

“Criteria for good oversight”

Consultation Forum of Regulatory Bodies (MTB)

ACM, AFM, CBP, DNB, KSA and NZa

February 11, 2014



INTRODUCTION

This memo describes the joint vision of the Consultation Forum of Regulatory Bodies (MTB, in Dutch: *Markttoezichthoudersberaad*)¹ concerning the criteria for good oversight.² By publishing this joint vision, a framework is offered for carrying out market oversight in an independent and targeted manner, as well as for critically evaluating oversight quality. In addition, the MTB believes it is important to have consensus between the ministries and the regulators regarding what constitutes 'good oversight'. While the MTB is aware that the question of what constitutes 'good oversight' is a multifaceted one, it hopes that this memo will provide some guidance.

The underlying principle in this memo is the idea that a *practical* translation of the criteria for good oversight contributes to their usability. With this in mind, criteria have been fleshed out into three levels of abstraction (for the two 'highest' levels, see below; Annex 1 summarises the criteria in detail). The criteria at the 'lowest', most specific level offer the most direct tools for application in practice. Although the typical activities, the nature of the oversight activities, and the specific context in which that oversight is carried out will differ from one regulator to another, the MTB believes the criteria set out in this memo apply to all of them.

This memo builds on several earlier initiatives³ that were developed in order to create an overview of the elements of good oversight. Rather than setting up a new study, it was decided to build on earlier findings. The elements that define good oversight that have been adopted in this memo therefore stem from, or paraphrase, those earlier studies.

Summary: A good regulator is⁴ ...

... effective:

mission-driven
impact-focused
accountable
change-minded

... efficient:

empowering
collaborative
efficiently organised

... professional:

independent
transparent
made up of professionals

¹ The Consultation Forum of Regulatory Bodies (*Markttoezichthoudersberaad*) is a collaboration between the Netherlands Authority for Consumers & Markets (ACM), the Netherlands Authority for the Financial Markets (AFM), the Dutch Data Protection Authority (CBP), the Dutch central bank DNB, the Netherlands Gaming Authority (KSA) and the Dutch Healthcare Authority (NZa). The CBP oversees compliance with basic rights by public authorities and therefore occupies a somewhat special position in this regard.

² The MTB wishes to thank all parties that contributed to the creation of this document by responding to the consultation, which took place in the spring of 2013.

³ Particular consideration was given to the following documents on oversight (i) Kaderstellende Visie op Toezicht – 2005, 'Minder last, meer effect', Tweede Kamer 2005-2006, 27 831 no. 15, Ministry of the Interior and Kingdom Relations; (ii) "Effectief Markttoezicht" : contribution by the MTB for reform of the Kaderstellende Visie op Toezicht (Framework Paper on Oversight), (2011), (iii) Viñals, Fiechter, The Making of Good Oversight: Learning to Say "No", IMF paper, (May 18, 2010), SPN/10/08 and (iv) previous evaluations by regulators.

⁴ Annex 1 presents a complete list of the criteria for good oversight described in this document.

CRITERIA FOR GOOD OVERSIGHT

Good oversight is effective, efficient and professional. Although there are several classifications of the elements of good oversight, the concepts of effectiveness, efficiency and professionalism are a common thread running through them all. Effectiveness here refers to the 'substantive results', while efficiency is a measure of how efficiently tools and resources are used in order to achieve those results. Professionalism, finally, is a concept that defines the way in which those resources are used and how those results are achieved.

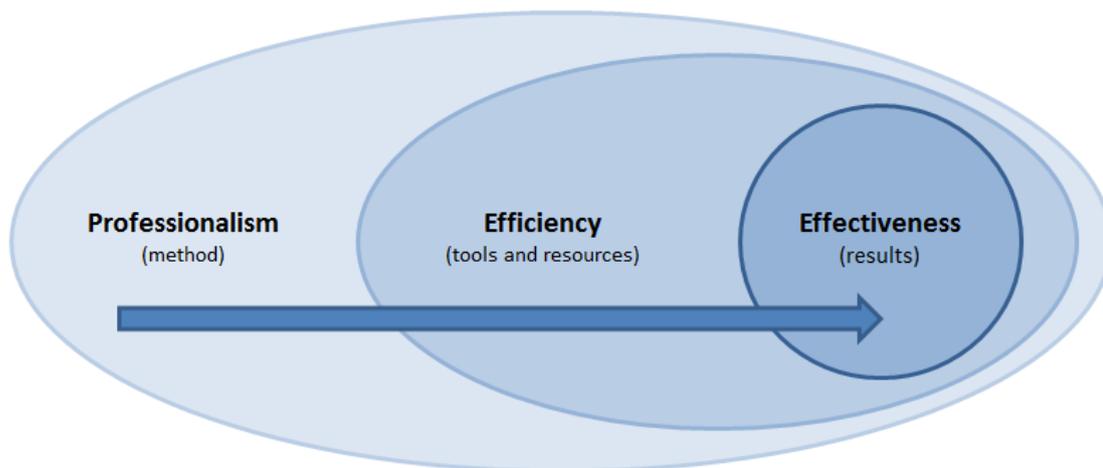


Figure 1 – Effectiveness, efficiency and professionalism as core values of good oversight. Professionalism and efficiency are conditions for achieving the primary goal: effectiveness.

Effectiveness is the core value of these three concepts. Efficiency and professionalism are necessary conditions for fulfilling that core value to the required standard of quality. These three aspects of good oversight are discussed in more detail below.⁵

A. The effectiveness of oversight

An effective regulator is mission-driven, impact-focused, accountable and change-minded (see also Figure 2).

A.1 *Mission-driven oversight*

Mission-driven oversight focuses on a higher objective, not just on compliance with legislation and regulations. This means that oversight involves more than just the strict exercise of powers when

⁵ Despite the relationship between the core values effectiveness, efficiency and professionalism, the factors that contribute to them are cited under just one of the core values. Although they often also relate to one (or both) of the other aspects of good oversight, for the sake of clarity they are only cited under the core values to which they relate most closely.

implementing and enforcing certain laws and rules.⁶ Aspects such as advocacy (vis-à-vis the national and European authorities) and guidance and information vis-à-vis the regulated parties and consumers) are crucial in this regard.⁷ Arguing for a sufficiently broad mandate, appropriate powers and suitable legislation and regulations,⁸ or putting forward best practices and consumer information, are examples of this.

Market oversight focuses on both the macro and micro-level. The envisaged effects of oversight lie at the heart of mission-driven oversight. This not only means the envisaged effects in an individual case, but also the impact on the sector as a whole.⁹

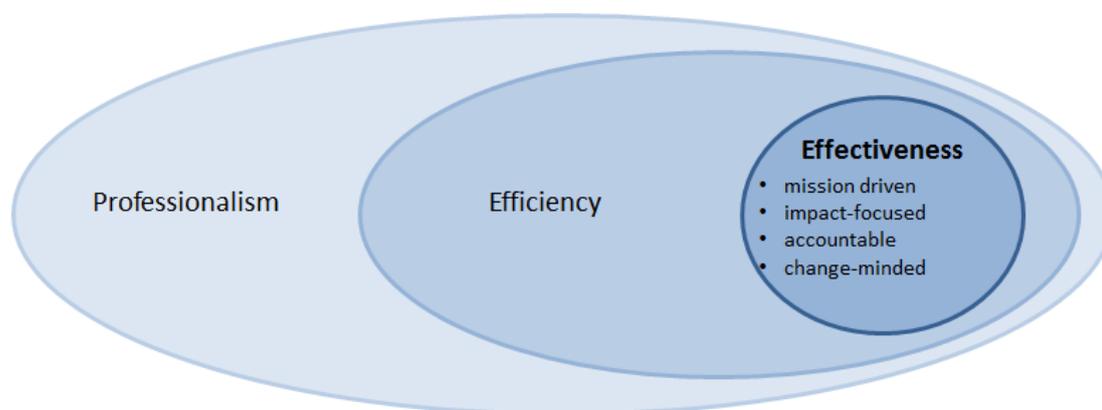


Figure 2 – Core values of an effective regulator.

Increasingly, a large part of the regulatory capacity is devoted to oversight activities that go beyond the individual level and relate to the broader system. This 'systemic oversight' is important because more broadly-based risk assessments and theme-based studies can generate indications that are important for oversight at the individual level. Conversely, developments at the individual level can have an impact on the broader system.

<i>A.1</i>	<i>Criterion - Mission-driven oversight</i>
	The regulator
A.1.1	... bases its oversight on a specific mission.
A.1.2	... regulates both individual institutions and the sector as a whole.
A.1.3	... acts as a policy advisor and advocate for its mission vis-à-vis national and European authorities.
A.1.4	... acts as an informant to the sector and consumers, and provides direction.

⁶ This does not of course alter the fact that mission-driven oversight is carried out within the prevailing legislative framework.

⁷ "Effectief Markttoezicht" contribution by the MTB for the reform of *Kaderstellende Visie op Toezicht* (2011).

⁸ The institutional embedding of oversight is also part of this, i.e. the effectiveness of oversight is partly determined by the institutional framework chosen by the government. A good regulator calls on the government to provide an institutional framework that fosters the achievement of its mission.

⁹ "Effectief Markttoezicht" contribution by the MTB for the reform of *Kaderstellende Visie op Toezicht*.



A.2 *Impact-focused oversight*

Market regulators are committed to the early identification and prevention or resolution of the most pressing problems in the market and/or society. Selectivity is a primary condition for impact-focused oversight. In this regard, risk-based oversight is a key concept in modern oversight. Regulatory capacity is scarce, and, therefore, choices have to be made: the aim here is to reduce the number of investigations, and to increase the impact of each individual investigation. It is good practice to allocate *ex ante* regulatory resources based on risk identification¹⁰. The guiding principle is the protection of public interests.¹¹

In addition to selectivity, decisiveness is a second condition for impact-focused oversight. While selectivity is particularly important in the preparation of oversight (individual and systemic), decisiveness is a characteristic of oversight in action. After identifying and assessing risks, it may be necessary to take action. In that case, the following statements are relevant¹²: (i) good oversight is intrusive; the regulated parties and the sector must feel the presence of the regulator; (ii) good oversight is sceptical and proactive; regulators must adopt a permanently critical attitude, especially in times when things are going well (for the sector); (iii) good oversight is conclusive; regulators must enforce effective risk-mitigating measures. A regulator must be prepared to take risks when necessary.

Influencing the behaviour of stakeholders is an important part of decisive oversight. To achieve this, the regulator can focus on both (i) encouraging norm-compliant behaviour by regulated parties, and (ii) promoting the role of consumers as a countervailing power. Explaining the background of a norm to the sector, explicitly describing what constitutes desired conduct (good practices, naming) and formulating the message (framing) are examples of ways of influencing behaviour.

A.2	<i>Criterion – Impact-focused oversight</i>
	The regulator
A.2.1	... focuses on the early identification and prevention or resolution of the most pressing problems in the market.
A.2.2	... is selective and bases its activities on a risk-based <i>ex ante</i> prioritisation.
A.2.3	... is decisive (conclusive, intrusive, sceptical and proactive) in its actions.
A.2.4	... influences the behaviour of stakeholders.

¹⁰ Where risk is the product of the impact and probability of a failure.

¹¹ WRR report *‘Toezien op publieke belangen’*, (9 September 2013).

¹² Viñals, Fiechter, *The Making of Good Oversight: Learning to Say “No”*, IMF paper, (May 18, 2010), SPN/10/08.

A.3 *Accountable oversight*

A regulator's legitimacy is based on being accountable to society.¹³ A corollary to the increased attention for the impact of oversight is a growing emphasis on measuring that impact. The central argument here is that impact evaluation is essential in order (i) to ensure the legitimacy of oversight (public accountability) and (ii) to improve oversight (learning from evaluation).¹⁴ The underlying principle is that the ‘authority of a regulator today is no longer based on adhering to routines, but on rendering account, publicly and academically, for the regulatory methods used and goals achieved.’¹⁵ While the MTB is aware of the limitations of measuring oversight¹⁶, the regulators in question feel responsible for ensuring adequate communication about their policies and results to both government and society, and for the resultant public support for their oversight (‘licence to operate from stakeholders’).¹⁷ Creating a realistic pattern of expectations among politicians and the public, among other things, by communicating both what you do and what you do not do, is part of this.

A.3	<i>Criterion - Accountable oversight</i>
	The regulator
A.3.1	... measures the impact of the oversight it carries out.
A.3.2	... learns from impact evaluations and improves its oversight on the basis of them.
A.3.3	... communicates the impact of its oversight to society.
A.3.4	... develops sufficient public support for its oversight.

A.4 *Accountable oversight*

Regulators must continually scour the horizon for new developments and risks, both for institutions and for the system as a whole. The ambition of good oversight is not to miss any developments.¹⁸ This also means that regulators must continually internalise new knowledge.

In addition, what is considered good oversight is subject to change over time, due both to changing social views and to developments within the sector itself.¹⁹ Regulators must be able to take into account both types of development and respond to them appropriately.

A.4	<i>Criterion – Accountable oversight</i>
-----	--

¹³ ‘Society’ here is taken to mean politicians, the regulated parties, and the broader public.

¹⁴ P. Welp, “Effectiviteit van toezicht: tijd voor responsive evaluation”, TvT 2012.

¹⁵ “Effectief Markttoezicht” contribution by the MTB to the reform of *Kaderstellende Visie op Toezicht*.

¹⁶ See e.g. P.L.C. Hilbers, D.R. Rijsbergen, K. Raaijmakers & F. de Vries, “Effectmeting in het toezicht op de financiële sector”, TvT 2012.

¹⁷ “Effectief Markttoezicht” contribution by the MTB to the reform of *Kaderstellende Visie op Toezicht*.

¹⁸ Viñals, Fiechter, The Making of Good Oversight: Learning to Say “No”, IMF paper, (May 18, 2010), SPN/10/08. The increasing globalisation and EU integration underline the importance of this ambition.

¹⁹ DNB, “Van analyse naar actie” - *Plan van aanpak cultuurverandering toezicht DNB*, (2010), p. 6.

The regulator	
A.4.1	... constantly explores the existence of new developments and risks in its sector.
A.4.2	... develops sufficient knowledge and skills to remain continually up to date.
A.4.3	... regularly assesses its own vision, mission and methods based on developments in the sector and stakeholder expectations.

B. The efficiency of oversight

An efficient regulator is empowering, collaborative and efficiently organised (see also Figure 3).

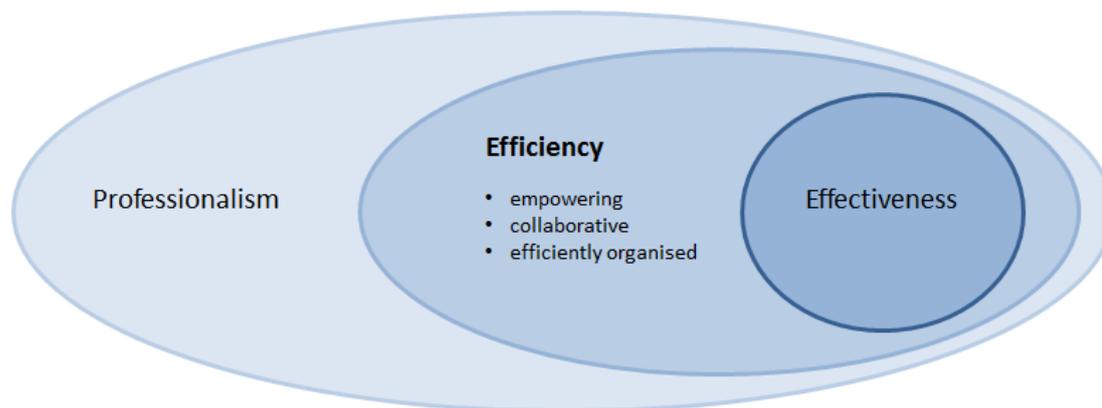


Figure 3 – Core values of an efficient regulator.

B.1 Empowering oversight

‘The government cannot and should not seek in all cases to direct the process of social organisation. Market participants and citizens also have a responsibility in protecting public interests.’ This is stated by the Netherlands Scientific Council for Government Policy (WRR) in its report ‘Public interests in a market society’ (*Publieke zaken in de marktsamenleving*). The prominent role of a market participant in relation to the balanced functioning of the market in which it operates is based on (i) the information advantage it has over the regulator; (ii) its duty to comply independently with open norms; and (iii) the control and power of decision it alone has over its actions. This means that the market participant, sometimes even more than the regulator, is the appropriate organisation to take on certain responsibilities. One of the most important challenges for the regulator is therefore to challenge regulated parties directly about their conduct and responsibilities. The actions of market participants largely determine the direction and effectiveness of the market.

Developing stakeholder empowerment and promoting their learning ability and social resilience are values that contribute efficiently to the balanced operation of these markets. The principle here is that responsibility for their actions and results lies primarily with the regulated parties themselves. The regulator has the power to both inform and offer guidance to regulated parties, as well as to encourage their self-learning capacity. Good contact between the regulator and regulated party, is



being careful to avoid the trap of ‘regulatory capture’, contributes to an awareness of mutual responsibilities and the development of the associated competences. This strengthens the foundations of high-trust oversight. Citizens, too (as individuals or as organised groups) can make a key contribution to the balanced operation of markets. Increasing the empowerment of citizens and promoting their learning capacity and social resilience can therefore be a valuable task for regulators.

B.1	Criterion – Empowering oversight
	The regulator
B.1.1	... promotes a sense of responsibility and the capacity of the sector to contribute to the balanced operation of the market.
B.1.2	... contributes to the empowerment and development of the learning capacity of stakeholders such as citizens and market players.

B.2 Collaborative oversight

Collaboration is an important means of increasing the effectiveness of oversight as well as reducing the burden for citizens, businesses and autonomous organisations. Collaboration between regulators can achieve several goals, with benefits for both regulated parties and regulators. Means of achieving this include the exchange of information, the formulation of vision and policy, exercising oversight jointly or on each other's behalf, and identifying and reducing conflicting or overlapping regulations.²⁰ The trend whereby regulated parties respond to increasing globalisation and EU integration by progressively organising themselves transnationally or offering products across borders, requires coordination with other regulators, including at an international level.

As well as collaboration between regulators, collaboration between regulators and the government as policymaker also demands special attention. Although the policymaker is ultimately responsible for drafting policy, the regulator also plays an essential role in this process, based on its own role and responsibility: a good regulator brings to bear knowledge about typical national and international developments and risks in the sector, identifies obstacles and weaknesses in legislation and regulations that impede it in its oversight, and reports on what is and is not possible, and on the social context. The objective is to create a framework within which the regulator is able to achieve its mission.²¹

B.2	Criterion – Collaborative oversight
	The regulator
B.2.1	... works in different national and international fields together with other regulators.
B.2.2	... is a knowledge partner and advisor to the government as a policymaker.

²⁰ *De kaderstellende visie op toezicht – 2005, 'Minder last, meer effect'*, Ministry of the Interior and Kingdom Relations.

²¹ See also criterion A.1.3.

B.3 Efficiently-organised oversight

The costs of oversight are lower if the internal organisation and operations are configured efficiently. In particular, this means developing a sharply formulated, practical strategy (ambitions and initiatives), control (organisational structure, management tools and governance models) and organisational culture (conduct and collective patterns of action) as well as a clear alignment between these concepts.²² As a corollary to this, regulators have a duty to strive continually to achieve the most flexible and effective possible configuration and deployment of the available scarce capacity.

B.3	<i>Criterion – Efficiently-organised oversight</i>
	The regulator
B.3.1	... has worked up a detailed strategy that is in line with its mission and duties.
B.3.2	... has an efficiently configured organisation and governance model that matches its strategy.
B.3.3	... has an organisational culture that contributes to the achievement of its strategy.

C. The professionalism of oversight

A professional regulator is independent, transparent and made up of professionals (see also Figure 4).

C.1 Independent oversight²³

It is essential for the successful operation of markets that the government contributes to the effective organisation of those markets. The task of market oversight here is to ensure a balanced assessment of private and public interests. To be able to carry out this task, oversight needs to stand apart from both the political 'issues of the day' and sectoral interests. This means among other things that the regulator is willing to act against generally-accepted views and/or vested interests.

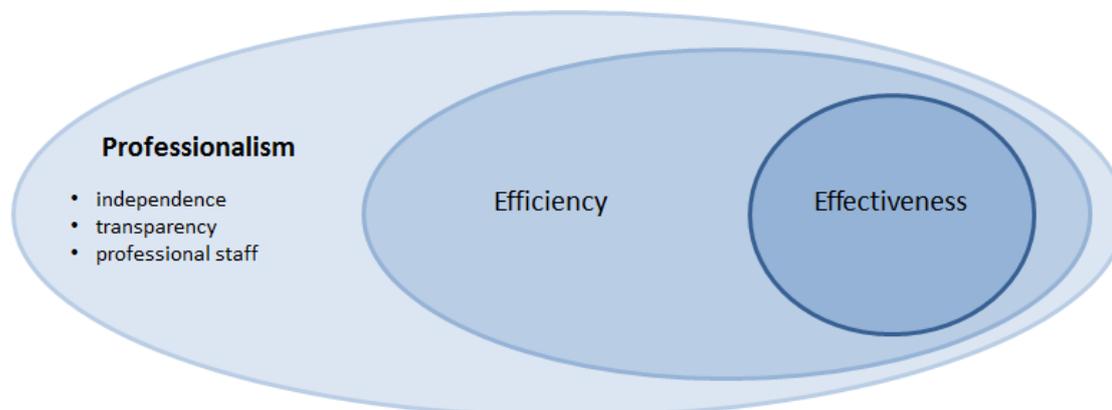


Figure 4 – Core values of a professional regulator.

²² A free interpretation of D.J.B. van der Leest and F.R. Roozen, "Strategy Realization: the next level" (2012).

²³ Transparency of operation and accountability is of particular importance from a democratic perspective for independent regulators. Consequently, the criteria of independence, transparency and accountability are closely interrelated.

As far as the sector is concerned, the regulator must avoid any semblance of partiality towards regulated parties. This can appear to be at odds with other criteria for good oversight. To guarantee responsive (i.e. a combination of selective and decisive) oversight, it can be desirable to display impartial empathy or to carry out oversight based on a certain bond of trust. The use of 'open norms' and the need to operationalise these in consultation with the field can also lead to intensive contact with the sector. However, this does not prevent the regulator from fulfilling its duty to avoid non-impartial empathy and 'regulatory capture'.

The regulator must be able to exercise its powers independently of politicians (policymakers).²⁴

These powers relate to things such as setting priorities, choice of examination methods, publishing opinions and intervening in the sector. Now that 'policy' and 'oversight' are increasingly having to work together because of their shared responsibility for the effective control of social risks, measures to safeguard the independence of oversight from politics are becoming increasingly important. Collaboration is not in conflict with a credible independence for oversight, but does require that those concerned stick firmly to their roles and that there is transparency.

The regulator must display a certain degree of daring in exercising independent oversight. In addition to conclusiveness and intrusiveness, as referred to under the heading 'decisiveness' (see criterion A.2.3), this requires qualities such as perseverance and courage.

<i>C.1</i>	<i>Criterion – Independent oversight</i>
	The regulator
C.1.1	... avoids any (semblance of) partiality towards regulated parties and the sector.
C.1.2	... operates independently of policymakers and other (political) stakeholders.

C.2 Transparent oversight

The regulator must be transparent both for the public and for regulated parties. With regard to citizens, the regulator must make clear what oversight means for society. As a corollary to this, politicians must be able to decide on the basis of facts whether the costs of oversight are justified by the public benefits. In addition, the regulator must be able at all times to account for its actions to the regulated parties.

Transparency of oversight relates both to the process of oversight itself and to the results of that oversight. It is important for the process that the regulator has acted consistently, with due care and

²⁴ This independence is of course constrained by the prevailing legal frameworks.

lawfully in performing its tasks. The regulator's duty of transparency also extends to retrospective transparency. To foster predictability, every regulator also publishes information about its regulatory process in advance. Examples include publication of the procedures for ensuring a fair hearing (legal certainty, lawfulness) and of procedures used in the selection of regulated parties to be visited (legal equality). With regard to transparency about the results of oversight, where possible the regulator publishes its formal opinions on regulated parties. Publishing opinions about individual regulated parties can be desirable and is, in some cases, a legal requirement, but must be accompanied by a framing of measures that is not unnecessarily harmed.

C.2	<i>Criterion – Transparent oversight</i>
	The regulator
C.2.1	... is transparent about its oversight to the public, politicians and supervised entities.
C.2.2	... demonstrates that it performs its duties consistently, with due care and lawfully.
C.2.3	... provided its task as a regulator does not prevent this, publishes its opinions about regulated parties .

C.3 The regulator is made up of professionals

A good regulator feels responsible for the professionalism of its staff and develops initiatives to maintain and improve that professionalism. In practice, the above criteria often relate to the professionalism of the regulator as an organisation. Having professional staff is a necessary condition for this. The regulator therefore needs to stimulate the necessary professionalism and to encourage its staff in this regard, for instance by offering facilities for the maintenance and development of both knowledge and skills.

A good regulator has sufficient knowledge both of the sector and of oversight-specific skills. An example is recognising that 'sound judgement' is one of the most important core competencies. The complexity and dynamic of oversight means that an ability to assess different situations in different circumstances is one of the most distinctive characteristics of a good regulator.

Finally, senior management of a good regulator leads the way in the continuous commitment to further improving oversight. It sets an example in relation to the above criteria for good oversight and inspires its staff to contribute to an organisation that performs its duties as effectively, efficiently and professionally as possible. The integrity of the regulator is an aspect that warrants particular attention here.

C.3	<i>Criterion – The regulator is made up of professionals</i>
	The regulator
C.3.1	... demonstrably encourages its staff to develop further as professionals.

C.3.2	... is expert: staff have sufficient knowledge both of the sector and of oversight-specific skills.
C.3.3	... acts with integrity and is led by a senior management that sets an example.



ANNEX 1 - LIST OF CRITERIA FOR GOOD OVERSIGHT

A good regulator is...		
A	... effective	
	1	... mission-driven
	1	... and bases its oversight on a specific mission.
	2	... and supervises both individual institutions and the sector as a whole.
	3	... and acts as a policy advisor and advocate for its mission vis-à-vis national and European authorities.
	4	... and acts as an informant to the sector and the consumer and provides direction.
	2	... impact-focused
	1	... and focuses on the early identification and prevention or resolution of the most pressing problems in the market.
	2	... and is selective and bases its activities on a risk-based ex ante prioritisation.
	3	... and is decisive (conclusive, intrusive, sceptical and proactive) in its actions.
	4	... and influences the behaviour of stakeholders.
	3	... accountable
	1	... and measures the impact of the oversight it carries out.
	2	... and learns from impact evaluations and improves its oversight on the basis of them.
	3	... and communicates the impact of its oversight to society.
	4	... and develops sufficient public support for its oversight.
	4	...change-minded
	1	... and constantly explores the existence of new developments and risks in its sector.
	2	... and develops sufficient knowledge and skills to remain continually up to date.
	3	... and regularly assesses its own vision, mission and methods based on developments in the sector and stakeholder expectations.
B	... efficient	
	1	... empowering
	1	... and promotes a sense of responsibility and the capacity of the sector to contribute to the balanced operation of the market.
	2	... and contributes to the empowerment and development of the learning capacity of stakeholders such as citizens and market players.
	2	...collaborative
	1	... and works in different national and international fields together with other regulators.
	2	... and is a knowledge partner and advisor to the government as policymaker.
	3	... efficiently organised
	1	... and has worked up a detailed strategy that is in line with its mission and brief.
	2	... and has an efficiently configured organisation and governance model that matches its strategy.
	3	... and has an organisational culture that contributed to the achievement of its strategy.
C	...professional	
	1	... independent
	1	... and avoids any (semblance of) partiality towards regulated parties and the sector.
	2	... and operates independently of policymakers and other (political) stakeholders.
	2	... transparent
	1	... and is transparent about its oversight to the public, politicians and regulated parties.
	2	... and demonstrates that it performs its duties consistently, with due care and lawfully.
	3	... and provided its task as a regulator does not prevent this, publishes its opinions about regulated parties.
	3	... made up of professionals
	1	... and demonstrably encourages its staff to develop further as professionals.
	2	... and is expert: staff have sufficient knowledge both of the sector and of oversight-specific skills.
	3	... and acts with integrity and is led by a senior management that sets an example.