



**regulatory capture
risk maturity assessment
consulting report**

centium 

Independent Pricing and Regulatory Tribunal NSW

FINAL August 2023

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summary report

Overview

IPART commissioned Centium to develop a tool for assessing IPART's risk maturity in relation to managing the risk of regulatory capture, and then to use that tool to undertake such an assessment.

The objective of this review was to:

- Identify and understand IPART's risk of regulatory capture
- Identify in relation to mitigating the risk of regulatory capture:
 - What IPART is doing well, and
 - Priority areas for improvement to ensure that IPART continues operating effectively in the public interest.
- Ensure that the regulatory capture risk management maturity tool and associated practice notes enable the easy use of the tool in a manner that will produce consistent, accurate and repeatable results.

This project was not part of IPART's approved Internal Audit Plan for 2022-23, but it is intended that future assessments using the tool may be included as part of IPART's cyclical Strategic Internal Audit Program.

This report is intended to be released publicly to promote awareness of this project and its results.

Context

'Regulatory Capture' is a term used to describe a situation in which a regulatory agency becomes controlled or unduly influenced by one or more regulated entities. Such control or influence may lead to the interests of regulated entities or interest groups being accommodated in a manner that overrides the public interest.

It is important that regulators remain alert to the risk of regulatory capture and take sufficient steps to avoid it. This helps to ensure that the regulator's activities continue to serve the public interest well, thereby retaining public confidence.

While at the outset of this project, IPART management did not believe that IPART had been subject to any significant regulatory capture, it is important to note that regulators may not be aware that they have been so captured.

It is therefore notable that IPART management commissioned this independent review.

Approach

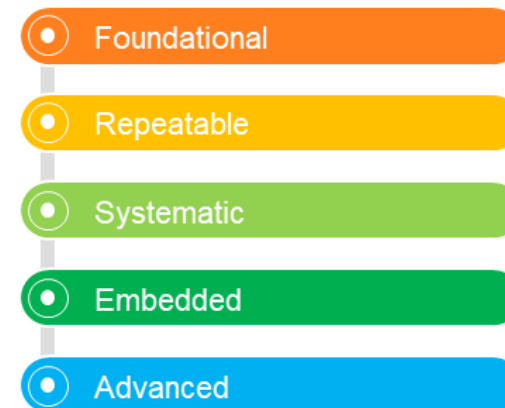
Regulatory Capture is difficult to measure as it inherently subjective and relates to the mindset of people employed by the regulator.

A degree of interaction between a regulator and regulated entities is considered to be healthy and necessary in order to identify and avoid situations where excessive regulation might have negative impacts on the public interest (e.g. by requiring excessive compliance costs or creating restrictive barriers to market entry).

Consideration of these two factors led to the use of a risk maturity approach to assess IPART's risk of regulatory capture. This approach allowed for a detailed and holistic examination of specific IPART regulatory functions in relation to the following risk attributes for regulatory capture:

- Adherence to public interest principles
- Culture of the regulator
- Regulator structure
- Regulator processes
- Transparency
- Staff experience and diversity.

The risk maturity approach we used rates the risk of regulatory capture on the following scale:



The criteria relating to each category is provided in **Appendix 2** of this report.

Regulatory Impact Criteria

In order to assess the potential impact of regulatory capture for a particular regulatory function, the following criteria were considered.

Public Interest

- Potential impacts of regulatory failure on the consumer
- Potential impacts of regulatory failure on market operators
- Potential impacts of regulatory failure on competition
- Other impacts of regulatory failure

Track Record

- Has the regulatory function been unduly influenced by regulated entities in the past?
- Have regulators of similar activities in other jurisdiction been unduly influenced by regulated entities in the past?

Public Perception

- Public perception of the regulator’s performance regarding this function
- Public perception of the regulator’s degree of influence regarding this function

Potential Impact	Minimum Recommended Maturity Rating

Sampling

A sample of IPART's regulatory functions were assessed by this project for regulatory capture risk maturity. These were:

- Water
 - Licensing and compliance
 - Pricing
- Local Government
 - Rates
 - Contribution Plans
- Energy Networks
- Energy Saving Scheme
 - Licensing and accreditation
 - Regulation and compliance.

In order to assess the regulatory capture risk management maturity of these regulatory functions, nominated IPART personnel were interviewed and a range of relevant documentation was reviewed.

Outputs from these activities were entered into the Regulatory Capture Risk Maturity Assessment Tool (RegCap RMAAT) in relation to the sampled regulatory functions to produce maturity ratings for each risk attribute and an overall rating.

The tool was also used to assess the potential impact that regulatory capture might have on these regulatory functions and recommend a minimum level of risk maturity for each function.

This recommended level of risk maturity then was compared to the assessed level in order to identify areas where IPART's risk maturity should be improved.

These assessments were validated by the nominated representatives for each regulatory function.

Summary of results

OVERALL RESULTS



All of the regulatory functions reviewed had an assessed overall regulatory capture risk management rating that was higher than or equal to its minimum recommended level.

All of the regulatory functions reviewed scored an overall regulatory capture risk maturity rating of **Embedded**, which is the second-highest available rating and reflects well on IPART's efforts to strengthen and reinforce its management of this type of risk.



All individual risk attributes that contributed to the overall regulatory capture risk maturity ratings were assessed as having a rating between **Advanced** (the highest level) and **Systematic** (the third-highest level).

The minimum recommended regulatory capture risk maturity level for each assessed regulatory function varied from **Repeatable** to **Embedded**. This was based on individual assessments of the potential regulatory impact of regulatory capture on each regulatory function of between Low and High impact.



While resourcing was sufficient to cover business-as-usual activity, resource pressures have the potential to limit IPART's capacity to effectively manage regulatory capture risk if not managed well. We noted that IPART is able to move resources between functions to address any additional regulatory demands it may face over and above business-as-usual.

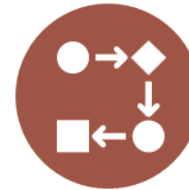
The assessments are summarised in the following table:

TYPES OF RATING	LOCAL GOVT	WATER	ENERGY NETWORKS	ENERGY SAVINGS SCHEME
OVERALL MATURITY				
Public Interest				
Culture				
Regulatory Structure				
Regulatory Process				
Regulator Transparency				
Staff				
POTENTIAL IMPACT				
MINIMUM RECOMMENDED MATURITY				

Positive findings



IPART has strong public interest objectives that are used to guide its regulatory activities.



IPART's regulatory processes are appropriate and there is consistent effort to simplify these processes and make them more efficient.



IPART's culture strongly reinforces the effective servicing of its public interest objectives.



IPART is almost reflexively transparent with its approach to regulation, which is vital for avoiding regulatory capture.



IPART's structure is appropriate for a regulator, with its high-risk decision-making being separated and elevated from the mechanics of regulation.



IPART staff are generally from mixed professional backgrounds. There are few key person dependencies and these appear to be managed effectively. There is little transit of staff between IPART and regulated entities.

LOCAL GOVERNMENT

IPART Independent Pricing and Regulatory Tribunal | NSW
Regulatory Capture Risk Management Maturity Assessment Tool

Subject Regulatory Function	Local Government
Date of Review	Jul 2023

Regulatory Capture Risk Management Maturity Rating Overall **Embedded**

Risk Attributes	
Public Interest	Embedded
Culture	Embedded
Regulator Structure	Systematic
Regulatory Processes	Embedded
Regulatory Transparency	Embedded
Regulator Staff Experience/Diversity	Embedded

Regulatory Capture Potential Impact Rating	High	Minimum Maturity Level	Embedded
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Scope of assessment

- Rate Setting
- Contribution Plans

Measures

- Minimum recommended maturity level = **Embedded**
- Potential Impact rating = **High**
 - Note: the **High** impact rating is based on the high public interest factors (e.g. waste, sewage, roads) and only moderate public understanding/acceptance of regulated actions.

Key results

- Overall Risk Maturity Rating Regulatory Capture = **Embedded**
 - 5/6 Risk Attributes rated as **Embedded**
 - 1/6 Risk Attributes rated as **Systematic**

The rating of Systematic is mainly due to resourcing pressures arising from special requests

WATER

IPART Independent Pricing and Regulatory Tribunal | NSW
Regulatory Capture Risk Management Maturity Assessment Tool

Subject Regulatory Function	Water
Date of Review	Jul 2023

Regulatory Capture Risk Management Maturity Rating: Overall **Embedded**

Risk Attributes	Rating
Public Interest	Embedded
Culture	Embedded
Regulator Structure	Systematic
Regulatory Processes	Embedded
Regulatory Transparency	Advanced
Regulator Staff Experience/Diversity	Embedded

Regulatory Capture Potential Impact Rating: **Medium** Minimum Maturity Level: **Systematic**

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Scope of assessment

- Regulation & compliance
- Pricing

Measures

- Minimum recommended maturity level = **Systematic**
- Potential Impact rating = **Medium**
 - Note: the **Medium** impact rating is based on the high public interest impacts (e.g. safe, reliable drinking water) and reasonable public acceptance of regulated actions

Key results

- Overall Risk Maturity Rating Regulatory Capture = **Embedded**
 - 5/6 Risk Attributes rated as Embedded or Advanced
 - 1/6 Risk Attributes rated as **Systematic**

The rating of Systematic is mainly due to resourcing pressures in Pricing

ENERGY NETWORKS

IPART Independent Pricing and Regulatory Tribunal NSW
Regulatory Capture Risk Management Maturity Assessment Tool

Subject Regulatory Function	Energy Networks
Date of Review	Jul 2023

Regulatory Capture Risk Management Maturity Rating Overall **Embedded**

Risk Attributes	
Public Interest	Embedded
Culture	Embedded
Regulator Structure	Embedded
Regulatory Processes	Embedded
Regulatory Transparency	Embedded
Regulator Staff Experience/Diversity	Embedded

Regulatory Capture Potential Impact Rating **Medium** Minimum Maturity Level **Systematic**

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Scope of assessment

- Energy Networks Regulation

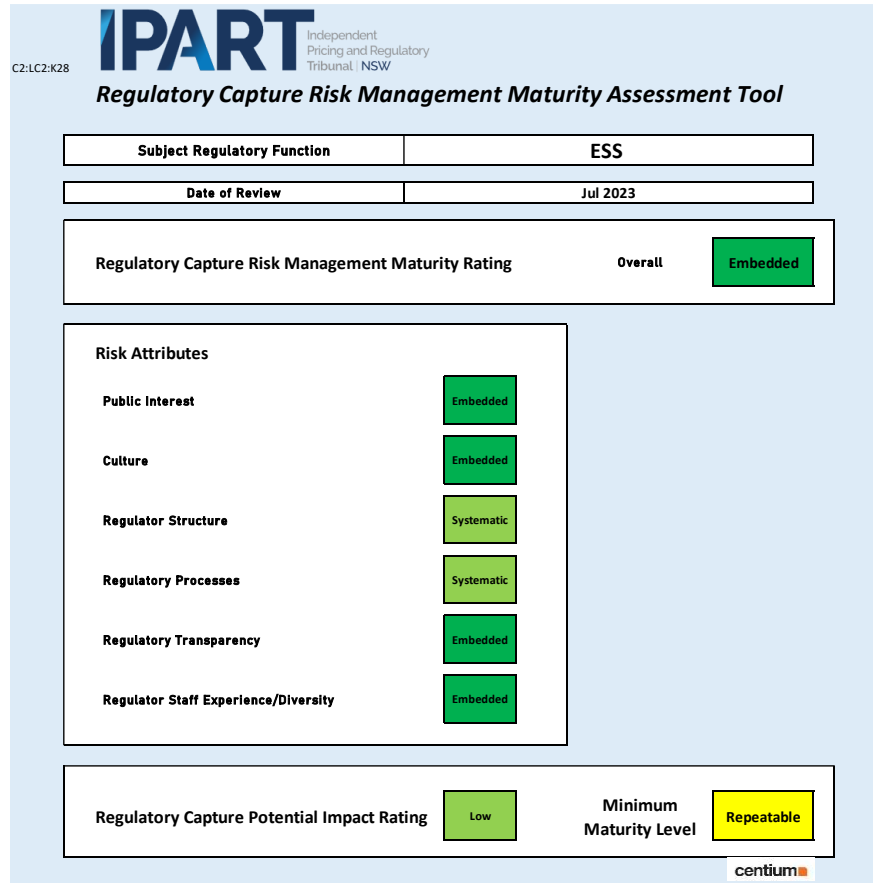
Measures

- Minimum recommended maturity level = **Systematic**
- Potential Impact rating = **Medium**
 - Note: the **Medium** impact rating is based on high public interest impacts (safe reliable energy) and reasonable public acceptance of regulated actions

Key results

- Overall Risk Maturity Rating Regulatory Capture = **Embedded**
 - 6/6 Risk Attributes rated as **Embedded**

ENERGY SAVINGS SCHEME



Scope of assessment

- Energy Savings Scheme Licensing & Accreditation
- Peak Demand Reduction Scheme Licensing & Accreditation

Measures

- Minimum recommended maturity level = **Repeatable**
- Potential Impact rating = **Low**
 - Note: the **Low** impact rating is based on the comparatively lower direct impact of regulatory failure

Key results

- Overall Risk Maturity Rating Regulatory Capture = **Embedded**
 - 4/6 Risk Attributes rated as **Embedded**
 - 2/6 Risk Attributes rated as **Systematic**

Regulator Structure rating of systematic mainly due to resourcing of non-BAU activity regarding licensing

Regulatory Processes of systematic mainly due to public remoteness from regulatory activity

Acknowledgement

Centium acknowledges with thanks the involvement and cooperation of all the IPART personnel who took part in this project.

Report clearance

This report and the contents herein were discussed with the Project Sponsor and the key stakeholders.





Penny Corkill
Director Risk & Assurance
Centium












appendices

Appendix 1 – Risk Maturity Criteria

Centium developed a risk maturity model, set out below, which was expanded on from the basic criteria initially proposed by IPART. This model was agreed with IPART management prior to the risk maturity assessment taking place.

RISK ATTRIBUTE	FOUNDATIONAL	REPEATABLE	SYSTEMATIC	EMBEDDED	ADVANCED
 PUBLIC INTEREST	<ul style="list-style-type: none"> There is no agreed model for determining the public interest. 	<ul style="list-style-type: none"> A model to determine the public interest has been agreed in relation to regulatory functions. 	<ul style="list-style-type: none"> An agreed model to determine the public interest is in place and is used to guide regulatory processes. 	<ul style="list-style-type: none"> An agreed model to determine the public interest is in use to guide regulatory processes, which is consciously reinforced and occasionally reviewed. 	<ul style="list-style-type: none"> A universally agreed model to determine the public interest is in use to guide regulatory processes, which is strongly reinforced and regularly reviewed.
 CULTURE	<ul style="list-style-type: none"> Governing body / top management do not seek to set a strong tone regarding serving the public interest. Policies and procedures may not be in place to encourage serving the public interest. Compliance with public interest policies and procedures may not be enforced. Assurance processes may be lacking. 	<ul style="list-style-type: none"> Governing body / top management make pronouncements supportive of serving the public interest. Policies and procedures are largely in place regarding public interest matters. Staff may not be fully aware of public interest policies and procedures. Enforcement and oversight of public interest policies and procedures may be inconsistent. 	<ul style="list-style-type: none"> Governing body / top management make clear and strong pronouncements supportive of serving the public interest. A comprehensive suite of public interest policies and procedures is in place. Staff are trained in public interest policies and procedures, compliance with which is enforced. Assurance processes are planned and structured. 	<ul style="list-style-type: none"> Governing body / top management support serving the public interest in word and deed. Public interest policies and procedures align with best practice and are periodically reviewed. Staff training in public interest matters is mandatory and periodically reinforced. Compliance with public interest policy and procedures is stringently enforced and subject to routine audit/assurance. 	<ul style="list-style-type: none"> Governing body / top management are exemplars of serving the public interest. Public interest policies and procedures are in practice and are constantly revised to remain so. There is mandatory ongoing staff public interest training. Management and staff perpetuate full compliance with public interest policy and procedure. Independent assurance regarding public interest protection is expected and commonplace.

					
RISK ATTRIBUTE	FOUNDATIONAL	REPEATABLE	SYSTEMATIC	EMBEDDED	ADVANCED
 <p>REGULATOR STRUCTURE</p>	<ul style="list-style-type: none"> The regulator has not fully established what structures and resources are needed to provide effective regulation. 	<ul style="list-style-type: none"> The regulator has established a regulatory structure and basic resourcing model with basic governance measures. 	<ul style="list-style-type: none"> The regulator has an effective regulatory structure and standard resourcing model with sound governance measures in place. 	<ul style="list-style-type: none"> The regulator has a regulatory structure that is proven to be effective, with confirmed adequacy of resourcing and mature governance measures. 	<ul style="list-style-type: none"> The regulator has a world-class regulatory structure with demand-responsive resourcing and superior overall governance.
 <p>REGULATORY PROCESSES</p>	<ul style="list-style-type: none"> Regulatory processes are overly complex, with limited capability to receive public input. Decision-making bodies may lack balance or governance. 	<ul style="list-style-type: none"> Regulatory processes are somewhat complex, with limited capability to receive public input. Decision-making bodies may lack balance or good governance. 	<ul style="list-style-type: none"> Regulatory processes are reasonably simple, with open capability to receive public input. Decision-making bodies have some balance and sound governance. 	<ul style="list-style-type: none"> Regulatory processes are simple, and public input is sought and received. Decision-making bodies are well-balanced with strong governance. 	<ul style="list-style-type: none"> Regulatory processes are as simple as possible. Public input is aggressively sought. Decision-making bodies are impeccably balanced with leading governance.
 <p>REGULATOR TRANSPARENCY</p>	<ul style="list-style-type: none"> The public interest is unclear to stakeholders. The public is unable to access and/or understand the regulatory process. The outcomes of regulatory processes are not made available to the public. Regulatory decisions are not clearly justified. 	<ul style="list-style-type: none"> Stakeholders do not have a good understanding of the public interest or the regulatory process. Regulatory outcomes are not easily accessible to the public. Justification for regulatory decisions may not be fully explained. 	<ul style="list-style-type: none"> Stakeholders have a sound understanding of the public interest and the regulatory process. Regulatory outcomes are available to the public. Justification for regulatory decisions is available. 	<ul style="list-style-type: none"> Stakeholders have a good understanding of the public interest and the regulatory process. Regulatory outcomes are freely available to the public. Detailed justification for regulatory decisions is available. 	<ul style="list-style-type: none"> Stakeholders have an excellent understanding of the public interest and the regulatory process. Regulatory outcomes are promoted and freely available to the public. Clear and detailed justification for regulatory decisions is promoted and freely available.
 <p>REGULATOR STAFF EXPERIENCE & DIVERSITY</p>	<ul style="list-style-type: none"> Regulator staff do not come from diverse backgrounds. There is strong reliance on individual staff or entities. 	<ul style="list-style-type: none"> There is some diversity in staff backgrounds. There is reliance on individual staff or entities to produce regulatory outcomes. 	<ul style="list-style-type: none"> The diversity of staff backgrounds is considered when putting together teams. Key person dependencies are identified and some action taken to limit them. 	<ul style="list-style-type: none"> Diversity in staff backgrounds is actively sought. Opportunities for key person dependencies are actively managed. 	<ul style="list-style-type: none"> Diversity in staff backgrounds is mandated. Key person dependencies are proscribed.

Appendix 2 – Disclaimers

This report is prepared on the basis of the following:

- **Management Responsibility:** Management is responsible for establishing and maintaining an effective system of internal control over its operations and financial reporting. This includes without limitation, systems designed to assure the achievement of its control objectives and compliance with applicable laws and regulations.
- **Limitations:** The matters raised in this report are only those that came to our attention during the course of our review and are not necessarily a comprehensive statement of all the weaknesses that exist or all improvements that might be made. Our procedures were not designed to detect all weaknesses in control procedures as they were not performed continuously throughout the period and the tests performed are on a sample basis.
- **Fraud:** There is an unavoidable risk in any assurance project that fraud or irregularity may not be detected due to the limitations noted above. Our report therefore should not be relied upon to disclose fraudulent activities.
- **Recommendations:** Centium is not responsible for whether, or the manner in which, any recommendations made in this report are implemented. Your entity should assess our recommendations for their full commercial and operational impact before implementing them.
- **Confidentiality:** This report is confidential, has been prepared solely for the use by your entity and ownership of the report and any attachments lies with your entity.
- **Third Party Responsibility:** This report should not be quoted in whole or in part without our written consent. We disclaim any assumption of responsibility for any reliance on this report to any person other than management of the entity or for any purpose other than which it was prepared.
- **Information Requests – Costs:** Costs of information requests under any “*freedom of information*” legislation such as the NSW Government Information (Public Access) Act, the Commonwealth Freedom of Information Act or subpoenas arising from actions taken by individuals or groups as a result of this report will be passed on to you.



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