real effort, but the overall level of engagement with the industry remains a concern. Without this engagement, it is difficult for the operators to identify the most appropriate sites for development, and to gauge the appropriate level of community consultation. This clearly has implications further down the planning process, when some of these issues are difficult or expensive to resolve.
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> *Mobile Operators Association*:

69. Allied to this, witnesses suggested that in the absence of adequate staffing levels, the new target-based planning system has led to a deterioration in quality. Planning departments should determine 80% of minor and major applications within eight and 13 weeks respectively. It was reported to us that many are blocking difficult applications or using what one witness referred to as "sharp practices" in order to meet the deadline. The halving of the deadline for making an appeal to three months led to a 21.5% jump in appeals for the Planning Inspectorate to work through. The Inspectorate has admitted that it will not meet any of its performance targets and it has now bought a breathing space by reverting to a six month limit, but the underlying resource-based problem of significant delay remains, with most inquiries taking a year. Witnesses claimed that even basic site visits can take a year to organise, slowing the system still further.

70. Applicants could also take steps to reduce the scope for risk arising in the process through embracing community consultation. The Rowntree Foundation looked in

2004[30] at how local people in key parts of the South East developed their opinions about proposals for new housing, although some of the principles can be applied to other developments. The key message of its study is to start early, consult widely and take the heat out of issues by preempting many of the arguments.

Pharmaceuticals

71. We took initial evidence on this sector with the intention of including pharmaceuticals as a more detailed sub-study in a subsequent report. The paragraphs that follow summarise submissions from branded generic and generic manufacturers.

72. Witnesses suggested that the Pharmaceutical Price Regulation Scheme, which sets the framework for prices paid by the NHS, can increase regulatory uncertainties. It was believed that periodic renegotiations (the current scheme runs for five years, with an option for both government and industry to call for a mid-term review) create an environment of uncertainty and operate to timescales that do not necessarily match investment planning horizons, particularly for smaller companies or those reliant on limited domestic or European product networks. It was felt that ad hoc price cuts when the PPRS is renegotiated add to this uncertainty, and limited scope for adjusting pricing clouds decisions about how to respond to changes in the market environment. Witnesses reported that it is not uncommon for investment decisions to be postponed close to or during PPRS renegotiations, which themselves can be lengthy.[31]

73. Concern over risk focused on the Medicines and Healthcare products Regulatory Agency. On the one hand, we were told that during the recent renegotiation of European pharmaceutical law the MHRA had consulted industry assiduously and carefully weighed the arguments of the branded, generic and over the counter sectors. It held regular meetings with representatives of all three sectors to review progress and, where possible, to coordinate activity. Bilateral meetings were also held between the Agency and the representatives of the different industry sectors to debate contentious issues. Where there was a definable common UK interest, all parties were able to work together to pursue that interest. It was described as “an almost textbook approach”.

74. However, it was felt that uncertainty had been created over what was perceived as the MHRA seeking to take the lead in adopting unilateral interpretations of some of the measures in the resulting EU legislation rather than waiting for the European Commission to publish its own interpretation. In addition, it chose to implement certain provisions without a clear understanding of how they might operate in practice. On user testing, for example, discussions continue between the MHRA and the industry on how best to implement the requirement even though the implementing SI has come into force (though its provisions do not yet apply). The industry protested to the MHRA that early implementation would distort international competitiveness and that the approach taken, in particular the failure to consult separately on draft legislation, failed to meet Cabinet Office best practice guidelines. The Agency informed the industry that the Cabinet Office had agreed to waive the normal procedures because this was a patient safety matter but

[30] cf *Housing Futures - informed public opinion*, Joseph Rowntree Foundation, 1994

[31] The latest renegotiation took place over one year and the confidentiality of the process meant that companies had no information on the likely size of price cuts imposed.

did not produce evidence to support the claim that early implementation and the waiving of CO requirements were necessary.

75. We were given further examples where the MHRA's interpretation of the revised EU legislation may, through adopting interpretations of existing EU legislation out of step with the majority of other Member State agencies and the views of the European Commission, place greater burdens on industry in the UK that will be faced in other Member States. In the majority of cases, the MHRA has eventually had to fall into line with the rest of Europe following decisions by the European Court of Justice. It was claimed that this is damaging to the competitiveness of the British industry, to the NHS, and to patients. We recommend, therefore, that in future the MHRA should seek to apply and implement EU pharmaceutical regulatory legislation in harmony and in step with its European partners.

76. UK industry and NHS patients have also, we were told, potentially suffered because of the lack of resource at the MHRA. It is clearly right that medicines should not be marketed until they have been properly assessed and authorised by the Agency. It is important, however, for both the originator and generic sectors, that assessment and issue of the appropriate marketing authorisation is carried out in a timely fashion. The originator industry needs to launch new products as quickly as possible to protect its cash flow. Generic manufacturers need to launch their products as soon as possible after the expiry of intellectual property protection of the originator product: a company that is slow to get to the multisource market with a new generic is inevitably damaged commercially.

77. It was also put to us that the Industry faces increased risk due to devolution and the proliferation of agencies concerned with ensuring patient safety and cost effectiveness within the NHS. We heard of examples where investigations carried out by NICE were subsequently repeated in Scotland; and where Welsh Ministers were considering issuing their own guidance on the use of particular classes of medicine which had already been assessed by the MHRA and NICE, and where the medical professions had their own guidance in place. This can only add to confusion in the marketplace. Greater coordination is necessary.

Pensions

78. We also took initial evidence on this sector on the same basis as pharmaceuticals.

79. Among the issues highlighted by witnesses were

- Uncertainty over the way in which the Financial Ombudsman Service (FOS) may make decisions in responding to future complaints by consumers. It was suggested that this may constrain some firms from entering the market for stakeholder pensions when the proposed 'light-touch' basic advice regime is introduced by the Financial Services Authority.

- Frequent changes made by Governments to the structure and levels of state pensions, potentially changing the ground rules on which previous pension decisions were made. It has been assessed that such changes have resulted in the annual real

internal rate of return on the second-pillar state pension (SERPS) for the average male worker falling from 5% to 1.5% over the last quarter century[32]. It was claimed that the complex interaction between state and private pension saving (contracting-out) and income (notably pension credit) creates major risks, raising questions for large sections of the population about the value of pension saving, adding to the costs of selling, and leaving insurers and advisers vulnerable to subsequent redress if sales are later judged to be unsuitable.

80. Among solutions proposed to us and which may be examined at a later date were

- Adoption of the Treasury Select Committee recommendation that stakeholder price caps should be set by an independent body after clear and transparent analysis. Best practice in other price regulated sectors suggests that the process of setting the cap would be enhanced by clear timetables, open consultation, independent economic analysis and a right of appeal.

- The Pensions Regulator should have a statutory duty, similar to that under which the FSA operates, to conduct cost:benefit analysis on new proposed Codes of Practice.

- Measures to reduce the likelihood of unpredictable but significant FOS rulings. Greater formality and clarity is needed to facilitate external input when the FOS makes decisions on cases with wider implications, and issues should be referred to the FSA where appropriate.

- More radical solutions might transfer major political decisions on pensions – such as the state pension age or basic state pension levels – to independent advisory bodies. At the very least, the Pensions Commission (which the Government established to advise it on the case for compulsory saving) should become a permanent feature of the pensions landscape to reduce the likelihood of arbitrary decision-making. There are however clear constraints on MPC-style solutions given both that there are few obvious focussed objectives that could be set for such a body and the political nature of these issues.

[32] *What is a Promise from the Government Worth? Measuring and Assessing the Implications of Political Risk in State and Personal Pension Schemes in the United Kingdom*, David Blake, UBS Pensions series 13, LSE Financial Markets Group Discussion Paper DP457, July 2003

Conclusions

81. At the end of nine months of work, the Commission was left with several important questions drawn from the evidence it received:

- Despite the many statutory and administrative controls that already exist, policy decisions emerge from a system that can be undisciplined: statements creating expectations can be reversed; political judgements about priorities can be unpredictable; timetables are frequently overrun (or not even set), and so on. Should we regard the risk that this creates as an acceptable price to be paid?

- Many sector regulators regard the giving of clear signals to markets and operating on a "reasonable expectations" basis as fundamental to the reduction of risk. Whitehall and the European Commission have no such culture or protocols. Why?

- Why have some Departments and bodies found it so easy to introduce systems that reduce uncertainty by easing and widening access to information and why have so many others been sluggish or resistant?

- Why is the system so apparently coy about demonstrating that decisions have properly balanced available evidence?

- Given that public confidence in politicians generally low, why has the system, both here and in Brussels, only taken isolated steps to improve faith in its governance?

Counting the cost of Brown's U-turn over property tax
More than 80 providers of self-invested personal pensions (SIPPS) were yesterday counting the cost of the Government's last-minute u-turn on residential property investment.

Financial services companies acused Gordon Brown of misleading them after the Chancellor's pre-Budget report evealed tax breaks that were due to be introduced in April were being abandoned. Mr Brown said SIPP investors would not, after all, be allowed to buy residential property – or a range of exotic investments such as fine wine and art – at up to a 40 per cent discount.

Tim McPhail, head of pensions at Hargreaves Lansdown, one of the country's biggest independent financial advisers, said: "If every Sipp provider has done as much work preparing for this reform as we have, the amount of money that has been spent in vain will run into several hundred million pounds."

David Baker, a director of James Hay, the Abbey Bank-owned company that is the UK's largest Sipp provider, said: "We've certainly spent six-figure sums that will now be wasted – we've had a full-time team working on this for the past 12 months and we've also had to take specialist IT and legal advice." Mr Baker rejected suggestions that the Government's reforms were always subject to last-minute amendment. "We took the view that once the draft regulations were published in the summer, we had to take this work seriously."(…)

Independent, 7 December 2005

82. We sought solutions, not answers, and we approached our task on the assumption that all parts of the system, here and in Brussels, can learn from best practice examples – clearer signals, more predictable timing, demonstrating proportionality, reducing scope for suspicion and misunderstanding through more transparent decision making, easier access to information, and demonstrating workability before EU proposals are agreed.

83. The class leaders, examples from whom are featured in our text, have shown that it is possible to put in place mechanisms that improve certainty without unreasonably restricting freedom of manoevre, although in some cases restriction (whether through the threat of legal challenge, more clearly defining the basis for political intervention or the imposition of evidential requirements) may by increasing confidence and objectivity both benefit the policy process and reduce risk.

84. They have realised that, media inaccuracies aside, uncertainty arising from imperfect knowledge of policy or regulatory mechanisms is not in their interests or those of parties affected by their activities.

85. And they have accepted that risk can be reduced and engagement boosted through a realistic explanation of the policy or regulatory process, perhaps following the example set by the "Approach Documents" produced by some regulators, as an integral and initial consideration. They have seen the advantages of agreeing approaches or methodologies with stakeholders and of setting out decision parameters early in the process.

> One of the questions frequently asked [in relation to major reviews] is 'what happens when, inevitably, events move on beyond the original assumptions'? We have accordingly published a change protocol setting out for all stakeholders how [we] will approach such change. This offers the companies and others clarity on one important aspect of their decision whether or not to appeal to the Competition Commission for redetermination of price limits. It was subject to consultation before it was finalised.
>
> Sector regulator

86. The extent to which risk has undesirably influenced corporate performance may perhaps have been exaggerated by some of our survey respondents and would be difficult to calculate to any meaningful degree of accuracy, but in many ways that is not the point because, as we have observed, risk need not be *experienced*: it exists if it is merely *perceived*, and we concluded that assumptions are probably as significant as concrete exposure to political and regulatory risk in affecting strategy and investment decisions.

87. But, while it was evident that the impact of uncertainty was neither immaterial nor isolated and should be addressed, we also accepted that businesses and financial institutions may contribute to the risk they face. Political and regulatory risk may arise as much through the creation of unnecessary exposure as through the action of the public sector. Company directors and financial institutions need to embrace the monitoring and assessment of political and regulatory risk and accept that it is as integral a governance

requirement under the Combined Code and successive interpretations of it[33] as is direct financial risk mitigation. Improving risk management may reduce actual risk by developing more accurate perceptions of the policy process.

88. This applies in similar measure to Whitehall, public bodies and the European Commission: few senior officials have had experience of working within, let alone running, the types of organisations to whom they seek to apply policy or regulation. While secondments are becoming more commonplace (in the UK at least), greater exposure to contextual training is needed if policy makers are to develop an ingrained culture of appreciation of the factors that contribute to risk.

89. Business must also accept that risk will often cut both ways – one company's assertion of the damaging unpredictability of a politically-driven U turn may be another's windfall, considered as "welcome flexibility". That poses the further question of what happens when reduction in business risk can be achieved only at the cost of a possible increase in, for example, consumer risk; and who should reconcile competing evidential claims. We concluded that there are some circumstances in which that can be better resolved through delegation of the decision to independent specialists working within politically-set parameters and accountable to Parliament. In others, it should not be sufficient for governments to claim a form of public interest immunity from having to justify the principle that Ministers Decide: Ministers should have to explain why they are best placed to be the ultimate decision maker.

90. In drafting solutions, we deliberately concentrated on mechanics; on administratively realistic and relatively mundane changes, and we sought to ensure that our recommendations would benefit the public, and not just narrow business interest. One proposal, the strengthening of Regulatory Impact Assessment through converting what are currently no more than guidelines into the more formal duty that already applies to some regulatory bodies[34], would necessitate legislation, although the progressive incorporation of the RIA requirement into all new legislation or regulation containing decision-making powers would be a start that would not require additional parliamentary time. Another, the creation of a new impact assessor or the transfer of scrutiny responsibility to the National Audit Office, will involve additional resources. Of a total of forty recommendations in this report, only one other – the clearer delineation of ministerial power – might be considered controversial, but even then we have in part sought to build on several existing precedents.

91. One key word appears regularly in this report. Confidence. Organisations (and individuals) need to believe that the process of government will operate evidentially and without undue favour. They need to understand how it will operate. They need to know when the process will operate; and that when it does, it will do so on the basis of consistency. Given the concern shared by all political parties over declining engagement with the governed, it is in their interest to seek to address the lack of confidence that feeds risk.

It is all about trust.

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[33] *Internal Control: Guidance for Directors on the Combined Code*, ICAEW 1999; *Independent Review of Non-Executive Directors*, DTI 2003. See also *Building Better Boards*, DTI, 2004; Companies Act 1985 (Operating and Financial Review and Directors Report Regulations) 2005.

[34] The Environment Agency, Financial Services Authority, Food Standards Agency and Ofcom

Summary of findings and recommendations

How great a problem is it?

- 63 per cent of survey respondents believed that political/regulatory risk considerations had inhibited their investment decisions or forecasts, 48 per cent that they had increased the cost of capital or influenced the structure of corporate finance packages, and 69 per cent that such considerations had inhibited corporate strategy decisions (9).

- The most significant risk factors were regarded as uncertainty over the criteria to be taken into account in making policy/regulatory decisions, uncertainty as to the outcome of policy processes, concern that costs and benefits will not be fairly calculated/balanced, and uncertainty as to whether politicians or regulators will intervene (9).

Limits on the ability to reduce risk

- Although political control is considered important in order to retain democratic accountability, the way it is exercised should perhaps be reconsidered if confidence in politicians is low. (23).

Candidates for political withdrawal/improved impact assessment

- Political involvement in the policy process does not necessarily increase risk, but because Whitehall and Brussels at present do little to explain how they will reach or have reached decisions, concerns over the way evidence is balanced are greater than they might be, and the perception of risk is therefore higher than it might be (26). Government has acknowledged that this can be a problem in certain areas by delegating responsibility for monetary policy and for most competition and many other regulatory decisions to apolitical expert bodies subject to policy frameworks set by Ministers (27).

- Candidates for political withdrawal should be drawn up in areas involving price or standard-based regulation, where determination can be left to expert bodies working within ministerially-set parameters (29).

- Stricter timetabling, consistent with the practice followed by several regulators, and horizon-setting (creating a reasonable expectation that policy frameworks will not be significantly amended for a declared period) should be introduced (29). Timetabling should be tested through three pilots spread over different Departments and involving a major policy development exercise, a policy review, and a Bill. It should only apply to the parliamentary stage of the process in extremis (33-34).

- Ministers should determine whether the public interest requires them to be the ultimate decision maker and should be prepared to justify that role. (30).

- There should be a presumption in favour of the publication of research, internal analysis or external advice and that it should be incumbent on the system to explain any departure from it (32).

- Government should produce regularly updated three year or full-Parliament legislative programmes as a development of existing departmental five-year plans (35).

- UK and EU bodies should adopt the Scottish Executive's practice of posting on its website a forward consultation schedule (35).

- Ministers will have to decide whether giving greater structure to the process is an acceptable price to play for an increase in faith in that process and therefore a reduction in perceived and actual risk. Our proposals seek to raise trust in political decision-making to the same level as that enjoyed by the judiciary (36).

- Whitehall and Brussels should borrow from DG Competition's Best Practice Guidelines for mergers, where State of Play meetings are offered to discuss the development of thinking on cases, allowing assumptions on outcomes to be steadily built up rather than sprung upon affected sectors and their financiers (37).

- One option to encourage greater use of horizon-setting could be the seeking of views on reasonable investment/certainty horizons as part of initial consultation. Policy or regulation could then be set on a detailed framework basis. The State of Play review would also include ex-post assessment of actual compared with forecast costs and benefits, with the option of subsequent consultation on amendment, strengthening, or relaxation (38).

- Regulatory Impact Assessment could more effectively be used to make the system more punctilious about Evidence Based Decision Making. One option is to give independent status to the Better Regulation Executive, which could be empowered to undertake RIA independently and require that a proposal failing should, if necessary, fall or its owner renew it with a public explanation (39-40). An alternative would maintain the BRE's role during the drafting process but empower the NAO to review all RIAs between ministerial sign-off and Council political agreement or, for UK-originating measures, implementation of the policy in question or the parliamentary stages of legislation. In practice, this would involve auditing the governance of the RIA process, assessing compliance against a set of tests (41).

- The RIA process should either become statutory, allowing ministerial proportionality decisions to be judicially reviewed, or a Regulatory Appeals Tribunal should be established to cover all cases which do not currently fall under the jurisdiction of the Competition Commission (43). At the very least, it could be progressively introduced through incorporating in new legislation an RIA requirement in respect of decisions made under that Act (Note 14).

- A closer relationship between the Public Accounts Committee and the Better Regulation Commission and Executive, possibly taking the form of an annual performance review, would be welcome (44).

- As an interim measure, around 20% of Assessments should be examined against the proposed tests, with a smaller number being subjected to the current depth of review (46).

- The Conciliation stage of the EU legislative process currently operates behind closed doors and is exempt from Impact Assessment requirements. Compromises are produced with little explanation and no analysis of costs and benefits. Clarity and accountability are as important at that stage as at any other (48).

Transposition risk

- Common Position should not be reached until draft implementation plans have been submitted to the Council Bureau and posted on line. Initial consultation on transposition should become part of the RIA process, with views on costs, benefits and implementation options being invited while proposals are at Working Group stage (53-54).

- Widespread introduction of automatic notification of material produced by the system would make an appreciable contribution to the reduction of risk by limiting one of its factors – imperfect communication (54).

- Transposing Directives verbatim is not an effective remedy. Thin or unclear legislation only creates a demand for detailed guidance notes, in the absence of which the apparent reduction in Red Tape would in most cases be offset by an increase in risk (55).

Enforcement and interpretation

- If the Environment Agency had the autonomy of other agencies such as the Health and Safety Executive and the Food Standards Agency it could take total responsibility for regulatory policy and implementation, enabling more independent and holistic approaches to regulation and offering greater clarity about responsibility and communication (59).

- Regulatory responsibilities could be transferred from local authorities to the relevant central government agencies (62).

- HSE and EA are seeking greater inter-agency co-operation but are hampered by different legislative and institutional regimes. This suggests the more radical solutions flagged by the Hampton Review, namely greater consolidation of regulatory activities (63).

- HSE, for example, publishes its guidance to inspectors, much of it on the web. This practice is to be encouraged (63).

- Greater co-operation is needed between business, government and worker/ environmental representatives at the drafting stages of legislation. This would involve fora where these groups could focus on practical implications (63).

- Greater co-operation is needed between stakeholders about compliance solutions. It is possible, for example, that two track compliance schemes should be given greater attention (63).

Planning

- Local Plans should be monitored on a rolling annual basis, with the possibility of a fast track process. Plans should set out areas where capacity is coming on stream and then establish a simplified planning system within those zones (66).

- Local Development Plans could be shorter if a clear national standards book was produced and much of the detail was moved to local technical manuals. These manuals would also set out s.106 criteria, possibly moving to a tariff basis to reduce uncertainty (67).

- The burden on applicants and planning officers could be reduced through expanding Deemed Consent (67).

- An authority's unreasonable behaviour or failure to produce evidence should be subject to stricter censure. In order to encourage more careful debate on applications, ODPM should review the procedure for awards where appeals or Local Government Ombudsman determinations not only overturn decisions or censure procedures but award costs against the planning authority. An audit trail should be established to show how Councillors voted on planning matters and whether they were acting against officers' advice, with the information published annually as part of the Council's audit report (67).

- Where Committees endorse officers' advice and a cost award is made on appeal, such costs should be deducted from any Planning Delivery Grant made to the Authority or from its own resources in the absence of Grant. All planning officers should have performance assessments based on their delivery of advice to Committee, so where a refusal recommendation is overturned on appeal with or without costs, such matters should be subject to the officer's performance review. Where officers consistently perform at a high level they should be eligible for a bonus payment from the Planning Delivery Grant, which should be ring-fenced for this purpose (67).

- Public consultation should be focused on Community Plans. Consultation on Local Development Frameworks should be restricted to spatial planning issues such as land use – in other words, non-planning items should be excluded from the planning process (67).

- Greater scope should be offered for the option of dispute resolution ahead of/after the inspector's hearing in order to streamline hearings and reduce the need to appeal. Appeal costs should be loaded as an incentive to settle earlier but Government guidance would be needed on award discretion in order to avoid undue disincentive to appeal (67).

- Call-In should be limited to genuine national projects (67).

- Training should be compulsory for all planning committee members (68).

- Applicants could take steps to reduce risk through embracing community consultation (70).

Other

- Despite the many controls that already exist, policy decisions emerge from a system that can be undisciplined: statements creating expectations can be reversed; judgements about the relative weight of public versus business interests can be unpredictable; timetables are frequently overrun (or not even set), and so on. Should we regard the risk that this creates as an acceptable price to be paid? (81).

- Many sector regulators regard the giving of clear signals to markets and operating on a "reasonable expectations" basis as fundamental to the reduction of risk. Whitehall and the European Commission have no such culture or protocols. Why? (81).

- Why have some Departments and bodies found it so easy to introduce systems that reduce uncertainty by easing and widening access to information and why have so many others been sluggish or resistant? (81).

- Given that public confidence in the policy process and the role of decision makers is generally low, why has the system, both here and in Brussels, only taken isolated steps to improve faith in its governance? (81).

- A realistic explanation of the process, perhaps following the example set by the "Approach Documents" produced by some regulators, should be an integral and initial consideration in any consultation exercise, with approaches or methodologies being agreed with stakeholders early in the process. Similarly, where they are foreseeable, decision parameters should be set out at an early stage in the process (85).

- There should be a presumption in favour of publishing information on evolving thinking on the application and enforcement of regulatory rules. Decisions on the application of such rules should be shared with all market participants to avoid information asymmetries (p.8)

- Company directors and financial institutions need to embrace the monitoring and assessment of political risk and accept that this is an integral governance requirement under the Combined Code and other corporate governance requirements. Improving risk management may reduce actual risk by developing more accurate perceptions of the policy process (87).

- Few senior officials have had experience of working within, let alone running, the types of organisations to whom they seek to apply policy or regulation. Greater exposure to contextual training is needed if policy makers are to develop an ingrained culture of appreciation of the factors that contribute to risk (88).

ANNEX 1 – RISK COMMISSION STRUCTURE

The following participated in the work of the Commission. Positions are those held during the term of the Commission's work

Bob Armitage (Director, Merck)

Henry Bellingham MP (Conservative employment spokesman)

Edward Blades (DTI observer)

Michael Chambers (Director of Policy, Royal Institute of Chartered Surveyors)

Tony Collins (Partner, Atis Real Weatheralls)

Dr Dan Corry (Director, New Local Government Network; former DTI Special Adviser)

Jitesh Gadhia (Managing Director, Corporate Finance, ABN AMRO)

Ian Gregory (DTI observer)

Brian Harte (Director, Group Head of Compliance and Regulatory Affairs, Barclays plc)

Lord Haskins (former Chairman, Better Regulation Task Force)

Simon Holmes (partner, S J Berwin)

Prof. Bridget Hutter (Director, Centre for Analysis of Risk and Regulation, London School of Economics)

Sharmin Joarder (Better Regulation Executive observer)

Alan Kemp (Director, Haymarket plc; former Special Adviser, DTI and DoE)

James King (Policy Adviser, Regulation and Strategy Team, Association of British Insurers)

Rt Hon Francis Maude MP (former DTI, Treasury and Foreign Office Minister)

Charles Miller (Regulatory Policy Institute)

Huw Morris (Editor, *Planning*)

Simon Oates (DTI observer)

Craig Pickering (consultant and former Head of Asset Finance, Finance and Leasing Association; former Head of Industry Division, H M Treasury)

Hilary Plattern (Director of Public Affairs, Clifford Chance)

Stephen Rea (Government Affairs, Shell UK)

John Rhys (Managing Director, NERA)

Richard Ritchie (Director, UK Government Affairs, BP)

Sue Slipman (Chairman, Financial Ombudsman Service)

Warwick Smith (Secretary, British Generic Manufacturers Association; Chairman, Citigate Public Affairs; former Departments of Environment and Transport official)

Iain Taylor (Director of Regulation, Centrica)

James Walsh (Policy Unit, Institute of Directors)

Sir Steve Robson (former H M Treasury official; Director Cazenove, XStrata and Royal Bank of Scotland) and John Denham MP (Chairman, Home Affairs Select Committee; former DSS, Department of Health and Home Office Minister) also contributed to the Commission's work, but not to the final report

ANNEX 2 – RISK COMMISSION SURVEY

We sent the following questionnaire by mail and email to 1015 targets comprised as follows:

- 541 companies (all FT 250, Social Market Foundation Business Forum members, and others randomly selected from the aerospace and defence, construction, energy, chemicals, property, engineering, pharmaceuticals and healthcare, leisure, media, financial services, technology and communications, retailing, utilities and miscellaneous industrial sectors)
- 23 targets in five retail banks
- 190 directors of 28 investment banks
- 81 Extel-rated analysts covering significantly regulated or "policy heavy" UK and EU sectors in 33 institutions
- 112 managers covering the leading rated UK and EU-focused funds in 41 institutions
- 65 individuals in the corporate finance and consulting arms of seven accounting firms

392 responses (227 corporate; 165 City) were received.

Political and regulatory risk
How significant is it in shaping corporate finance, investment and corporate strategy decisions?

The Social Market Foundation has established a Risk Commission to assess the scope for reducing uncertainty and business risk over the outcome of UK/EU policy or regulatory processes and decisions. As part of our work, we are seeking to survey a selection of companies, business bodies and financial institutions to determine whether political/regulatory factors have materially inhibited investment decisions or corporate strategy planning. We would be grateful if you could assist us with the survey, on the express understanding that the identity of respondents will not be published or disclosed to Government or to members of the Commission. All respondents will be sent a copy of the survey results.

Category of respondent	Please tick one
Bank (general)	
Bank (corporate finance)	
Fund manager	
Analyst	
Corporate	

1. [Corporates] If you regard your sector/company as being materially influenced by political/regulatory activity

[Financial institutions] In sectors which you regard as being materially influenced by political/regulatory activity

How significant are considerations of political/regulatory risk in shaping investment/ corporate strategy?

Significant	*387*
Not significant	*5*

2. This section examines 1. in greater detail

Political/regulatory risk considerations have inhibited your investment decisions/forecasts	*63%*	
Political/regulatory risk considerations have increased the cost of capital/influenced the structure of corporate finance packages	*48%*	
Political/regulatory risk considerations have inhibited corporate strategy decisions	*69%*	

3. Those who answered YES to any of 2. were asked to rate political/regulatory risks from 1 (not significant) to 5 (highly significant). The scores are averages

Uncertainty as to whether politicians/regulators will intervene	*4.16*
Uncertainty as to the outcome of policy processes	*4.22*
Uncertainty as to the outcome of regulatory processes	*4.05*
Uncertainty as to the timing of policy decisions	*3.83*
Uncertainty as to the timing of regulatory decisions	*2.77*
Uncertainty over the criteria to be taken into account in making policy/regulatory decisions	*4.41*
Uncertainty as to the interpretation of statutory powers/duties by regulatory bodies	*3.80*
Risk that technical/specialist evaluation will be amended by politicians	*3.94*
Risk that technical/specialist evaluation will be amended by regulators	*2.45*
Concern that costs and benefits of policy/regulatory options will not be fairly calculated/balanced	*4.35*