Economist Intelligence Unit

The Economist

Review of the Regulatory Environment in Ireland

A report from the Economist Intelligence Unit

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Symbols for tables

"n/a" means n/a; "–" means not applicable

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1. Executive summary

Introduction

In May 2008 the Economist Intelligence Unit was contracted by the Department of the Taoiseach to review the economic regulatory environment in Ireland. The review has been overseen by an inter-departmental group chaired by the Department and including representatives of the Departments of Finance, Communications, Energy and Natural Resources, Enterprise, Trade and Employment, Transport and the Office of the Attorney General. The work was completed in March 2009.

The review has examined the current regulatory framework in Ireland and compared it with international practice in five "case study" sectors—financial services, energy, telecommunications, health and safety and transport (civil aviation and taxis). It has also prepared recommendations on how regulatory structures in Ireland might be improved. Five questions were examined in the course of the review:

- appropriateness of current structures;
- sufficiency of their existing mandates;
- potential to merge functions;
- effectiveness and value for money; and
- potential to strengthen accountability.

The review was based on desk research, an interview programme in Ireland and international research in 11 countries.

Principles of economic regulation

The review has examined the principles underlying regulation and how these have evolved both in Ireland and overseas. Economic regulation is primarily concerned with regulating the commercial operations of firms in an industry where there is a risk of monopolistic powers being abused. Of the regulators in Ireland included in the review, the Commission for Aviation Regulation (CAR), the Commission for Energy Regulation (CER), and the Communications Regulator (ComReg) fit this definition. Regulation, though, is also conducted for other reasons, for example to protect consumer interests or in the case of the financial sector to ensure sound prudential supervision of financial markets.

Regulation was initially applied to public utilities that were seen as natural monopolies. In many European countries, including Ireland, this included extensive nationalisation of the utility industries on the assumption that public

ownership would protect public interests. Over time, weaknesses in this approach became apparent.

- It became clear that public ownership was no guarantee of domestic and business consumer interests.
- Imposed limits on profits, for example "break-even" obligations, could be avoided by different accounting treatments of the profits earned.
- Rate of return limits did not provide incentives for firms to reduce costs and maximise efficiency.
- There was scope for "regulatory capture", with regulators effectively dominated by firms because of information asymmetries between them.

From the early 1980s, a series of reforms was prompted partly by these weaknesses and also by increasingly rapid changes in technology and markets. In addition, a series of EU directives imposed obligations on member states in terms of regulatory approach and structures.

As a result, a different pattern of regulation emerged. Independent regulatory agencies increasingly became the norm, working within a statutory framework set by government, but free to make their own regulatory decisions. Price-cap methods of regulation also became more prevalent, although these too proved to have limitations. In financial services, market stability was seen as a "public good" requiring prudential supervision.

Ultimately, all forms of regulation have limitations. Inefficient regulation can distort market operation. It can stifle innovation and encourage the wrong choices of new technology. Regulators can find it difficult to keep pace with rapid technology and market changes, while regulated firms can use the system as a shield against effective competition. As regulators become better established, there is a tendency for "mission creep" with new roles being added by government or at the behest of the regulator on an *ad hoc* basis.

In short, regulation is not a substitute for competition. However, where it remains necessary, good practice requires:

- clarity of functions, both for the regulators and for other organisations in the regulatory system such as the competition authorities;
- organisational autonomy, both from government and the regulated industry;
- accountability, both formal and informal, to government and parliament; and
- transparency, in terms of open decision making and good communication.

It is also clear that no one model works best in all environments. Structures must fit with the economic and political contexts of each country, and thus a range of models should be expected internationally.

Economic regulation in Ireland

This review has examined how regulatory structures in Ireland have evolved, and how they currently perform in terms of a range of factors—appropriateness of structures, governance, adequacy of mandate, effectiveness and value for money, accountability and potential for restructuring. As an indication of scale, a report by the Department of the Taoiseach published in 2007[1] identified 213 regulatory bodies in Ireland, 205 of which were in the public sector and 114 were local authorities.

Evolution

The current regulatory framework took shape from the mid-1990s. Regulatory reform was one of the strands of the Strategic Management Initiative introduced into the Irish public sector at that time. Ireland participated in an OECD peer review of regulation in 2000-01, which also recommended improvements in the regulatory system. Meanwhile, EU measures to liberalise public utilities required that changes be made, especially in electricity, gas and telecommunications. Thus, the period from 2001-03 saw the establishment of ComReg (succeeding its predecessor, the Office of the Director of Telecommunications Regulation, which was established in 1996), the CER, the CAR and the Irish Financial Services Regulatory Authority (Financial Regulator). This process was, however, considered to have been undertaken in an *ad hoc* and inconsistent way, recognised in a 2004 government white paper, "Regulating Better".

Appropriateness of structures

The review has examined the original rationale for regulatory intervention in each sector, whether this is still valid and whether the existing structures can deliver the type of regulation required. This aspect of the work confirmed the continued need for regulation in certain sectors and sub-sectors, but also highlighted a number of issues requiring closer examination, for example overlaps between regulatory, consumer protection and competition roles.

Governance

The review considered the variations in the governance models currently used for the regulators in Ireland. The range includes an individual regulator (the CAR), a three-member commission (the CER and ComReg), an individual regulator with advisory panels (the Commission for Taxi Regulation—CTR), an individual regulator with a part-time board (the Health and Safety Authority—HSA) and also an individual regulator with advisory panels and a part-time board (the Financial Regulator). For the economic regulators, we believe that a multi-member commission has the advantage over a single regulator, avoiding personalisation of the process and bringing benefits in terms of handling complexity and work load, improving decision making and embedding institutional experience.

Adequacy of existing mandates

The key issue examined here was whether existing statutory mandates were sufficient to protect public policy objectives and consumer interests. This largely revolves around the extent of power given to ministers to issue directives to the regulators, and the safeguards built in to protect the regulators from

[1] Department of the Taoiseach, (2007), *Bodies in Ireland with Regulatory Powers as of February 2007.*

inappropriate use of such powers. In some cases, the relevant minister must consult before issuing such directives. Furthermore, the responsibility of ministers and government departments for public policy means that there will be occasions where instructions to regulators to take account of policy objectives are appropriate. There are, however, risks attached to the issue of directives, for example where government retains a shareholding in a regulated firm, or where the overruling of pricing decisions would affect regulatory credibility and/or breach EU regulations. So while the power to issue directives is an appropriate one to retain, it is important to ensure that public policy considerations are not invoked as a pretext for influencing or changing regulatory decisions. The report also examines threats to the adequacy of the existing mandates such as mission creep, regulatory capture, market changes and technological advances and the importance of a regulatory framework that can adapt to such challenges.

Effectiveness and cost comparisons

Specific examination of these factors is carried out in the individual sectoral chapters of the review. Overall, however, there are wide variations in the cost structures and trends of the regulators in Ireland. This was evident even when taking into account the differences in their functions and the impact of one-off costs in any one year, for example in handling major legal cases. Comparative measures such as salary costs as a proportion of total costs, consultancy costs as a proportion of total costs, costs per employee and payroll costs per employee all showed significant variations. Similarly, there is an inconsistent relationship between the general cost of goods and services as measured by the OECD comparative price index and the cost of regulation identified in this report. The report also makes the point that low-cost regulation is not the same as effective regulation.

Accountability

Effective regulatory accountability is important for a number of reasons, including proper accounting of public funds, impact on economic competitiveness, avoidance of abuse of power and avoidance of mission creep. The review examined a number of aspects of accountability and the key findings are summarised below.

- There are weaknesses in the effectiveness of the scrutiny of the regulators by the Oireachtas (the Irish parliament).
- It is unclear whether departments have sufficient expertise fully to supervise the regulators.
- The role of the Comptroller and Auditor General, the Public Accounts Committee and the Committee on Economic Regulatory Affairs provide for accountability in terms of public expenditure.
- The Financial Regulator's consultative panels play a useful role in promoting budgetary discipline.
- There is little accountability for incorrect regulatory decisions.
- In particular, the appeals process requires strengthening.

Potential for restructuring

Regulation can be implemented at various levels, from individual sectors through to more integrated cross-sectoral and functional models. As markets develop, the case for specific sector-level regulation can diminish. The review's consideration of the potential for restructuring is covered in the sectoral chapters and thereafter in the overall conclusions.

The international dimension

The review has compared the regulatory environment in Ireland with that in 11 other countries, selected to include a mix of characteristics: overall scale, legislative contexts, evidence of effective or innovative regulatory approaches and availability of information. Different combinations of sectors were examined in each country.

Four sets of criteria were used in the comparative analysis:

- cost-effectiveness;
- governance and accountability;
- impact on regulated business; and
- impact on consumer markets;

Information was collected primarily from the regulators themselves, but also from government departments and business representatives where possible. Comparisons were made between the mandates of the regulators in each country to ensure that the analysis was conducted on a like-for-like basis.

Financial services

The review was conducted in the midst of the ongoing global turbulence in financial markets, the consequences of which for future financial regulation remain unclear. The basic purpose of prudential regulation of the financial sector—to ensure that institutions maintain adequate levels of liquidity and remain solvent—will, however, remain constant. Financial regulation also covers consumer protection, although it is unusual for prudential supervision and consumer protection to be undertaken by the same body, as happens in Ireland through the Financial Regulator. The comparator countries for financial regulation were Australia, Denmark, Germany, Luxembourg, the Netherlands, Norway, Spain and the UK.

Effectiveness and cost comparisons

It became clear during the review that no particular regulatory structures across the comparator countries had proved more capable than others of protecting their financial systems against such a fundamental, global shock. The Spanish system perhaps emerged more positively than others, although the specific structure and behaviour of the financial sector there were also important factors.

The structure in Ireland compared favourably with others and, taking the longer view, the Irish model with close links between the Financial Regulator and the

Central Bank is one that may be more widely adopted internationally in the context of a likely trend towards tighter and more integrated regulation. The consumer protection role of the Financial Regulator was highly regarded by all stakeholders interviewed.

The Financial Regulator's operating costs are the largest of the Irish regulators examined, although its costs per employee were lower than the others apart from the HSA. The share of its annual income raised from industry levy was lower than in all of the other countries examined except Australia.

A number of metrics were used to benchmark the Financial Regulator's costs internationally. Ireland has the largest regulator income per head of population—Denmark's regulator has the same broad functions, but requires one-third of the Irish income. The Dutch and Norwegian regulators are not responsible for both prudential supervision and consumer protection, but still appear significantly less resource-intensive than the Financial Regulator. However, the financial sector in Ireland contributes a greater proportion to the economy. Looking at regulator income to sector income provides a more meaningful comparison and Ireland is about average on this measure. The Financial Regulator's income per employee is towards the higher end of the spectrum, but comparable with that of the UK and the Netherlands. In terms of staffing, the Financial Regulator is above average, but not to a concerning degree. Overall, the Financial Regulator appears to be broadly in line with the comparator countries in terms of the resources at its disposal.

Governance and accountability

A number of points emerged from the comparisons between these criteria.

- The clear remit and resources of the Financial Regulator's consumer and industry panels compared well with those of other sectors and countries. They provide both practical input and an additional demonstration of accountability.
- The Financial Regulator's position as part of the Central Bank was unique, but there was no evidence that this made it any less independent than the others—it may in fact become more consistent with international practice in the wake of the current financial crisis.
- Its relatively low proportion of industry funding is unusual internationally, and may prejudice the Financial Regulator's perceived independence from government. This should be balanced however against the importance of perceived independence from industry in terms of the regulator’s consumer protection role.
- No significant differences were apparent between the financial regulators regarding frequency of changes to their remit, ministerial reporting or directives or, for member states, the influence of EU directives.
- Effectiveness of accountability to parliament did vary, however, with the Irish approach comparing less favourably with others, in particular that of the UK.

- Considerable variation was also apparent in approaches to performance measurement and evaluation. These were generally found to be weak, with possible exceptions in the UK and the Netherlands.

Impact on business and consumers

Variations in the overall principles of regulation were apparent, however, from light touch, risk-based models through to more rules-based approaches. The former were more prevalent where regulation was part of a policy to attract foreign direct investment (FDI), such as in Luxembourg for example. This lighter touch approach is unlikely to be sustainable in the wake of the current financial turmoil. Recent events raise very serious concerns about the effectiveness of the Financial Regulator, revealing as they do serious failures in the oversight of regulated institutions along with serious breakdowns in internal communications. Some questions also arise in respect of the regulator's failure to use its admittedly limited powers to try and dampen a property market that was clearly overheating.

Consumer protection is not a core objective for most financial regulators, with the Financial Regulator being the clearest exception and the Danish and Norwegian regulators also adopting distinct consumer protection responsibilities. Feedback on the Financial Regulator's work in this area was positive and it certainly enhanced the regulator's reputation.

Energy

Energy sector regulation currently faces a number of challenges. Alongside economic regulation responsibilities, many regulators have been given additional roles related to security of supply, consumer protection, reduction in carbon dioxide (CO_2) emissions and encouragement of renewables. The comparator countries for this sector were Australia, Denmark, Germany, Great Britain (not the UK, since there is a separate regulator for Northern Ireland), the Netherlands, Norway, Portugal and Spain.

Effectiveness and cost comparisons

Irish energy prices have consistently been higher than in other EU member states. There are some factors beyond the CER's control, in particular the fuel mix of electricity-generating plants. Nevertheless, there remain inefficiencies in the Irish energy market that require continued attention from the regulator. In other respects, the CER has made good progress, with regulation no longer considered necessary for gas and electricity prices to medium and large industrial users. To date, however, there has been limited new entry in electricity generation, with Ireland comparing poorly with other countries such as Australia, Denmark and Norway. The establishment of the Single Electricity Market with Northern Ireland in 2007 should, in theory, increase competition, although further structural reforms will be required to deliver this in practice.

On costs of operation, the CER compares well with the other sectoral regulators in Ireland. It appears, however, to be more heavily resourced than most of the international comparators. Regulator income per head of national population is highest in the CER, as is regulator income per regulator employee. The CER has more employees in relation to employment in the regulated sector. While there

are differences in the mandates of the regulators across countries, these were not sufficient to explain the cost differentials.

Governance and accountability

There was considerable variation in the legal status of the energy regulators. In particular, the regulator was often integrated into a wider structure—part of the competition authority in the Netherlands and Australia; with transport in the Netherlands; and with post and telecommunications in Germany. There was no evidence that these links led to more effective regulation—the British regulator, Ofgem, is generally considered to follow good practice, but is specific only to energy, while Germany has made slower progress towards market liberalisation. In terms of changes to remit or lines of accountability, differences in structure did not appear to affect significantly regulatory operation or effectiveness. Performance evaluation procedures were generally activity- rather than outcome-based in the countries examined. Where there were close links to the competition authority, though (in Australia for example), performance was more explicitly linked to progress in achieving competitive markets.

Impact on business and consumers

The energy regulators used various combinations of price, revenue and rate-of-return limits to constrain the commercial operations of energy companies, and ultimately to protect consumer interests. Outcomes have been varied. The UK gas market has become reasonably competitive, electricity less so. Denmark, for example, has had more success in building a competitive electricity market.

Telecommunications

The telecoms sector has experienced rapid technological and market convergence. Competition has developed more rapidly than in other utility sectors, and the roll-back of regulation is more advanced. Regulators have had to adapt to these changing circumstances. For example, within the EU regulation is now only allowed where the national regulators can demonstrate that competition remains inadequate. The comparator countries examined in the review were Australia, Denmark, Germany, the Netherlands, Norway, the UK and New Zealand.

Effectiveness and cost comparisons

Irish telecoms prices generally compare well internationally. In both fixed and mobile telephony, Irish prices have been below the EU average in recent years. Competition within the Irish market has also increased recently and the market share of the incumbent fixed-line operator, Eircom, has fallen. Competition in the mobile market has increased markedly over the past decade, while mobile market penetration rates have risen to a level broadly in line with the rest of the EU. Broadband penetration has been slower, with Ireland lagging behind the EU average.

Given the rapid rate of market and technology change, these trends were always likely to happen and it is difficult to isolate the actual impact that the regulators have had. Broadly, however, it is the case that progress towards more fully competitive markets and pricing has been as rapid in Ireland as elsewhere.

Regulatory cost comparisons are made difficult by the wide range of responsibilities and structures evident internationally. As with energy, the telecoms regulators are sometimes linked with the competition authorities and/or with other sectoral regulators. The closest comparison with ComReg in terms of remit is Norway and to a lesser extent the UK and Australia. On most measures, ComReg requires more resources to operate than the comparators, for example on income per head of national population, income per regulator employee and regulator income to industry income.

Governance and accountability

Of the countries reviewed, only the UK and Ireland had an independent telecoms regulator with a sole focus on this sector. In the other countries, there were various permutations of links to the competition and other sectoral authorities. This in turn resulted in a mix of governance arrangements, but with no particular model demonstrably more effective in achieving regulatory objectives. Performance evaluation also showed a varied picture. As with energy, where the regulator was linked to the competition authority, there was a more obvious emphasis on performance related to competitive market outcomes. Otherwise, with the possible exception of Ofcom in the UK, there was a lack of systematic performance evaluation. Appeals procedures have been particularly contentious in Ireland with the establishment of a sectoral appeals panel in 2003 followed by its abolition in 2007 after dealing with just two substantive cases.

Impact on business and consumers

Across the comparator countries, there was substantial evidence of increasingly competitive markets emerging and lower prices for consumers. As indicated earlier, it is difficult to identify how much of this can be attributed to regulatory action—the industry was moving in these directions in any case.

Health and safety

Health and safety supervision does not come under the category of economic regulation, having no role in price or competition matters. Its reach across all sectors of the economy can, however, have an economic impact. The comparator countries in the review were Denmark, Germany, New Zealand, Norway and the UK.

Effectiveness and cost comparisons

With the exception of Germany, remits were broadly comparable, as were activity levels when adjusted for size of the national economy. The Irish authority compares well with the other international agencies in terms of costs of operation, with the exception of regulator income per regulator employee where it was the most expensive.

Governance and accountability

A common feature of the health and safety authorities examined was a tendency towards mission creep— additional roles and responsibilities being added over time. This was evident with the HSA in Ireland, but also with most of the other regulators reviewed.

Another consistent feature of health and safety authorities was the extent of reporting and consultation with other organisations such as employer bodies,

trade unions and research institutes. Performance evaluation was also generally well developed, with clear targets set for metrics such as the reduction of accidents and illness.

Impact on business and consumers

These factors were not covered in as much depth in the review as for other sectors, given the particular nature of health and safety regulation. Recent industry feedback on the work of the HSA in Ireland has been positive, with recognition of its role in reducing the costs of accidents and insurance. Employer feedback in Denmark and Norway was more critical of their national agencies, citing the costs of compliance, lack of commercial awareness and insufficient consultation.

Transport

Two transport sectors were covered in the review—civil aviation and taxis.

Civil Aviation

There is considerable variation in the mix of functions performed by civil aviation authorities. The Irish authority, the CAR, is principally responsible for price regulation of airport charges at Dublin Airport and of aviation terminal services at Dublin, Cork and Shannon airports. It also has a range of other roles in licensing certain services, schedule co-ordination and consumer protection. This range is also evident in the comparator countries—Denmark, Norway, the UK, France and New Zealand. In fact, the remit is considerably broader in some of these comparators. In France, Denmark and New Zealand, for example, the regulator is responsible for airport security services.

Governance and accountability

While each country has its own specific approach to supervising the work of their aviation regulators, there was no evidence of this having any significant impact on their effectiveness.

The case for economic regulation of airports rests on the individual airport operators having a monopoly or dominant position in their region. In Ireland's case, there is limited prospect for rolling back regulation in the near future, although the CAR's role in travel trade regulation is currently under separate review. Ireland is unique among the comparators, however, in having two separate regulators in the sector. The other, the Irish Aviation Authority (IAA), is responsible for safety regulation and air traffic control, with its charges for the latter regulated in turn by the CAR.

Effectiveness and cost comparisons

On cost comparisons, Ireland compares unfavourably with the comparators in terms of regulator income per head of national population (with the exception of France, where the remit is much wider). In terms of regulator income per regulator employee, only the UK is more expensive than Ireland. In terms of staffing numbers, however, Ireland compares well with the other countries.

Taxi

In the taxi sector, natural monopoly is unlikely and in fact the number of taxis operating in Ireland has risen substantially in recent years. The case for

regulation instead rests on the particular circumstances of taxi operation, for example tourists taking a taxi on arrival at an airport or customers needing to hail a taxi on the street at night. This creates scope for unscrupulous pricing and therefore a case for regulation to protect consumer interests. Regulation is also required to ensure quality control.

Ireland is unique in having a national taxi regulator, the CTR. This makes direct comparison with other places more difficult, and the review therefore examined the situation in some major cities and regions rather than at other national levels—London, Copenhagen, Oslo and Stockholm.

Governance and accountability

In most countries, the framework of regulation is set by legislation and implemented by the local authorities. In London, there is a separate public body, the Public Carriage Office (PCO), which licences taxis and drivers and which is part of Transport for London, a statutory body reporting to the mayor. In Denmark, local authorities regulate taxi services within their boundaries, with a Public Taxi Council made up of 11 politicians responsible for the greater Copenhagen area. In Norway, the Ministry of Transport sets quality and safety standards and maximum prices are set by the national competition authority. Five major cities, including Oslo, are however exempt from fare regulation.

Effectiveness and cost comparisons

The different structures make cost comparison difficult, but in relation to the numbers of licensed taxis, the CTR appears less expensive to operate than the PCO in London. A full international cost comparison would require detailed examination of combined national and local government costs, which the review has not attempted.

Conclusions and Recommendations

The review's conclusions and recommendations are summarised below.

General

- There remains a case for continued regulation, albeit to varying degrees in different sectors.
- In telecoms, rapid technological change means that effective competition has developed in many areas. This has resulted in a scaling back of regulation, which is likely to continue.
- In the energy sector, effective competition has developed in the case of medium and large scale industrial customers, enabling the removal of price regulation for such customers. However, there is insufficient competition in the energy supply market for households and SMEs to remove price controls in those sectors.
- Regulation of the natural monopoly energy transmission and distribution networks will be required for the foreseeable future. Similarly, the monopoly position of Dublin Airport will require continued regulation of airport charges. This will have to be extended to Cork and Shannon airports if plans to fully separate the three state airports are not implemented.

- The rationale for continued regulation of taxi services remains. Regulation in financial services will also continue to be required and is likely to tighten in response to the current global financial crisis. Similarly, regulation of health and safety in the workplace continues to be required.
- An overall restatement of the case and objectives for regulation is required. Neither the case nor the objectives are fully understood in the wider political, business and consumer communities and we recommend a revised statement of principles to help ensure greater clarity and consistency of approach.

Appropriateness of current structures

- The independent status of the regulators is a strength and should be retained. Any attempt to change this would undermine regulatory credibility.
- We do not recommend the creation of a "super-regulator". Variants of this option have been put in place in other countries, but there is insufficient evidence that they have created better or more cost-effective regulation.
- On a more limited basis, we do, though, recommend that the case for merging the CER and ComReg be examined The underlying principles of regulating network services are similar; the scale of regulation required in each sector is diminishing, especially in telecommunications; and they are of a combined scale that should make it possible to gain efficiencies in operation. As a minimum or first step in this process, we recommend that the CER and ComReg share their support and administrative services.
- We also recommend a review of the respective roles of the CAR and IAA. The IAA was not included in this review, but the existence of two aviation regulators is unusual internationally. Another option would be to link the CAR with the new Dublin Transport Authority (DTA). Again, the DTA was not included in this review so that, as with the IAA, we cannot make a firm recommendation on merger. Nonetheless, the options should be considered.
- More generally, a review of existing responsibilities is required in order to reduce the mission creep evident among the regulatory agencies. Overlaps are evident between regulatory and competition roles, for example ComReg's concurrent powers with the Competition Authority. There is also overlap between certain aspects of regulators' consumer protection functions and the role of the National Consumer Agency (NCA). The report notes that a merger of the Competition Authority and the NCA was announced in the 2009 Irish government budget. In health and safety, some regulators have responsibilities that do not appear to fit with the core role of economic regulation: for example the CER's role in setting safety standards for electrical contractors and gas fitters.
- We recommend more formal co-operation between the regulators, similar to the model of the Joint Regulators Group in the UK. This would demonstrate a more structured, transparent approach to ensuring consistency, exchanging good practice and researching shared areas of interest.

Governance and accountability

- We recommend that a more systematic approach to evaluating regulatory performance be developed, including objective tests of progress towards achieving the desired outcomes and reviews of operating costs.

- We recommend that the Financial Regulator consumer panel model should be adopted by the other regulators, in particular the CER and ComReg. While consumer panels already exist in some cases, we believe that they should be strengthened, and that they should include representation from the NCA.
- We believe that effective parliamentary scrutiny of regulators is essential in maintaining the legitimacy of continued intervention and its long-term effectiveness. The current arrangements for Oireachtas scrutiny are not considered to be effective, not least by committee members themselves. We recommend that the resources available to support parliamentary scrutiny are reviewed and revised if necessary.
- We believe in the case of the economic regulators that multi-member commissions make for more effective regulation than single-member commissions and recommend that they should be the norm in all cases. There is a cost implication to this, especially for a small regulator, but the regulatory benefits are clear.
- There is a general view that the current framework and process for appeals is unsatisfactory, although there is no consensus on what should replace it. We recommend the model of a single, cross-sector specialist appeals panel, which would deal with appeals of decisions by the CAR, the CER, ComReg and the CTR There are complex issues to be considered in the design and implementation of this model. However, we believe that these are worth resolving in order to bring greater confidence to the regulatory appeals process.

Adequacy of existing mandates

- We recommend that each regulator should be subject to a fundamental mandate review by government on a regular basis, most likely every five years. This would cover market and technology changes, reset objectives where necessary and propose any legislative or organisational changes required. While there are risks associated with this, the benefits of ensuring that mandates, responsibilities and structures remain appropriate to market needs will outweigh these.
- We recommend that the existing provision for regulators to provide advice to ministers should continue. This is common practice internationally and there is no evidence to suggest that it distorts the regulatory process. Departments do of course need to retain sufficient in-house expertise to ensure balanced advice to ministers.
- We recommend that regulators review their risk-assessment systems to ensure that sufficient attention is paid to anticipating the effects of major systemic shocks. Financial regulators generally were unable to anticipate or mitigate the impact of the current market turmoil. Similar shocks could occur in other sectors, for example in relation to security of energy supply. They may be out of regulators direct control, but they will have a major impact on how they operate.

Effectiveness and value for money

- There is evidence of regulation being generally more expensive to administer in Ireland than in the comparator countries. Lower cost regulation does not mean better regulation. However, we recommend that the reasons for the cost variations be explored further from an accounting perspective.

2. Introduction

The Economist Intelligence Unit was contracted by the Department of the Taoiseach (the prime minister) in May 2008 to undertake a review of the regulatory environment in Ireland. The Economist Intelligence Unit contracted the consultancy services of Compecon Ltd to assist in carrying out the review. The commissioning of the review meets a commitment made in the *Agreed Programme for government*, published in June 2007, to instigate a review designed to ensure that the existing regulatory regime operates efficiently, balances the needs of consumers and producers, and does not impose excessive costs on the economy. The review was commissioned following an open tender procedure and has been overseen by an inter-departmental group chaired by the Department of the Taoiseach and including representatives from the Departments of Finance; Communications, Energy and Natural Resources; Enterprise, Trade and Employment; Transport; and the Office of the Attorney General.

The two broad objectives of the review have been to benchmark Irish economic sectoral regulators against comparable international practice and to prepare conclusions and recommendations on how structures in Ireland might be improved. It has examined both the overall system of economic regulation and, as case studies, the operation of selected sector-specific regulators—in energy, communications, transport (civil aviation and taxis), health and safety, and financial services.

Within these broad objectives, the review has sought to address five key questions:

- whether current regulatory structures remain appropriate, given developments since their establishment and likely future requirements;
- whether existing statutory mandates sufficiently protect both public policy objectives and consumer interests, having regard to international best practice;
- the potential to merge regulatory functions in the light of international experience;
- the extent to which regulatory structures are effective and provide value for money based on international benchmarks; and
- the potential to strengthen accountability arrangements relating to the performance of regulatory functions.

Our approach to the review has involved a combination of desk research, literature review, over 40 face-to-face interviews with regulators, government departments, business representatives and others within Ireland, and telephone or e-mail interviews with respondents in the countries selected for comparison.

Within Ireland, we have held meetings with six regulators, five government departments, members of Oireachtas committees, business representative

groups, the Competition Authority, the National Consumer Agency and the Irish Congress of Trade Unions.

Internationally, research has been undertaken in 11 countries with a different combination of sectors covered in each. In total, there are 33 separate "units" of international work, each unit being one sector in one country. A great deal of data and information has been collected and provides a unique resource of material against which to benchmark the Irish regulatory system.

Patrick Massey of Compecon Ltd was engaged by the Economist Intelligence Unit as a consultant with expertise on the regulatory environment in Ireland.

The Economist Intelligence Unit bears sole responsibility for this research. The findings and views expressed in this report do not necessarily reflect the views of the inter-departmental steering group. Our sincere thanks go to the interviewees for sharing their insights on this topic.

3. Principles of economic regulation

Introduction

In this chapter of the report we provide an overview of the rationale for economic regulation, how the approach to regulation has evolved internationally and how this evolution has been influenced by the growing economic literature on regulation that first began to emerge in the 1960s. The aim is to provide a research and evidence-based framework within which the regulatory regime in Ireland and the comparator countries can be reviewed.

A narrow definition of economic regulation would limit it to sectoral regulators the functions of which include regulating the economic operations of one or more firms in a specific industry. This involves the regulation of commercial decisions such as the setting of prices. It is designed to prevent the firm from exploiting its market power by charging excessive prices. The Commission for Aviation Regulation (CAR), the Commission for Energy Regulation (CER), the Commission for Communications Regulation (ComReg) and the Commission for Taxi Regulation (CTR)[1] all satisfy this definition and the terms of reference for this review required that it include case studies of all four.

Arguably, all regulation has some economic impact. While pure economic regulators might have specific functions in relation to regulating prices of firms within a sector, decisions by other types of regulatory agencies may have implications for prices charged by the firms affected. The two other agencies chosen as case studies for inclusion in this review, the (Financial Regulator and the Health and Safety Authority (HSA) are examples of this more general type of regulatory agency rather than purely economic regulators. The different characteristics and roles of the agencies included in the review obviously have implications for the extent to which comparisons can be made between them.

The evolution of economic regulation of public utilities

The energy and telecommunications sectors have traditionally been referred to in economics literature as public utilities[2]. Public utility industries were traditionally

[1] The Oireachtas (Irish Parliament) has enacted legislation providing for the establishment of a new Dublin Transport Authority (DTA) to regulate transport in the city, but bus and rail transport are outside the scope of the present study. While the CTR's primary functions include regulating taxi fares and thus come within the definition of economic regulation, we suggest elsewhere in the report that the rationale for regulating taxi fares differs significantly from that for regulating public utilities and airport services.

[2] Water and sewage services also come within the definition of a public utility, although that sector lies outside the scope of this review. While airport services might not traditionally be regarded as being a public utility the issues that arise in the economic regulation of airports are similar to those that arise in gas and electricity networks.

regarded as natural monopolies[3]. Some form of regulatory control was considered necessary to prevent utility companies from exploiting their monopoly power and charging excessive prices to consumers. In Ireland, the traditional policy response to such natural monopolies was to nationalise the industry and extend the monopoly into the upstream production and downstream supply markets, thereby establishing state-owned, vertically integrated, monopoly public utility operators. This was a common response to the natural monopoly problem in many European countries. In contrast, in the US private ownership of such industries was the norm, with the potential for abuse of market power because of natural monopoly being dealt with by regulation.

State ownership was traditionally seen as a means of protecting consumers against abuse of market power by natural monopoly utilities, since it was assumed that public ownership would ensure that these industries were operated in the public interest. This assumption is now generally seen as flawed, however. This is because of the existence of principal-agent problems and information asymmetries (managers have more information about the business than government or regulators), which limit the ability of government to prevent utilities from exploiting their market power[4].

In some instances, additional regulatory constraints were imposed on state companies in the form of a "break-even" mandate—for example, the Electricity Supply Board (ESB)[5]. Such break-even obligations can be seen as a further regulatory mechanism designed to prevent the firm from taking advantage of the natural monopoly to earn excess profits. Such a mechanism is not very effective as the firm may earn monopoly profits but record a break-even position in its accounts since the monopoly profits can be absorbed in various ways.

While doubts were raised about the traditional European model of state control as a regulatory tool, economic analysis also called into question the rate-of-return model traditionally employed to regulate privately owned utilities in the US. Specifically, rate-of-return regulation was seen to provide little incentive for regulated firms to reduce costs and maximise efficiency. As rate-of-return regulation linked the regulated firm's profits to its asset base, it was also seen to encourage excessive or "gold plating" investment. Empirical studies indicated that regulation had no impact on regulated firms' behaviour[6].

Regulators are prone to regulatory capture, which may be defined as the regulator implementing policies that further the interests of the regulated firm

[3] It is now recognised that only parts of these industries such as the transmission and distribution networks for gas and electricity are natural monopolies, while the other elements such as generation and supply are potentially competitive. In telecommunications the "local loop" was traditionally considered a natural monopoly although technological developments mean that this is no longer the case.

[4] M Chick, (1993), Nationalisaton and the Background to Recent Regulatory Issues, in R Sugden, (1994) ed., *Industrial Economic Regulation,* London, Routledge.

[5] Legislation permitted the ESB to include a provision for capital replacement in its allowed costs. Normal accounting conventions would record such a provision as profit. Department of Transport, Energy and Communication, (1997), *Proposals for Reform of the Electricity Supply Industry in Ireland*.

[6] G J Stigler and C Friedland (1962), What Can Regulators Regulate? The Case of Electricity, *Journal of Law and Economics*, 5: 1-19.

at the expense of the wider public interest[7]. Some consider that regulatory capture is inevitable[8]. Information asymmetries mean that firms are better informed than regulators about their business, which means that regulators are dependent on the firm for information. The fact that regulated firms were the main repository of specialist industry expertise meant that regulators often recruited staff from regulated firms. Similarly, the potential for senior staff in regulatory agencies to take up consultancy or board positions with regulated firms upon retirement also gave rise to potential conflicts of interest[9]. Repeated close interaction between regulators and their counterparts in regulated firms was also seen as contributing to regulatory capture[10].

From the early 1980s onwards many countries implemented wide-ranging reforms of the economic regulation of public utilities[11]. On both sides of the Atlantic the traditional forms of regulation were seen to have failed. In addition, the key role that public utility industries played in modern economies and the contribution that they could make to better macroeconomic performance were major factors in driving change. Technological drivers also played an important role in regulatory changes, especially in telecommunications. They altered the basic characteristics of the industry to such an extent that the previous system of regulatory controls was rendered obsolete. Financial services was another area where technological change contributed to the pressure for regulatory reform. Significantly, EU directives began to determine the direction and frameworks for regulatory action, an issue that we cover below.

Reform of economic regulation of public utilities thus sought to address the perceived shortcomings of traditional regulatory structures and thereby improve the performance and efficiency of those industries. The latter objective was important because of the significant impact that utility industries had on overall competitiveness. The reform process adopted in many countries had two broad elements:

- the introduction of competition into those parts of public utility industries where competition was possible; and

[7] M Armstrong and D Sappington, (2006), Regulation, Competition and Liberalization, *Journal of Economic Literature*, XLIV 325-66. There is a substantial literature on regulatory capture, which includes G J Stigler, (1971), The Economic Theory of Regulation, *Bell Journal of* Economics, 2(1): 3-21; G S Becker, (1983), A Theory of Competition Among Pressure Groups for Political Influence, *Quarterly Journal of Economics*, 98(3): 371-400; and (1985) Public Policies, Pressure Groups and Deadweight Costs, *Journal of Public Economics*, 28(3): 329-47; J-J Laffont and J F Tirole, (1993), *A Theory of Incentives in Procurement and Regulation*, Cambridge: MIT Press and J F Dewey, (2000), More is Less? Regulation in a Rent-Seeking World, *Journal of Regulatory Economics*, 18(2): 95-112.

[8] A E Kahn, (1988), *The Economics of Regulation Principles and Institutions*, Cambridge, Ma, MIT Press.

[9] In a number of countries, including Ireland, there are restrictions on members of regulatory commissions taking up appointments with regulated firms on leaving office for that reason.

[10] During the course of our discussions with regulatory agencies, several commented on the fact that they had much more developed relations with the regulated industry than with customer groups. Similarly, in chapter 4 we note the example of one agency that requested that the firms that it was regulating should prepare proposals on how they should be regulated and then invited third parties to comment on those proposals.

[11] Such reforms are generally considered to have emerged independently in the US and UK in the early 1980s. In the US this is linked to the landmark 1982 antitrust case that resulted in the break-up of monopoly telephone operator, AT&T, while in the UK it is associated with the decision by the then Conservative Party government that led to the privatisation of British Telecom in 1983.

- the development of improved methods of regulating where regulation was still required. Ongoing regulation was required in the case of the natural monopoly parts of the industry, while regulation of newly liberalised markets was also seen to be necessary in the short run until effective competition emerged.

Under the traditional state-owned monopoly model the state fulfilled three different roles in airports, energy and telecommunications: policy-making, service provision and regulation. In other words, ministers and government departments were simultaneously responsible for determining policy for the sector, owning the monopoly service provider and regulating the market[12]. Market liberalisation of these industries, however, gave rise to potential conflicts of interest between the minister's role as market regulator and as owner of the dominant firm in that market. In order to address this issue a number of independent regulatory agencies were established and were assigned responsibility for exercising the regulatory function within a policy context set by the minister and government[13]. In the energy and communications sectors EU measures actually required the establishment of such independent sectoral regulators.

Some further aspects of regulating utility industries merit mentioning at this point:

- the issue of regulatory credibility and commitment;
- the trade-off between short-term and long-term gains; and
- promoting entry.

The issue of regulatory credibility and commitment arises because of the sunk-cost nature of investment in public utilities and the long lifespan of the assets. Once the regulated firm has invested in new capacity, a price that is sufficient to cover its variable costs will enable it to continue supplying services[14]. The risk that the regulator may set prices *ex post* that are too low to cover the fixed costs of the investment may deter firms from undertaking such investment *ex ante* as firms will recognise the potential for the regulator to alter the rules once the investment has been made. Financial institutions will also recognise this risk, resulting in the cost of raising capital for such projects being increased. Such problems can be overcome by obliging the regulator to allow the regulated firm to earn a "fair" rate of return on its investment, although an overly generous guarantee may mean that unnecessary or inefficient projects have to be rewarded as much as efficient ones.

Forcing dominant suppliers to charge low prices might benefit consumers in the short term, but it may also inhibit entry by new suppliers, thus preventing the

[12] With a single state-owned monopoly service provider, regulation of the sector was largely confined to regulating the prices charged by the state monopoly.

[13] This model was described in Department of Public Enterprise, (2000), and its application can be seen in key aspects of Ireland's regulatory regime for communications, energy and airports.

[14] Take the example of an electricity generating plant. Once built, the cost of the plant is sunk while plants typically have a life span of 20 years or more. Once the plant has been built, if the price is sufficient to cover the operating costs, then it makes sense to keep it operating since the fixed costs cannot be recovered by withdrawing from the market.

development of competition and lower prices in the longer term to the detriment of consumers. Thus, regulators must trade-off short-term against long-term gains.

While regulators might adopt measures that include maintaining higher prices in the short run to encourage new entrants, it is important that these should not encourage inefficient entry since this will increase prices to consumers in the long run[15].

Price-cap regulation

Because of doubts about the efficacy of the US model of rate-of-return regulation, the UK government commissioned a study of all options for regulating British Telecom (BT) before its privatisation in 1983. The study recommended an alternative regulatory mechanism that involved capping prices. It argued that such price-cap regulation was superior to rate-of-return regulation in terms of restraining monopoly power, promoting competition, reducing X-inefficiency and providing incentives for cost reductions. It also claimed that price-cap regulation would be simpler to operate and be less vulnerable to producer capture[16]. As a result, price-cap regulation was applied to BT following privatisation and was subsequently applied to electricity, gas and a number of other industries in the UK. Several US states subsequently switched from rate-of-return to price-cap regulation of telecommunications. Price capping has since been applied by regulatory agencies in a number of countries throughout the world.

Price-cap regulation is frequently referred to as incentive regulation[17]. The regulator sets a maximum rate for annual price increases for a range of the regulated firm's activities. The price cap is generally set by reference to the general rate of inflation as measured by the consumer price index (CPI). Where the regulator believes that the regulated firm can cut costs by improving efficiency, the rate of price increase permitted is less than the rate of inflation, ie, the price cap is expressed as CPI minus x, where x is the regulator's estimate of possible efficiency gains. Theoretically, the regulated firm faces a strong incentive to achieve greater cost savings than the target set, since this will increase its profits. However, this in turn provides more accurate information to the regulator about potential efficiency gains when the price cap is due for review. In other words, price-cap regulation attempts to overcome the information asymmetry problem faced by regulators by encouraging the regulated firm to reveal accurate information about the potential for cost reductions.

Price caps normally apply for a number of years. The longer the length of time between price-cap reviews, the greater the incentive for productive efficiency, ie, cost cutting, since it increases the benefit to the firm arising from any cost

[15] Armstrong and Sappington, (2006), highlight the dangers of certain policies designed to aid new entrants.

[16] S G Littlechild, (1983), Regulation of British Telecommunications Profitability, London, HMSO.

[17] While incentive regulation grew in popularity in the 1980s, the concept itself is an old one. See Laffont and Tirole, (1993) at note 7.

reductions. Long lags, however, might adversely affect allocative efficiency, as they allow for greater divergence between price and costs. There is obviously some trade-off between these two objectives. A five-year gap between reviews has been chosen in many cases.

Price caps are generally set in respect of a basket of products. This obviously simplifies the task of the regulator. It also allows regulated firms to increase profits and, if the price cap ensures that consumers, as a whole, are not worse off as a result, the net result is increased social welfare. In other words, by giving regulated firms freedom to adjust the prices of specific products within the framework of a price cap on the overall product basket, it seeks to promote efficiency and innovation, given the firm's information advantage.

Pure price-cap regulation would not permit any degree of cost pass-through. In the UK, cost pass-through is permitted in respect of a relatively large part of the regulated firms' total costs[18]. Permitting cost pass-through is designed to protect the firm against increases in costs that are outside of its control, while allowing consumers to benefit from downward movements in costs.

Although price-cap regulation is seen as superior to traditional rate-of-return regulation, it does have some significant limitations[19]. Empirical evidence indicates that although price caps may be superior to traditional rate-of-return regulation, competition, where it is possible, is likely to yield more efficient outcomes than regulation. Evidence from local US telephony firms indicates that those subject to price-cap regulation achieved higher levels of efficiency than those subject to rate-of-return regulation[20]. Evidence for all four UK utility industries, along with airports and telecoms in the US, found "little evidence that firms had moved towards more efficient pricing structures" under price-cap constraints in contrast with a move towards cost-reflective pricing where competition had been introduced[21].

Claims that price caps would reduce the regulatory burden because they did not require the measurement of capital or rates of return have proven to be incorrect. Regulators concerned with allocative efficiency must take such factors into account[22]. In the UK price-cap regulation has become more like rate-of-return regulation over time. Estimating the cost of capital and the value of the regulated firm's asset base is a complex task. Accounting profits and asset valuations are particularly subjective in capital-intensive businesses like utilities,

[18] M Armstrong, S Cowan and J Vickers, (1994), *Regulatory Reform, Economic Analysis and the British Experience*, Cambridge, Ma, MIT Press.

[19] J-J Laffont and J F Tirole, (2000), *Competition in Telecommunications,* Cambridge Ma, MIT Press, Laffont and Tirole, (2003) and Laffont (2004).

[20] M Resende, (2000), Regulatory Regimes and Efficiency in US Local Telephony, *Oxford Economic Papers*, 52(3): 447-70.

[21] M Giuletti and C Waddams-Price (2000), *Incentive Regulation and Efficient Pricing*, Royal Economic Society, Annual Conference, mimeo.

[22] S G Littlechild, (1986), *Economic Regulation of Privatised Water Authorities*, London, HMSO; Armstrong et al, (1994) at note.

with long-lived assets[23]. Where utilities have been privatised, share price data and analysts' reports provide additional information to the regulator.

"Effective regulation of costs and capital outlays would require a detailed, day-by-day, transaction-by-transaction and decision-by-decision review of every aspect of the company's operation. Commissions could do so only if they were prepared completely to duplicate the role of management itself."[24]

"...price regulation is typically highly imperfect, however well the regulators do their jobs..."[25]

Regulation is a repeated game that provides scope for strategic behaviour by the regulated firm, which will recognise that although it will be able to retain efficiency gains in excess of those set by the regulator in the short run, such gains will lead to tighter price caps in the future[26]. Thus, its proponents originally argued that price capping would only work on a one-off basis[27]. Studies report considerable evidence of gaming around the time of price reviews in a number of regulated sectors in the UK and US[28]. Price capping also assumes that firms are profit maximisers and relies on providing firms with an incentive to increase profits as a means of inducing them to provide information to the regulator. Public-sector firms may not be profit maximisers, which raises questions about the effectiveness of applying price-cap controls to such firms[29].

High profits earned by regulated firms prompted regulators to adjust price caps ahead of the originally scheduled review date in both the UK and US. Although price-cap regulation is supposed to encourage the firm to try and exceed the regulator's target for efficiency gains, by allowing it to keep profits earned as a result, in practice high profits were regarded as politically unacceptable and regulators acted to reduce them. Such actions, however, obviously reduce the incentive effects and undermine the credibility of the regulator. Such episodes also raise questions about whether the object of regulation is to promote greater efficiency or to reduce industry rents.

Like other forms of price regulation, price caps provide no incentive for the firm to deliver a good quality service. If anything, the firm has an incentive to under-invest in quality. Consequently, price capping like all forms of regulation, also requires that the quality of services be regulated. A E Kahn argues that the

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[23] A Mayer and T Jenkinson, (1997), Regulation, Diversification and the Separate Listing of Utilities in M Beesley (1977) ed., *Regulating Utilities: Broadening the Debate,* London, Institute for Economic Affairs.

[24] A E Kahn, (1998), *The Economics of Regulation,* Cambridge, Ma, MIT Press.

[25] D Currie, (1997), Regulating Utilities: The Labour View, in M Beesley (1997) ed., *Regulating Utilities: Broadening the Debate,* London, Institute for Economic Affairs, p 3.

[26] Laffont and Tirole, (2003) at note 7.

[27] S G Littlechild (1983) at note and M E Beesley and S G Littlechild (1988), Privatisation, Principles, Problems and Priorities, in C Johnson ed., *Privatisation and Ownership*, London, Pinter.

[28] Giuletti and Waddams-Price (2000) at note.

[29] For this reason Dodgson (2003) argued that price-cap regulation should not be applied to the Post Office in the UK. J Dodgson (2003), Liberalizing Postal Services in C Robinson ed., *Competition and Regulation in Utility Markets*, Institute for Economic Affairs.

regulator's role in ensuring quality is essentially a negative one, raising fundamental questions about the efficacy of the entire process[30].

Financial services regulation

There are two broad categories of regulatory issues that are relevant in the financial services sector. The first relates to prudential regulation while the second involves consumer information. The case for prudential regulation rests on the unique role of money in the economy, together with the risk of instability of banks due to their ratios of cash reserves and capital to assets.

Prudential regulation seeks to ensure that banks maintain adequate reserves of capital and that they do not engage in excessive risk taking. It is likely, for example, that if some banks engage in excessive risk taking, competitive pressures will force others to follow suit[31]. Unrealistic asset valuations by one bank are likely to be matched by others[32]. A further reason for prudential regulation is the concern that the failure of an individual bank may lead to a loss in public confidence in the banking system, with the risk of a run on other sound banks. In this way the banking system is seen to be vulnerable to possible contagion. A failure of the wider financial system would have major negative effects on the entire economy. Thus, it is suggested that financial stability is a form of "public good" and this constitutes the basic justification for financial regulation[33].

Such views have been criticised most notably by proponents of "free banking" who argue that banks and financial institutions should be treated no differently to other institutions and that the general presumption that competition is superior to regulation applies as much to banks as to other firms[34]. Recent developments in financial service markets do, however, reinforce the case for financial regulation, although they also call into question the effectiveness of existing regulatory regimes.

Regulation to protect consumers of financial services reflects the fact that the complexity of many financial products means that consumers have insufficient information to decide whether particular products are suited to their needs. While protecting consumers may be an important consideration in such circumstances, the existence of this type of information asymmetry may lead to market failure, which suggests an additional justification for such regulatory intervention in financial services.

[30] A E Kahn (1988) at note.

[31] C Goodhart (1988), *The Evolution of Central Banks*, Cambridge Ma, MIT Press.

[32] H P Minsky (1982), *Inflation, Recession and Economic Policy*, Brighton, Wheatsheaf. This view would appear to be particularly relevant at the present time.

[33] R P Kinsella, (1988), Financial Regulation: A New Approach, *Irish Banking Review,* Spring 1988: 3-21.

[34] For a summary of this viewpoint see, K Dowd, (1996), The Case for Financial *Laissez Faire*, *Economic Journal* 106: 679-87.

Health and safety

Workplace health and safety regulation is rather different in nature to economic regulation. On the face of it, the rationale for such regulation may appear self evidently to be the protection of workers. In economic terms, information about risk is imperfect and may cause individuals to make non-optimal decisions. Nevertheless, it is important to recognise that, as with other types of regulation, health and safety regulation imposes costs on business. This means that there is a need to ensure that such costs are not disproportionate to the desired objective. Similarly, it is important to ensure that such regulations are implemented in an efficient manner, thereby minimising the costs involved.

The limits of regulation

Regulation imposes significant economic costs. In recent years there has been a growing recognition among policymakers of the potential adverse effects of inefficient regulation and its potential to impose significant costs and distortions on the economy. The Mandelkern Group, for example, estimated that at an EU level the burden of regulation was equivalent to 2-5% of total GDP[35].

Direct regulatory costs represent only a fraction of the true cost of regulation. The main cost of regulation is the result of compliance costs, ie, the costs of meeting regulatory standards, which are borne by the industry and for the most part are never even measured. In other words, there is a cost to the firm of conforming to the regulations, but regulators frequently ignore such costs[36]. In effect, regulation suffers from a form of negative externality since the direct costs of regulation borne by the regulator are less than the cost to society, resulting in an excessive level of regulation from society's point of view. As the regulator does not bear those costs it has an in-built bias towards setting higher targets that enables it to claim that it is trying to improve services for customers.

There are also additional hidden costs to regulation. For example, regulators sometimes establish rules designed to promote the adoption of new technologies, but the danger is that they may choose the wrong technology[37]. International experience also reveals examples where regulatory interventions stifled innovation. For example, in the US regulation delayed the introduction of voice messaging in telephony for more than a decade, with an estimated loss of consumer surplus of US$1.27bn per year[38]. The cost to consumers of regulation of cable television in the US was estimated at US$5bn per year[39]. More generally, the pace of technological change in telecoms means that there is an inevitable time lag before regulatory policies are adjusted to changed market

[35] Mandelkern Group on Better Regulation, Final Report, November 2001.

[36] Arguably this is something that regulatory impact assessments (RIAs) are designed to address.

[37] L Waverman and E Sirrel, (1997), European Telecommunications Markets on the Verge of Full Liberalization, *Journal of Economic Perspectives*, 11(4): 113-26. In order to prevent this, EU telecoms framework requires that regulatory decisions be technologically neutral.

[38] D Newbery, (2005), The Relationship Between Regulation and Competition Policy for Regulated Industries, LEAR Conference, Rome, mimeo.

[39] R W Crandall, (2003), An End to Economic Regulation? in C Robinson ed., *Competition and Regulation in Utility Markets*, London, Institute for Economic Affairs.

circumstances and the cost of such lags is considered likely to be substantial[40]. Energy regulation has been criticised for holding back innovation in the US electricity industry by blocking distributed generation technology, thereby increasing transmission and distribution costs[41]. The failure of regulators to adopt new innovations may occur in part because regulatory agencies fail to keep up to date by recruiting individuals familiar with the latest technological developments in the industry that they are responsible for regulating[42].

International experience also shows that regulatory agencies have a tendency to expand their role and to favour retaining regulatory controls even though the rationale for regulatory intervention may no longer be valid[43]. The literature has also identified the tendency for firms to abuse the regulatory process to obtain protection from competition. Entrants may seek to manipulate the regulatory process and use it to obtain protection against competition from the incumbent[44]. This may be particularly true where regulation is asymmetric as it has been in Ireland in energy and communications—ie, it is concerned with regulating a dominant firm and protecting entrants against abuse of dominance. Strong competition by a dominant firm may be wrongly perceived as abusive behaviour and the risk of such an outcome might deter such firms from competing aggressively. Asymmetric regulation may also reduce the incentive for entrants to compete strongly, since the benefit of being successful is that restraints on the incumbent will be removed, thereby exposing the entrants to more vigorous competition.

"Understandably, the incumbent would have us go faster, increasing its commercial freedom and profit potential, whereas the recent market entrants would tend to fear their exposure to anti-competitive behaviour in these circumstances."[45]

More generally, in markets where competition is possible, it results in substantial welfare gains relative to regulation. Regulation cannot replicate the level of innovation evidenced in competitive markets[46]. Thus, estimates of efficiency gains from removing regulation in markets where competition is possible tend substantially to underestimate the likely gains. It has also been

[40] D Geradin and R O'Donoghue, (2005), The Concurrent Application of Competition Law and Regulation: The Case of Margin Squeeze Abuses in the Telecommunications Sector, *Journal of Competition Law & Economics*, 1(2): 355-425.

[41] L Kiesling, (2004), The North American Blackout and Electricity Policy: Alternatives to Transmission Construction, *Economic Affairs* 24(1): 53-7.

[42] On this point see B Howell, (2006), *An Institutional Economics Analysis of Regulatory Institutions in the Telecommunications Sector*, New Zealand Institute for the Study of Competition and Regulation.

[43] See, for example, R Noll (1995), The Role of Antitrust in Telecommunications, *Antitrust Bulletin*, 39(3): 501-28; P MacAvoy (1996), *The Failure of Antitrust and Regulation to Establish Competition in Long-Distance Telephone Services*, AEI Studies in Telecommunications Deregulation, MIT Press; I M Stelzer (1997), Vertically Integrated Utilities: The Regulator's Poisoned Chalice, in *Lectures in Competition and Regulatory Policy*, Institute for Economic Affairs, (2000); C Robinson, (2004), Gas, Electricity and the Energy Review in C Robinson ed., *Successes and Failures in Regulating and Deregulating Utilities*, Institute for Economic Affairs and J A Hausman and J G Sidak, (2005), Did Mandatory Unbundling Achieve its Purpose? Empirical Evidence from Five Countries, *Journal of Competition Law & Economics*, 1(1): 173-245.

[44] W J Baumol and J G Sidak, (2004), *Toward Competition in Local Telephony*.

[45] Chisholm, (2008), p 48. Competition law exists to protect firms against behaviour that is genuinely anti-competitive.

[46] A E Kahn, (1988); at note.

suggested that firms may take some time to adjust to a changed regulatory environment and that the benefits may take some time to accrue, which may cause policymakers to become impatient and consider reversing policy[47]. An important lesson of the experience in various countries over the past 20 years is that regulation is not a substitute for competition[48].

Conclusions

In reviewing academic and other research on regulatory systems, we found significant consensus on what criteria should be used to judge effectiveness:

- clarity of functions, and how they are assigned among the relevant bodies;
- organisational autonomy (from both the government and the regulated industry), balanced by accountability;
- accountability, formal and informal; and
- transparency, with open decision making and justification of those decisions.

Other factors related to these are highlighted by researchers and policy-makers. These include the need for secure funding for regulators, paying regulatory staff the appropriate rate for the job and consistency of decision making.

Although the basic principles and criteria are clear, the literature generally does not favour any specific models or structures for regulation[49]. Instead, it recognises a need for regulatory systems to fit the specific economic and political environments of each country. Therefore, a range of different models should be expected, albeit that they should all aim to meet the criteria for effectiveness.

In framing the benchmarking criteria used in this review, as well as the questions asked in the Ireland and international research, we have sought to test for the key principles identified during our literature review.

[47] C Winston, (1998), US Industry Adjustment to Economic Deregulation, *Journal of Economic Perspectives*, 12(3): 89-110. Winston argued that US firms were still adjusting more than 20 years after regulatory reforms were introduced.

[48] S G Littlechild, (1999), *Privatisation, Competition and Regulation*, Institute for Economic Affairs, Wincott Lecture, and Ofgem, (2001), *The Development of British Electricity Trading and Transmission Arrangements (BETTA) A Consultation Paper*, Ofgem. The latter report, for example, describes regulation of the electricity industry in Scotland as "an imperfect substitute for effective competition." (p 13).

[49] Waverman, for example, suggests that no particular regulatory regime is ideal. L Waverman, (2003): Regulatory Incentives and Deregulation in Telecommunications. in C Robinson ed., *Competition and Regulation in Utility Markets*, Institute for Economic Affairs.

4. Economic regulation in Ireland

Introduction

In this chapter of the report we provide an overview of economic regulation in Ireland. The terms of reference required us to assess the existing regulatory regime under the following headings:

- the appropriateness of current regulatory structures;
- governance;
- the adequacy of existing mandates;
- effectiveness and value for money;
- accountability; and
- the potential for restructuring.

This chapter provides an analysis of these issues within the Irish context, while we return to them on a comparative basis in the individual sectoral chapters that follow.

The Irish government's 2004 white paper, *Regulating Better*, estimated that there were over 500 public agencies/bodies in Ireland, and that many of these had a regulatory function—either as a rule-maker or rule-enforcer[1]. This figure was an estimate as there had been no attempt up to that time to quantify the number of bodies, both public and private, with the power to regulate. The white paper identified several different types of regulatory bodies. These included:

- all government departments;
- all local authorities;
- independent sectoral regulators including the Communications Regulator (ComReg), the Commission for Aviation Regulation (CAR), the Commission for Energy Regulation (CER) and the Financial Regulator;
- organisations such as the Office of the Director of Consumer Affairs and the Competition Authority; and
- various agencies under the aegis of government departments that have been delegated regulatory/enforcement functions such as the Food Safety Authority and the Censorship of Publications Board.

A subsequent report, *Regulatory Bodies in Ireland*, published in 2007, put the number of regulatory bodies in Ireland at 213, of which 205 were public-sector

[1] Department of the Taoiseach, (2004), *Regulating Better: A Government White Paper Setting out Six Principles of Better Regulation*.

bodies, including 114 local authorities[2]. The report defined a regulatory body as one that has statutory recognition and has functions in at least two of the following three areas of activity:

- the formulation of goals, the making of rules and/or the setting of standards;
- monitoring, gathering information, scrutiny, inspection, audit and evaluation; and
- enforcement, modifying behaviour, applying rewards and sanctions[3].

In addition to its regulatory role, in order to be considered a regulatory body an organisation had to have the following features:

- be an independent organisation, separate from any other body;
- have some capacity for autonomous decision making;
- have some expectation of continuity over time; and
- have some personnel and financial resources[4].

If we exclude local authorities, then the number of regulatory bodies comes to around 100, with over 90 of these being public-sector bodies.

Evolution of the regulatory environment

As noted in Chapter 3, the electricity and telecommunications sectors in Ireland were traditionally the preserve of state-owned monopolies. Post and telecoms services were operated by a government department until 1984 when these businesses were transferred to two newly established state companies: An Post and Telecom Eireann. The gas industry had historically consisted of a small number of privately owned town gas companies that operated in a small number of the larger towns and cities. These were taken into public ownership during the 1980s with the introduction of natural gas.

Competition legislation, which was first introduced in 1953, largely excluded services including banking, energy and communications until the late 1980s. This exclusion resulted in a financial sector described as among the most heavily regulated in the world[5]. From 1953 until 1986 competition legislation, limited as it was, operated alongside a system of price control. This reliance on price control as a mechanism for economic regulation was criticised by the OECD:

[2] Department of the Taoiseach, (2007), *Bodies in Ireland with Regulatory Powers As of February 2007.* The Report stated that at the time of publication plans for the establishment of a further nine bodies had been announced by various government ministers.

[3] This report adopted a stricter definition of what constituted a regulatory body, which explains to a significant extent why it came up with a much lower figure than the earlier white paper estimate.

[4] This definition is consistent with that used in the wider study of agencification in Ireland (see A-M McGauran, K Verhoest and P C Humphreys (2005), *The Corporate Governance of Agencies in Ireland*, CPMR Research Report No. 6, Dublin, IPA.

[5] DKM, (1984), The Control of Banking in the Republic of Ireland, Dublin, DKM.

"In the 1970s, instead of proceeding with comprehensive legislation on competition, reliance was placed on such mechanisms as the National Prices Commission to monitor, and occasionally to try to control, prices."[6]

"Regulatory Reform/Better Regulation" was one of the original six strands of the Strategic Management Initiative introduced in the Irish public sector in the mid-1990s. As part of this, an action programme entitled *Reducing Red Tape* was launched in July 1999. The main focus of this programme was on administrative simplification and accessibility and quality of legislation. Progress on regulatory reform accelerated, and the agenda widened somewhat, as a result of Ireland's participation in an OECD peer review programme on regulatory reform in 2000-01. The object of the review was to get independent analysis of Ireland's regulatory regime, to benchmark it against best practice internationally and to obtain expert advice on the way forward.

The OECD report, which was presented to the government in April 2001, found that existing systems and capacity for assessing and reporting on the likely implications of proposed regulations needed to be strengthened[7]. In response, a High Level Group on Regulation was established comprised of senior officials from key government departments, offices and external regulatory authorities. The Group was asked to develop and co-ordinate the "Better Regulation" agenda with particular regard to the institutional and policy proposals outlined in the OECD report.

Separately, as noted in Chapter 3, EU measures to liberalise public utility industries required reform of the regulatory regime that applied to those sectors[8]. The energy and telecoms sectors throughout the EU largely consisted of a series of individual national markets. There was recognition that some elements of these industries were potentially competitive and that competition, where it was possible, could yield superior outcomes to traditional forms of regulation. This resulted in the adoption by the European Commission of a number of measures designed to open up national markets to cross-border competition from providers in other member states with the ultimate aim of establishing a single EU market. Thus, the electricity, gas and telecoms industries were opened up to competition in successive stages by virtue of a series of EU directives.

As noted in Chapter 3, the liberalisation of utility industries gave rise to potential conflicts of interest between a minister's traditional role as market regulator and as owner of the dominant firm in that market. In order to address this issue a number of independent regulatory agencies were established and were assigned responsibility for exercising the regulatory function, within a policy context set by government[9]. They were able to recruit specialist staff with skills not generally available within the civil service.

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[6] OECD, (2001), OECD Reviews of Regulatory Reform: Regulatory Reform in Ireland, Paris, OECD, p 16.

[7] OECD, (2001).

8 For the purposes of the present report, public utility industries include electricity, gas and telecommunications.

[9] In energy and communications sectors EU measures actually required the establishment of such independent sectoral regulators.

The Office of the Director of Telecommunications Regulation (ODTR) was established in 1996 and given responsibility for regulation of the telecoms industry. It was subsequently replaced by ComReg in 2002 and the latter's mandate was broadened to include all forms of electronic communications. Responsibility for regulating the postal sector was assigned to ComReg in December 2002. The Commission for Electricity Regulation was established in 1999. It was subsequently renamed the Commission for Energy Regulation (CER) in April 2002, when its remit was extended to include regulation of the gas market.

The CAR was established in 2001 and given responsibility, *inter alia*, for the regulation of airport charges. In contrast with energy and communications the establishment of an independent regulator for airports was not prompted by any EU legislative measures[10]. A further difference was that the airport services market had not been liberalised[11]. In this case, therefore, the potential conflict of interest that existed in energy and telecoms as a result of the state ownership of one of several competing entities does not arise. There is, nevertheless, another potential form of conflict as the state—as owner of the airports—has an interest in maximising the profitability of those airports, while as regulator it is responsible for protecting airport users from excessive charges. The state had no ownership role in the case of taxis so, arguably, there was no potential conflict issue if the state's role is viewed as being simply to protect consumer interests.

The various economic regulators were thus established on a somewhat *ad hoc* basis, for different reasons and with different structures and responsibilities. This raises some questions about consistency of regulatory policy, a point noted in the government's *Regulating Better* white paper.

"The evolution of regulatory policy in Ireland has not, to date, proceeded in a uniform fashion. The result has been the establishment of regulatory institutions with different mandates, as well as different levels of responsibility, different legal bases and different structures. Most other OECD countries have seen a similar pattern of development. One of the main issues is the variety in structures and responsibilities across different sectors. While these may not be significant problems in themselves, the adoption of a national regulatory policy should ensure that consistency is introduced across the regulatory system, where possible. The issue is not about following 'precedent', but rather one of dealing with situations consistently. It is also about public bodies seeking information or designing application processes, as much as possible, in the same format. This would ensure greater confidence in the system, greater transparency in decision making and promote greater efficiency across the various sectors."[12]

The decision to restructure health and safety and financial services regulation emerged from government-established reviews of both sectors. For example, the Health and Safety Authority (HSA) took over responsibility for functions

[10] There are plans for an EU Directive that would require member states to establish an airport regulator.

[11] While there is scope for competition between Cork, Shannon and a number of regional airports, Dublin Airport is generally considered to have a monopoly within its catchment area. See, A Reynolds-Feighan, (2003), A Review of Irish Airports Policy, *Irish Banking Review*, spring, 49-62.

[12] *Regulating Better*, p 34.

that had previously been undertaken by a government department. This followed an independent review that recommended that functions such as decisions to prosecute for breaches of legislation should be undertaken by a body independent of the minister[13]. Similarly, the Financial Regulator was established in 2003 following a government-commissioned review of financial services regulation[14].

Concern about the appropriateness of the existing regulatory structure and the proliferation of regulatory agencies with different structures, mandates and responsibilities was reflected in the 2004 white paper. It confirmed that no new regulatory bodies should be established unless there was a clearly demonstrable need to do so.

"The government will create new sectoral regulators only if the case for a new regulator can be clearly demonstrated in light of existing structures. It will assess the possibilities for rationalisation of sectoral regulators along with promoting the strengthening of existing contacts between the sectoral regulators, the Competition Authority and the Office of the Director of Consumer Affairs."[15]

Respondents' views on regulation

Regulation in general has been identified as imposing a significant burden on business, especially small and medium-sized enterprises (SMEs).

"It has been estimated that 44% of small Irish firms have cited red tape—form filling and compliance with regulatory requirements—as problematic, both as a barrier to market entry and as a significant impediment to business expansion. This is consistent with the results of a government-commissioned survey published in 2003 that found that 54% of businesses felt that regulations were a significant and increasing burden on their business."[16]

A subsequent survey published in 2007 indicated that 55% of all businesses felt that the overall regulatory burden was about right, although 43% of medium-sized enterprises considered it excessive. While 15% of all firms identified health and safety regulation as a heavy burden, this figure rose to 28% in the case of medium-sized firms. Another point worth noting at this stage is that 37% of all firms surveyed identified energy regulation as the area of regulation that government should tackle as a priority, while 35% of those cited costs/impact on costs as the reason why it needed to be addressed[17].

A number of concerns and criticisms of existing regulatory arrangements also emerged during the course of our meetings with various stakeholder groups. It is important that we highlight these here, as indicators of how the current system is perceived by some of its key stakeholders. Concerns were expressed

[13] *Report of the Commission of Inquiry on Safety, Health and Welfare at Work*, Chairman Mr Justice Barrington, July 14th 1983, Dublin, Stationery Office.

[14] *Report of the Implementation Advisory Group on the establishment of a Single Regulatory Authority for the Financial Services Sector,* Dublin, Stationery Office, May 19th 1999 ("the McDowell report").

[15] *Regulating Better*, p 3.

[16] *Regulating Better*, p 23.

[17] Department of the Taoiseach, *Business Regulation Survey 2007.*

by a number of parties, for example, that the current economic regulatory regime lacked a coherent framework. It was felt that agencies had been set up on an *ad hoc* basis with different structures, different appeals mechanisms and different financial structures. Often agencies were established in response to EU legislative requirements. There appeared to be no clear vision at government level of what the regulator's role should be and this contributed to claims of a lack of regulatory accountability. Many stakeholders perceived a lack of vision and expressed the view that, sometimes, there were no clear objectives set out in the legislation establishing a particular regulatory body. It was suggested that there were doubts about whether government trusted the regulators.

It was also felt that departments tended to think vertically. As a result, there was a tendency to establish new regulatory agencies on an *ad hoc* basis without considering whether such functions could be assigned to an existing body. At the same time, once a department had set up a regulatory agency there was a tendency to assign additional functions to that body rather than considering whether such a body was the most appropriate one to undertake a particular task. Consequently, agencies, the core function of which was economic regulation of a particular sector, were often given additional functions and responsibilities for licensing, and various other functions including safety and consumer protection. We were also told that there are no clear criteria for designating what agency should be responsible in the case of new legislation and regulation. In the case of EU directives it is often unclear which department should act as the lead. Frequently, decisions on which agency should be given responsibility for new regulations are not taken until an emergency situation arises, ie, an impending deadline for the implementation of directives.

Appropriateness of current structures

One of the issues that we have been asked to report on is the appropriateness of current regulatory structures. Most of the regulatory bodies that we are dealing with are not just involved in economic regulation, but have a range of additional functions. In a number of instances agencies' roles and responsibilities have grown in an *ad hoc* unplanned manner. In other instances the agency simply inherited functions previously carried out by their parent department. Given the *ad hoc* nature in which many of the regulatory agencies were established and their functions subsequently expanded, there is a need to examine existing regulatory structures.

The differences in the scope and range of the remits of the various regulatory bodies are reflected in differences in the size of the various agencies. Summary details on budgets and staff numbers are set out in Table 1.

Table 1: Details of budget and staff numbers in 2007

	Budget €m	Staff numbers
CAR	4.2	21
CER	15.5	59
ComReg	36.7	108
CTR	21.9	49.5
Financial Regulator	53.2	343.5
HSA	[18]27.1	197

Note: The budget figure for ComReg excludes €52m in spectrum fees. In a sense, ComReg simply collects such fees on behalf of the Exchequer so including them as part of its budget would grossly distort the comparison with other agencies. Staff numbers are whole time equivalents.

Source: Annual Reports of the various agencies.

In terms of budget and staff resources, the Financial Regulator is much larger than the other regulatory bodies. The HSA ranks next in terms of staff numbers, although its budget is significantly smaller than that of ComReg. Focusing purely on the four economic regulators, the CAR is a much smaller organisation than ComReg, the CER or the Commission for Taxi Regulation (CTR).

A more detailed breakdown of income for the various regulatory agencies is included in Table 2. This shows that there is a significant variation between the ways in which the various agencies are funded. The four economic regulators are essentially funded by industry levies or licence fees and thus are independent of the Exchequer. The Financial Regulator is funded broadly on a 50:50 basis through a combination of industry levies and Exchequer funding (by means of a direct subvention from the Central Bank), while the HSA is mostly funded by the Exchequer.

Table 2: Sources of income of regulatory bodies (2007, €m)

	Industry levy	Licence fees	Other income	Exchequer funding	Total
CAR	3.7	0.4	0.0	0.0	4.2
CER	15.3	0.1	0.2	0.0	15.5
ComReg	11.1	23.7	1.9	0.0	36.7
CTR	0.0	21.7	0.2	0.0	21.9
HSA	0.0	0.0	0.8	26.3	27.1
Financial Regulator	22.3	0.0	5.5	25.4	53.2

Source: Annual Reports of the various agencies; Note: The €5.5m figure for other income in the Financial Regulator's case includes a €2.2m surplus from the previous year.

We have approached the question of whether current regulatory structures are appropriate by asking whether regulatory intervention is required and, if so, whether the existing regulatory structures are appropriate for such regulation to be effective and efficient. Both here and in the sectoral chapters, we have considered the following criteria in assessing whether or not current regulatory structures are appropriate:

- what was the original rationale for regulatory intervention?

[18] The HSA approach to funding pension costs may result in its annual report income figures differing to those set out in the Irish government's Book of Estimates, which sets out the official funding figures for the various agencies. For the purposes of this analysis pension costs are included whether funded or not.

- is the original rationale for regulatory intervention still valid or is there some other rationale for continued regulation? and
- is the existing regulatory structure capable of providing the type of regulation required, ie, of addressing the justification for having regulation?

It is generally recognised that competitive markets represent the most effective means of ensuring that firms operate efficiently, thus maximising output and providing goods and services to consumers at the lowest possible price, thereby maximising overall economic welfare. The rationale for economic regulation in many of the sectors considered in the present report is that the relevant market is not sufficiently competitive[19]. In some areas, such as telecoms and to a lesser extent energy, this lack of competition may arise because incumbents may continue to enjoy a dominant position for a period after the market has been liberalised. However, in other areas, such as airport services through Dublin Airport, it reflects its ongoing monopoly position. Regulation of prices is required in those circumstances to prevent dominant firms from exploiting consumers by charging excessive prices[20].

In a number of cases there are questions about whether there is a good fit between the existing combination of economic regulation and other functions. All the bodies concerned have certain consumer protection and education functions. These were assigned to the agencies concerned before the establishment of the National Consumer Agency (NCA). Questions clearly arise regarding a potential overlap in roles between regulators and the NCA. In addition, on occasion there may be potential conflict between the regulation and consumer protection roles. This raises issues about where consumer protection should be located. While the Financial Regulator was widely recognised as discharging its consumer protection functions quite well, there was considerable dissatisfaction with other economic regulators. Many felt that they had failed to communicate properly with consumers. In a number of instances regulators expressed the view that while they had good contacts with the regulated industry, they had little contact with customers.

Governance[21]

The various regulatory bodies chosen as case studies for this report include a number of different governance models[22]:

[19] Arguably this is the rationale for regulating airports, energy, telecommunications and to a lesser extent taxis. As noted in Chapter 2, the rationale for financial and health and safety regulation is obviously different.

[20] Of course there are other markets that are not regulated where firms have dominant positions and may be able to charge excessive prices. The justification for regulating utility prices is based on a view that their products are essential services and that intervention to protect consumers from excessive prices is justified. The issue of whether excessive pricing constitutes a breach of competition law is highly controversial, and although there are some precedents at EU level, there have been few cases involving excessive pricing at EU level and none at national level in Ireland.

[21] Under this heading we address the issue of the management structures of the regulatory agencies. The interaction of regulators with ministers and government departments is addressed elsewhere.

[22] The various options were set out in Department of Public Enterprise, *Governance and Accountability in the Regulatory Process: Policy Proposals*, March 2000, which also summarises the various arguments for and against each of the options.

- an individual regulator—in the past the ODTR was an example, while the CAR is a current example;
- a three-member commission—the structure that currently applies in the case of the CER and ComReg, and which there is provision for in the statutes of both the CTR and CAR;
- an individual regulator with consultative/advisory panels—this structure currently applies in the case of the CTR;
- an individual regulator with a part-time board—this structure currently applies in the case of the HSA; and
- an individual regulator with both consultative/advisory panels and a part-time board—this model applies in the case of the Financial Regulator.

The issues involved in addressing the appropriate board structure for the four economic regulators appear somewhat generic and we consider them below. Given the rather unique governance structures that currently exist in the case of the Financial Regulator and the HSA, however, we have opted to discuss the governance issues of those bodies in chapters 6 and 10, respectively.

The advantages of an individual regulator are first, consistency, and second, speedier decision making. Consistency in the decisions of a regulatory authority is important for reducing the level of regulatory uncertainty. It is arguable that the decisions of an individual are more likely to be consistent over time than those of a board or commission, in which case an individual regulator should lead to increased certainty and greater regulatory credibility. Similarly, individual regulators have the potential to execute their functions more rapidly than may be possible for a multi-member board that requires discussion among, and the agreement of, the various members. The extent to which an individual can take decisions more quickly than a board will, however, also depend on the nature of the procedures that have to be followed, and is, to some extent, constrained by the imperative to follow due process. Nevertheless, with an individual regulator, the potential for delays as a result of a possible conflict between board members over a particular decision does not arise[23].

Arguments against an individual regulator include:

- having an individual regulator could lead to the undue personalisation of the regulatory process;
- one individual could not be expected to have a comprehensive range of expertise relevant to the regulated industry; and
- individual regulators could be more susceptible to regulatory capture[24].

A regulatory board is seen as likely to offer a more comprehensive and wide-ranging perspective on regulatory issues and could reduce the risk of personalisation of the process that can arise where there is an individual regulator. In addition, a regulatory board could be seen as more independent

[23] Department of Public Enterprise, (2000).

[24] These arguments were advanced in various submissions to the Department of Public Enterprise, (2000).

than an individual and less vulnerable to possible regulatory capture. As a result, the decisions of a board might be perceived to be more robust. It has also been suggested that it may be more appropriate to have decisions in key regulated sectors taken by a board rather than a single individual, given the importance of such decisions, both for those persons involved in the regulated industries and for the economy as a whole[25].

It has been argued that one of the disadvantages of a group structure is that it can generate internal conflicts that can detract from the regulatory process[26]. Such conflicts could lead to delays in decision making. There also seems to be an implicit suggestion that a group structure might lead to greater inconsistency in decision making, which would have implications for certainty and credibility.

The report published in 2000 by the Department of Public Enterprise concluded that a three-member board or commission, with the members being full-time, was the ideal model. This is the model that has been adopted in practice in the case of the CER and ComReg[27]. In the case of communications, B Tuohy subsequently argued that the growth in the regulatory workload, and the fact that the nature of the tasks and rulings that had to be implemented has become increasingly complex and qualitative, meant that a three-person commission was superior to an individual regulator[28]. The decision in the UK to have single-member regulatory bodies was criticised as tending to personalise the regulatory process. The UK subsequently moved to multi-member commissions[29].

Our discussions with stakeholders indicated that there was a widely held view that a regulatory commission was superior to an agency headed by a single regulator. It was felt that collegiality led to better decision making, for example. Also, a multi-person body might improve institutional memory and having a single regulator might lead to issues becoming highly personalised. It was accepted that some of the existing regulatory agencies were too small to justify having a commission rather than a single individual.

The model of a full-time chief executive and a part-time non-executive board seeks to combine the benefits of having decisions taken by a multi-member board, while reducing the costs involved. It seems implicit in this model that

[25] According to the Department of Public Enterprise, (2000), this point was made in a number of submissions.

[26] The Department of Public Enterprise, (2000), also reported that some submissions argued that the financial costs of a board would reduce the benefits of having such a structure, although the reasons for this are not clear from the report.

[27] The relevant legislation in both cases provides for a commission comprising between one and three persons. The Department of Public Enterprise, (2000), suggested that by allowing such flexibility the legislation allows the decision on the appropriateness of the individual regulator/commission structure to be reconsidered from time to time in the light of changing circumstances.

[28] B Tuohy, *Regulation of the Irish Energy and Communications Sectors—A Paper on Current Issues,* presented to an Expert Meeting on Designing Independent and Accountable Regulatory Authorities for High Quality Regulation, 10th-11th March 2005. The author of the paper was secretary-general of the Department of Communications, Marine & Natural Resources at the time. D Currie (2003) argues that a regulatory commission with staggered replacement over time increases the likelihood of consistency and continuity in regulatory decisions, D Currie, (2003), Mutualisation and Debt-Only Vehicles: Which Way for RPI-x Regulation? in C Robinson ed., *Competition and Regulation in Utility Markets*, Institute for Economic Affairs.

[29] Stelzer cites exchanges in the *Financial Times* between the telecoms regulator and BT chairman during the 1980s as an example of such personalisation of the regulatory process and proposed multi-member regulators to avoid such problems.

part-time members would be independent rather than be representatives of regulated firms or users, in contrast with the HSA model. If part-time members represented particular interests, this would obviously raise questions about regulatory independence and possible regulatory capture. Procedures for the management and control of potential conflicts of interest would be particularly important in the context of part-time members who would be pursuing other activities in addition to regulation. Given the complexities involved in economic regulation of major utilities such as energy and communications, serious questions would seem to arise about the potential for part-time members to exercise effective control over an executive director of a regulatory agency[30].

The structure chosen in the case of the CTR is to have an individual regulator with a statutory advisory council, the members of which have expertise in various relevant disciplines. The benefits claimed for such a model is that it allows ready access to expert advice from diverse perspectives, while decisions, including the decision to accept or reject the expert advice, remain in the hands of the individual regulator. A potential disadvantage of such a model is that appointees to purely advisory positions might perceive their role as representing their respective interests to the regulator, rather than giving impartial advice[31]. It was suggested to us during the course of our meetings with stakeholders that the advisory panel was seen to have helped divert some of the criticism away from the CTR, in effect reducing the degree of personalisation. It was felt that the regulator consulted the panel in all cases before taking decisions.

In the case of the economic regulators a multi-member commission would seem to have a number of advantages over the individual regulator model. The existing arrangements in the case of ComReg and the CER, which both have three-member commissions, seem appropriate. On that basis there is an argument for having a three-person commission in the case of the CAR and CTR, although their relatively small size suggests that this option might not be practical and could have a significant impact on costs. In the case of the CTR, there is a statutory advisory council that the regulator may consult. We note that since our study commenced it has been indicated that the CTR will be amalgamated with the newly established Dublin Transport Authority. The issue of a commission may be addressed in the context of the proposed changes.

Some examples of the approach taken to governance in the comparator countries are helpful at this stage. Generally, the pattern is one of collective decision taking by an authority or board of directors, with a lead executive responsibility held by a chief executive officer (CEO) or equivalent. The UK offers a clear example of the application of commercial governance practices to sectoral regulators with a board consisting of executive and non-executive directors. This reflects a decisive policy shift in the late 1990s away from a single regulator structure after a series of public spats between the regulated entities and the regulator had effectively personalised the regulatory process. In Ofgem, there are non-executive directors with expertise from industry, social

[30] The complex issues involved in regulating such industries means that part-time board members may be less well informed than full-time ones.

[31] Department of Public Enterprise, (2000).

policy, environment, finance and European affairs. Ofcom has a board that acts on the principle of collective responsibility where all board members are deemed to have agreed with all decisions. The Health and Safety Executive (HSE) board is appointed following consultation with representative groups including employers, trade unions and local authorities.

The Australian governance system is similar to that in the CER and ComReg. The Australian Energy Regulator (AER) has a three-member commission. The CEO leads the "office of the AER", which provides advice to the board. However, in contrast to the CER, the AER is not an independent institution; it is part of the Australian competition authority. The Australian financial consumer protection regulator, the Australian Securities and Investment Commission (ASIC), is an independent public body with three full-time commissioners. A recent strategic review concluded that this structure remained optimal, while also deciding to appoint an external advisory panel to advise on market development and potential systemic issues. The Australian telecoms regulator, the Australian Communications and Media Authority (ACMA), is governed by an authority comprising a chairman and deputy chairman, one full-time member, four part-time members and an associate member.

The Scandinavian countries have more of a single regulator approach albeit within the confines of being non-independent ministerial entities. In this respect the regulator or director-general would not have the same degree of discretion as in independent agencies. In Norway for example, the decision making in the energy and telecoms regulators is the responsibility of the director-general who in turn reports to the respective government departments. The Norwegian financial regulator, however, is headed by a board of five members reporting to the Ministry of Finance. The Danish financial regulator, Finanstilsynet (the Danish Financial Supervisory Authority), is an agency under the Ministry of Economics. The Danish energy regulator is unusual in that its members are appointed by the Ministry of Climate and Energy while the secretariat is managed by the competition authority.

Experience in other comparator countries is consistent with a board of directors' governance model with varying degrees of independence from central government. The German regulator covering energy, communications, post and railways is an independent agency governed by a board of directors with an advisory council consisting of 16 members from both houses of parliament. The New Zealand aviation authority is a crown entity governed by five members.

Overall, the evidence is in favour of a governance system of collective decision taking. It is also worth noting that Australia, with a relatively new regulatory framework, has chosen a model that is similar to the approach in Ireland with the CER and ComReg.

Adequacy of existing mandates

We have been asked to address whether existing statutory mandates sufficiently protect both public policy objectives and consumer interests, particularly in terms of international best practice. We interpret this to mean

that we should examine whether the existing powers assigned to regulatory agencies are adequate for them to discharge their functions and whether the split of responsibilities between regulators and ministers is in line with international best practice. The latter issue again is one that is germane to all of the bodies being reviewed and thus can be addressed in this chapter. The issue of the adequacy of powers of individual regulatory bodies clearly involves a case-by-case assessment and is addressed in the individual sectoral chapters.

As pointed out earlier, the liberalisation of the energy and telecoms sectors gave rise to potential conflicts of interest between the minister's role as regulator of the industry and as owner of the dominant, incumbent operator in the industry. Transferring responsibility from the minister to an independent regulatory body was seen as a means of resolving such potential conflicts. EU directives requiring EU member states to open up their national energy and communications markets also obliged member states to establish independent regulatory agencies for those industries.

Government ministers and their departments remain responsible for the formulation of policy. This is turn requires that departments retain a degree of technical expertise in respect of regulated industries. While ministers may seek policy advice from regulators, it is important that they and their respective departments should not be dependent on regulators for policy advice as this would constrain their ability to exercise effective control over regulatory agencies.

"Departments should re-establish themselves as the focal point for issues that arise in their sector. They need to capitalise on their broad view and knowledge of their sector area by identifying trends and anticipating problems and convening actors—drawn both from their agencies as well as other stakeholders—around clusters of issues that require a joined-up approach. By fostering such networks, departments can respond to some of their own capacity limitations by drawing on outside expertise and communities of practice. As the policy experts, departments should also be responsible for identifying innovative practices as part of the performance dialogue with their agencies."[32]

Questions arise about where the line should be drawn between the minister's policy-making role and the role of the regulator in regulating the industry. In an attempt to address this issue, in the case of the CAR, the CER, ComReg and the CTR, the relevant legislation enables the minister to issue policy directions to the regulator. This power has been invoked to varying degrees. In the case of ComReg, the minister has issued 15 such policy directions—12 in 2003 and a further three in 2004. To date three policy directions have been issued to the CAR while only one has been issued by the minister to the CER. No directions have been issued to the CTR.

The policy directions issued to regulators have covered a variety of issues. For example, in the case of ComReg, the policy directions issued by the minister include:

- requiring that ComReg, when taking decisions, takes into account the state of the electronic communications industry, and in particular the industry's

[32] OECD, (2008), Ireland, Towards an Integrated Public Service, OECD Public Management Reviews, Paris, OECD, p 41.

position in the business cycle and the impact of decisions on the sustainability of the business of undertakings affected; and

- requiring that ComReg minimise its costs in carrying out its functions, consistent with best practice in other EU member states; the directions also provide that ComReg's "costs should not be out of line with the cost of regulation" in other member states.

Directions issued to the CAR include two relating primarily to the importance that the government attached to its decision on development of the infrastructure at Dublin Airport and the financial sustainability of Dublin Airport in that context.

In some cases the minister is required to engage in a consultation process before issuing any policy directions, and it is suggested that this acts as a constraint on the minister's power to issue directions to the regulator. It has also been suggested to us that the power is considerably limited since any policy directions must be couched in quite broad terms, meaning that it can be difficult, if not impossible, to establish whether the regulator has complied with them.

Whereas regulatory agencies are responsible for the discharge of specific functions assigned to them under legislation, government is responsible for the formulation of overall public policy. Thus, on occasion, it may be appropriate for the government to instruct regulators to take account of wider public policy objectives. Nevertheless, this does give rise to some potential difficulties.

In some regulated sectors, notably energy and airports, the relevant minister is the shareholder in the regulated firm and consequently the possibility for a conflict of interest remains[33]. Thus, for example, it is important to ensure that "public policy" considerations cannot be invoked or used as a pretext for requiring regulators to make decisions that are favourable to state companies. Even in those sectors where no state companies are involved, it is important that the power to issue policy directions is not used as a way of altering regulatory decisions. Similarly, any possibility that the minister could require the regulator to change the rules of the game would obviously have significant implications for regulatory credibility and commitment. We noted in Chapter 2 that regulatory credibility and commitment are important in encouraging new entry and investment. Any indication that ministers could overrule regulators' decisions on pricing would also have a serious negative effect on regulator credibility and commitment.

It would also appear that any provision that would allow the minister to overrule regulatory pricing decisions would breach EU legislative requirements. In Spain the energy regulator could make recommendations to the minister regarding price increases, but the final decision to grant any price increase lay with the minister. The failure by ministers to sanction price increases recommended by the regulator has caused electricity prices in Spain to fall relative to those in many other member states. The European Commission has,

[33] Such conflicts of interest arise in two ways. First, as shareholder the minister arguably has an interest in maximising the profitability of state companies and thus might favour the regulator setting higher prices than are otherwise justified. In the energy sector, where state companies face competition, there is an additional conflict as the minister may be seen to want the regulator to favour the state companies.

however, launched proceedings against Spain on the grounds that such arrangements are not in conformity with EU legislative requirements.

While there may be valid reasons for issuing directions to regulators requiring them to take account of wider policy considerations, this can give rise to other problems. In particular, it may result in a situation where the regulator is required to achieve a multiplicity of conflicting objectives with little or no criteria on how these should be ranked in terms of priority. For example, there may be a trade-off between imposing universal service obligations and requiring that the regulated sector operates as efficiently as possible.

Examples drawn from our comparator countries are useful in this context. In general, the ability of ministers to alter the remit of the regulator or to issue directions is greater in the Scandinavian examples and in the Netherlands. In practice, however, such powers have rarely been exercised and there are constraints on ministerial interference. As a result, regulatory independence has been largely unaffected.

In the UK the regulators' remit can only be changed through legislation. For example, the Energy Act 2004 added a new sustainability duty to Ofgem. Ofgem was established to be demonstrably independent, to ensure freedom from political interference and to avoid the creation of uncertainty in the market. A duality approach, with a principal objective and general duties shared with the minister, sought to ensure consistency of approach by the regulator and government.

The energy regulator in Australia and the telecoms regulator in New Zealand can only be subject to ministerial direction through the legislative process. In Germany, the joint energy and telecoms regulator's remit can only be changed through legislation and its decisions cannot be overruled by the minister. The minister can issue general direction and guidance, but any such intention must first be published in the *Federal Gazette* and is rare. In Spain, the energy regulator's remit can only be modified by legislative change.

Both financial regulators in Australia can be issued with directives. The Australian Securities and Investment Commission's legislation permits the minister to direct the regulator on policies and priorities but cannot direct it on individual cases. Only one such general direction has ever been given. The minister has greater power to give directions to the Australian Prudential Regulatory Authority, but must first notify the regulator of an intention to direct and must also give the chairman an adequate opportunity to discuss the issue with the ministry. This power has never been used. The aviation regulator in New Zealand may be given direction to comply with government policy.

In Norway the minister retains final approval of policy matters for the financial regulator. The regulator reported, however, that in practice it has more discretion than indicated by law and there are no examples of ministerial interference with practical supervision, although the ministry does issue an annual delegation letter that specifies guidelines and priorities for the regulator. Similarly, the Norwegian energy regulator receives an annual letter of assignment from the ministry. The ministry also acts as the appeals body and can approve or reject individual decisions. The Norwegian health and safety

authority also receives an annual letter that defines the framework for its activities for the year. Additionally, it receives regular instructions throughout the year. For the Norwegian telecoms regulator, the minister determines general policy goals, but cannot issue instruction in individual cases.

In Denmark the energy regulator has reported that it cannot generally be instructed by the ministry. However, the ministry can make changes to specific rules if it believes that the requirements of electricity legislation are not being met. This power has so far not been used. The Danish financial regulator may be asked by the ministry to examine specific matters and the ministry must also be informed about any decisions of significant social or political importance. In the Netherlands the ministry has powers to intervene if it believes the financial regulator is behaving unreasonably although the legislative process would be the normal route to change the regulator's remit, as last occurred in 2007. The Ministry may issue general directives to the Netherlands telecoms regulator, but may not intervene in individual cases.

Effectiveness and value for money

Concerns have frequently been expressed about whether the existing economic regulatory regime is working effectively and whether it provides value for money. This has been particularly true in the energy sector, and to a lesser extent in communications, and we examine the evidence in each of these sectors in the relevant sector chapters.

In this chapter of the report we describe the framework that we have adopted for analysing the issue of regulatory effectiveness and value for money. We have considered the question of effectiveness and value for money of regulatory bodies from a number of different perspectives. These can be grouped under three broad headings:

- outcomes—in terms of prices charged to consumers of the regulated product and performance such as the level of service quality and product innovation;
- operating practices—in terms of the procedures adopted by regulators, such as measures to promote competition and method of price controls, and
- cost effectiveness— are the Irish regulators discharging their duties in a cost effective manner in comparison with international best practice?

The performance of the various regulatory bodies is considered in detail under each of these headings in the various sectoral chapters of this report. At this point some more general comments about the criteria applied are appropriate.

The various economic regulators (the CAR, the CER, ComReg and the CTR) are all responsible for regulating prices to varying degrees. For example: the CAR regulates airport charges at Dublin Airport; the CER regulates gas and electricity prices to households and small businesses as well as access charges for the gas and electricity transmission systems; ComReg regulates the price of certain telecommunications services and postal services; while the CTR sets taxi fares. The object of price regulation, as noted in Chapter 3, is to ensure that regulated firms do not exploit their dominant positions by charging excessive prices. In

this respect regulation should strive to replicate the outcomes achieved in a competitive market where firms would be forced to operate as efficiently as possible. Indeed, this was explicitly recognised by the CER in a paper published in February 2004, which stated that it would "develop a regulatory approach that will, in the absence of any structural reforms, ensure a market that works well and will achieve many, if not all market benefits"[34]. Hence, another indicator of the effectiveness of regulation is whether there is any evidence of inefficiencies in regulated firms. A third indicator is the level of service quality and product innovation. Finally, in the case of communications and energy, a further indicator of regulatory effectiveness is the extent to which competition has increased in the potentially competitive segments of the market.

In Chapter 3 we described how the approach to economic regulation has changed in various countries throughout the world over the past 20 years. In particular, there has been a growing recognition of the importance of information and the limits of traditional forms of regulation because of the existence of information asymmetries and an increased awareness of the potential for regulatory capture. Therefore, in analysing the performance of Ireland's economic regulators it is important to consider the extent to which they operate in line with international best practice.

In considering the issue of value for money, we consider how costs compare between the various Irish regulatory bodies and how they compare with corresponding agencies in other jurisdictions. The international comparisons are set out in the sectoral chapters while some comparisons between the various regulatory agencies included in this study are set out below.

Summary details of trends in operating costs of the various regulatory bodies are provided in Table 3. In the case of the CER and ComReg, respectively, we identify the costs of regulating electricity and gas and communications and postal services separately. As the CTR and the Financial Regulator only began operations in 2004 it is not possible to compare trends in costs between regulatory agencies over a long period of time.

Table 3: Regulators' operating costs (€m)

	CAR	CER		ComReg		CTR	Fin. Reg.	HSA
		Electricity	Gas	Communications	Postal services			
2002	3.6	3.9	2.1	12.9				14.1
2003	4.0	6.5	3.0	12.9	0.5			14.9
2004	2.9	5.1	2.1	15.3	0.9	0.1	35.0	15.8
2005	3.7	7.7	2.1	20.7	1.0	1.7	41.3	19.2
2006	3.9	9.6	3.3	17.4	1.3	5.7	48.6	26.2
2007	4.5	11.4	3.2	17.7	1.5	8.8	52.6	27.2
% change 2004-07	**+55.3**	**+122.2**	**+56.1**	**+15.5**	**+55.5**	**+8,631.7**	**+50.1**	**+72.1**

Source: Annual Reports of the various agencies.

The Financial Regulator had the highest operating costs at almost €53m in 2007. Its operating costs were greater than the combined operating costs of €47m of the

[34] CER (2004), A Regulatory Approach to ESB Dominance, February 2004.

four economic regulators (the CAR, the CER, ComReg and the CTR) in 2007. Operating costs of the HSA in 2007 came to €27m. The different nature of these two bodies may limit the extent to which comparisons can be made between them and the four economic regulators. The combined operating costs of the CAR, the CER, ComReg and the CTR amounted to €47m in 2007. To put this in context, this is roughly eight times the operating cost of the Competition Authority. The Authority has a very different remit from the economic regulators, but it is a crucial one in terms of helping build a competitive environment and its remit does cover the whole economy. The comparison is therefore valid in setting the context for cost structures.

If we compare the four economic regulators we observe substantial differences between their operating costs. ComReg spent €18m regulating communications in 2007 compared with €1.5m on postal services. The CER's spend on electricity regulation in 2007 was more than three and a half times that on gas. Taxi regulation on its own costs almost as much as aviation, gas and postal service regulation combined (€8.8m v. €9.2m). The cost of communications regulation was 55% greater than the cost of regulating electricity.

The table also shows considerable differences in the rate of cost increase between sectors over a relatively short period of time. Thus, in the three years to 2007 the cost of electricity regulation increased by 122% while that for gas and aviation and postal regulation all increased by around 55%[35]. The cost of financial regulation increased by 41%, while health and safety regulation increased by 72%. In contrast, communications regulation increased by less than 16%.

It should be noted that the overall operating costs of the regulatory agencies in any given year may be significantly distorted by legal costs. Thus, for example, in the case of ComReg most of the drop in operating costs from €21.7m in 2005 to €18.6m in 2006 was the result of a reduction in legal costs. ComReg's legal costs in 2005 amounted to €4.5m, which exceeded the total operating costs of the CAR and CTR for that year.

Table 4: Regulators' operating costs excluding legal fees (€m)

	CAR	CER		ComReg		CTR
		Electricity	Gas	Communications	Postal services	
2004	2.8	5.0	1.9	14.9	0.9	0.1
2005	3.1	7.6	1.8	16.2	1.0	1.6
2006	3.2	8.8	3.1	16.2	1.2	5.2
2007	3.3	10.6	3.2	17.5	1.5	8.3
% change 2004-07	**+20.3**	**+112.1**	**+63.6**	**+17.5**	**+57.6**	**+8,162.3**

Source: Annual Reports of the various agencies.

Excluding legal costs makes a significant difference to the numbers in the case of some regulators. The CER's operating costs excluding legal fees for electricity regulation and to a lesser extent gas regulation increased by significantly more than those of other regulators[36]. In contrast, the CAR's operating costs excluding

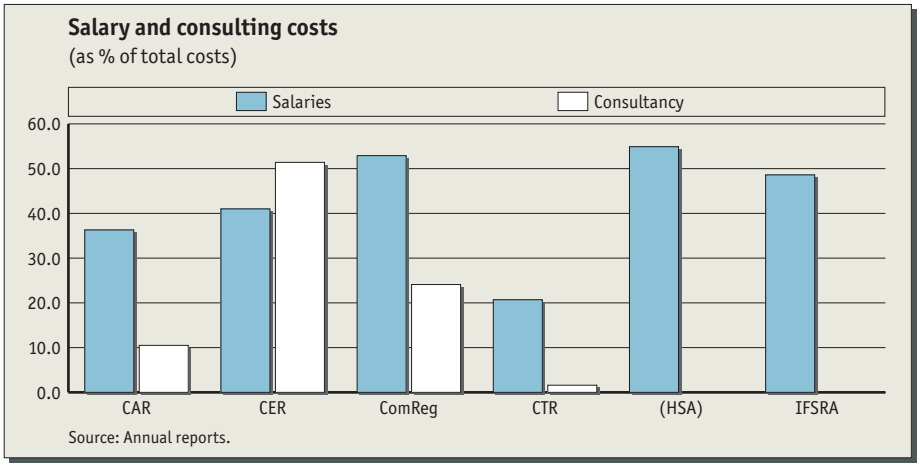
[35] The CER figures for electricity are likely to be distorted by one-off costs involved in the establishment of the Single Electricity Market (SEM).

[36] Again, work involved in establishing the SEM may explain some of the increase in electricity regulation costs.

legal costs increased by 20%, while ComReg's costs excluding legal expenses increased by 18% for communications, but by almost 58% on postal services between 2004 and 2007. While excluding legal fees reduces the cost of taxi regulation to some extent, the CTR's costs excluding legal fees exceeded the combined cost of aviation, gas and postal regulation in 2007.

The wide divergence in operating costs and the disparities in the rate of increases in operating costs may raise some questions about relative efficiency, although more detailed information would be required to confirm this.

The following chart shows salaries and consultancy costs as a proportion of operating costs for each of the agencies in 2007.



There is a wide divergence in the proportion of costs accounted for by salaries across the various regulatory bodies. Salaries range from 22% of total operating costs in the CTR to 55% in the HSA. In the case of communications, salaries accounted for 54% of total costs compared with 39% for electricity and 36% for aviation. Such figures must be treated with some caution. For example, some agencies had considerable outlays on consultants and thus their salary costs might have been reduced as a result. In 2007 almost 60% of the cost of electricity regulation was accounted for by spending on consultants. This compares with 20% for communications and 10% for the CAR. Consultancy costs accounted for less than 2% of expenditure by the CTR.

The Financial Regulator and HSA accounts do not identify expenditure on consultancy services. As noted, of the agencies examined, the HSA had the highest proportion of expenditure accounted for by payroll costs. In the case of the Financial Regulator, it shares a number of administrative and overhead functions with the Central Bank and Financial Services Authority of Ireland (CBFSAI) and it pays a contribution towards such costs. In effect this means that salaries for such functions that are part of the cost of the Financial Regulator's regulatory activities are not included in its salary cost and are not separately identified.

Table 5: Regulators' operating costs per employee (€)

	CAR	CER		ComReg		CTR	Fin. Reg.	HSA
		Electricity	Gas	Communications	Postal services			
2004	171,579	160,607	171,905	147,404	186,600		117,384	96,103
2005	207,958	227,331	172,113	211,010	173,500	151,137	129,903	115,642
2006	192,809	203,467	204,165	170,108	212,500	178,194	147,605	135,971
2007	215,763	278,543	178,843	170,231	241,833	178,037	153,150	137,500
% change 2004-07	**+25.8**	**+73.4**	**+4.0**	**+15.5**	**+29.6**	**n/a**	**+30.5**	**+43.1**

Source: Annual Reports of the various agencies.

Table 5 shows a considerable variation in costs per employee, with costs per person of €278,543 in electricity regulation for 2007, which was more than double those of the HSA. Costs per person at the Financial Regulator were second-lowest at €153,150[37]. Interestingly, there are also significant variations in costs per employee between sectors that are regulated by the same agency, ie, gas versus electricity and communications versus postal services. The table also shows significant variations in the rate of increase in cost per employee. The highest rate of increase occurred in electricity, which rose by 73% over three years compared with an increase of just 4% in gas[38].

Table 6: Regulators' operating costs per employee excluding legal fees (€)

	CAR	CER		ComReg		CTR	Fin. Reg.	HSA
		Electricity	Gas	Communications	Postal services			
2004	161,904	156,386	160,675	143,462	184,000		117,384	96,103
2005	173,137	222,792	154,040	165,745	171,000	142,557	129,903	115,642
2006	160,502	187,636	190,955	158,431	208,167	161,293	147,605	135,971
2007	157,685	258,920	175,279	168,615	241,667	168,465	153,160	137,500
% change 2004-07	**-2.6**	**+65.6**	**+9.1**	**+17.5**	**+31.3**	**n/a**	**+30.5**	**+43.1**

Source: Annual Reports of the various agencies.

The results in table 6 also show substantial variations. Costs per employee excluding legal fees in electricity regulation were €258,920 in 2007. In contrast, costs per employee in the HSA were €137,500 in 2007. Again, there is a significant difference in costs per employee between electricity and gas and between communications and postal services, despite these functions coming under the same regulatory body in each case.

In table 7 a substantial difference can be seen between agencies and within agencies. Average payroll costs in 2007 range from just over €50,000 in the CTR to almost €92,000 in electricity regulation. Average payroll per employee in postal services in 2007 was more than €86,000, compared with €89,000 for communications. In the case of the CER, average payroll costs for electricity regulation were 10% higher than for gas regulation. These issues are considered further in the sectoral chapters.

[37] The Financial Regulator figures are probably overstated as the total cost figure includes its contribution to shared overheads of the CBFSAI, which includes some staff costs, but those staff are not included in the Financial Regulator employment figures.

[38] The increase in the case of electricity can be explained at least in part by the costs of establishing the SEM.

Table 7: Average payroll costs per employee in regulatory bodies (€)

	CAR	CER		ComReg		CTR	Fin. Reg.	HSA
		Electricity	Gas	Communications	Postal Services			
2004	77,982	69,343	78,025	70,260	96,000		62,198	54,145
2005	66,148	83,929	89,030	83,041	96,833	38,308	67,726	
2006	75,511	74,325	81,751	89,588	119,333	56,224	76,301	73,989
2007	78,401	91,837	83,149	89,442	86,167	50,218	79,138	75,767
% change 2004-07	**+0.5**	**+32.4**	**+6.6**	**+27.3**	**-10.2**	**n/a**	**+27.2**	**+39.9**

Source: Annual Reports of the various agencies. Figures for the CTR provided by the CTR.

Accountability

Independent sectoral regulators should be accountable for the discharge of their remit and their overall performance. Effective regulatory accountability is important for a number of reasons.

- In many cases regulators have been delegated responsibility for functions previously undertaken by ministers. The interests of democracy demand that such delegation of responsibility be accompanied by clear and defined accountability mechanisms.
- The decisions of regulatory bodies, particularly in areas such as energy and telecoms, have major implications for competitiveness and thus for Ireland's overall economic performance. The fact that inefficient regulation imposes significant costs on the economy requires that regulators must be accountable both for specific decisions and for their overall strategy.
- Regulators are themselves monopolies and as with all bureaucratic organisations have a natural tendency to seek to expand their organisation and the scope of their activities. Effective mechanisms are therefore required to curb such tendencies.
- Regulators are responsible for the expenditure of significant sums of public money. As in all cases involving the expenditure of public money, proper accountability is required[39].
- Measures are required to prevent abuses of power by regulatory bodies.
- Regulatory accountability mechanisms therefore need to address a variety of issues. In addition, while accountability mechanisms should be designed so that regulators are required to give full account of the discharge of their duties, at the same time such mechanisms should be designed to ensure that their regulatory independence is not compromised in the process.

"In practice, the accountability of regulators needs to be balanced against their independence. Regulators have been established as independent entities in order to ensure that regulatory decisions are taken in an objective manner."[40]

[39] In some cases regulators are funded exclusively through levies on the industry. In a sense these represent a form of taxation. The fact that the regulator is allowed to recoup its running costs from the industry does not lessen the need for proper accountability in terms of how this money is spent.

Ensuring regulatory accountability is far from easy. "*...the welter of information that the public receives about political issues from the media and the difficulties of organising to achieve political ends insulate regulators from monitoring and general-interest pressures.*"[41]

In addition, as the regulatory framework is constantly evolving, it is necessary to ensure that proper lines of accountability are maintained. There are a number of possible ways in which regulatory bodies can be held to account including:

- publication requirements;
- government accountability;
- parliamentary accountability;
- judicial review;
- appeals; and
- advisory/consultative panels.

Existing arrangements for regulatory accountability include all of these types of accountability mechanisms to varying degrees. Nevertheless, there appears to be some concern about whether current accountability arrangements are effective. The government's white paper on better regulation, for example, stated that:

"*Regulators and regulated bodies alike have indicated that they are conscious that the question of 'who regulates the regulator?' is not always adequately addressed by the existing systems in place.*"[42]

The paper also declared that:

"*We will strengthen accountability in the regulatory process. Regulators and enforcement agencies should be clearly accountable to citizens, through the Houses of the Oireachtas and government.*"[43]

In order to address the effectiveness of existing arrangements and the potential need for change, we consider the extent to which existing arrangements are adequate to address the needs for regulatory accountability outlined above.

Publication requirements

The provision by regulators of detailed information, including full disclosure of the details of the decision-making process and of all submissions and representations made to the regulator, can assist in the accountability process. In general, sectoral regulators in Ireland have largely adopted such practices with regard to information dissemination. To the extent that the reasoning behind regulatory decisions is made public, it can promote greater

[40] *Regulating Better*, p 31.

[41] M Levine, (1998), Regulatory Capture, in J Eatwell, M Milgate and P Newman eds., *The New Palgrave – A Dictionary of Economics,* Basingstoke, Macmillan.

[42] *Regulating Better*, p 30.

[43] *Regulating Better*, p 10.

understanding of the issues and may contribute to the acceptance of such decisions. Many regulatory decisions simply summarise submissions of various parties and set out conclusions, which is insufficient and lacks transparency. UK regulators have been criticised for a lack of clarity in published decisions[44]. To outside observers, the published decisions of regulators do not always provide a "crystal-clear guide to what really went on, what was really decided, and what, in apparently similar circumstances, might be decided in the future"[45].

An even more serious criticism is that this type of regulatory process, ie, publishing consultation documents, inviting written responses and then issuing decisions, effectively excludes consumers.

"The decision to establish a decision-making process that, to all intents and purposes, excluded consumers from participation, relied on the very English notion that responsible chaps know what is best for the public."[46]

Some of the Irish regulators arguably display similar deficiencies.

"The Commission for Energy Regulation, the sectoral regulator for the industry, publishes in the region of 300 papers and documents per year on the subject, the vast majority concerned with electricity. Although the Commission consults on many of these documents, it receives barely a response from outside of the industry circle. The result is a general disquiet but also a lack of engagement in policy development, which has the potential to create an outsider/insider perspective."[47]

Similarly, Chisholm suggests that regulators "have to represent in the mix the interests of consumers who are rarely in a position to submit responses to generally quite complex issues"[48].

A theme that emerged frequently in the course of our discussions with regulatory agencies themselves was that they tended to have a lot of interaction with the regulated industry and regulated firms. Similarly, large organisations such as the Irish Business and Employers Confederation (IBEC) also tended to interact with the regulator. Smaller firms, consumer bodies and individual consumers tended to have little input into regulators' consultation processes.

The lack of effective consumer participation has two serious drawbacks:

- it severely limits the range of inputs available to the regulator, creating a reliance on inputs from the regulated firms; and
- it denies regulators' decisions the credibility that a more transparent system can provide[49].

[44] I Stelzer, Lessons for UK Regulation from recent US Experience in I Stelzer (2000), *Lectures on Regulatory and Competition Policy,* London Institute for Economic Affairs, p 122.

[45] I Stelzer, Lessons for UK Regulation from recent US Experience in I Stelzer (2000), *Lectures on Regulatory and Competition Policy,* London Institute for Economic Affairs, p 103.

[46] I Stelzer, Lessons for UK Regulation from recent US Experience in I Stelzer (2000), *Lectures on Regulatory and Competition Policy,* London Institute for Economic Affairs, p 105.

[47] B Thompson (2007), *Electricity Competition in Ireland – More Heat than Light?,* DEW, Annual Economics Policy Conference, mimeo.

[48] Chisholm, (2008), p 48. The author is a ComReg commissioner.

The regulatory process is in contrast with the planning system, where planning appeals involve public hearings. Open procedures add credibility to the result and give regulators access to varying points of view. Increasing consumer participation in the regulatory decision-making process would also increase accountability.

"Consultation and participation efforts could also be improved through greater clarity and transparency, ie, who is consulted and how is their input used? This does not necessarily mean that everything must be taken on board, but it does mean that participants should be able to hear back from Public Service bodies that their views have been heard and understood. The Public Service can achieve this by integrating a quality consumer service perspective into policy formulation and development."[50]

Such views are as relevant to regulators as to other public agencies.

To the extent that publication of information permits a form of external peer review of regulatory decisions by outside commentators, it may assist in identifying inefficient regulatory decisions. In this way, it can contribute to critical media and political evaluation both of individual decisions and of overall regulatory performance.

Publishing as much information as possible in relation to regulatory decisions and the reasons for them falls someway short of the required level of accountability. Such measures only permit a relatively weak level of accountability. Critical comment based on such information might encourage a regulatory body to "raise its game", but by itself would not provide any effective mechanism for addressing poor regulatory performance. This sort of informal external peer review of regulatory decisions may assist in identifying inefficient regulatory decisions and might give rise to some pressure on the regulator to alter such decisions. The regulator could simply choose to ignore such criticisms. These kinds of mechanisms are totally inadequate given the substantial adverse costs of incorrect regulatory decisions.

Regulators currently come under the umbrella of the Freedom of Information Act (FIA), which requires them to keep records for public scrutiny. The ability of the media and others to access information on regulatory activities under the FIA represents another mechanism by which regulators can be held to account, although arguably, as with the publication provisions described above, by themselves such provisions are relatively weak.

Government accountability

Regulators are accountable to government through being:

- appointed by ministers (after an independent selection process); and
- required to work within a policy framework set by the minister and to report to the minister on their strategy and work by producing strategy statements, work programmes and annual reports.

[49] Stelzer, (2000).

[50] OECD, (2008), p 37.

Table 8: Provisions regarding appointments to regulatory bodies

	CAR	CER	ComReg	CTR	Fin. Reg.	HSA
Appointing authority	Minister	Minister	Minister	Minister	Authority—6-8 ordinary members appointed by minister of finance after consultation with minister for enterprise, trade and employment. CEO and consumer director appointed by authority subject to approval of minister of finance	Minister Chairperson and 11 part-time board members. Three each nominated by IBEC and Irish Congress of Trade Unions
Appointment requirements	Must be recruited through competition run by civil service & local appointments commission No qualification requirements	None	Must be recruited through competition run by civil service & local appointments commission No qualification requirements	Must be recruited through competition run by civil service & local appointments commission No qualification requirements	Open competition	None
Period of appointment	3-5 years	3-7 years	3-5 years	3-5 years	5 Years	3 years for board members and chairperson. No limit set for CEO
Possibility of reappointment	Yes: 2-term limit subject to 10-year maximum	Yes: 2-term limit subject to 10-year maximum	Yes: 2-term limit	Yes: 2-term limit subject to 10-year maximum	Yes	Yes: subject to 2-term limit
Potential to remove member	Yes: because of incapacity or for stated misbehaviour; requirement to lay statement of reasons before both houses	Yes: because of incapacity or for stated misbehaviour	Yes: because of incapacity or for stated misbehaviour; requirement to lay statement of reasons before both houses	Yes : because of incapacity or for stated misbehaviour; requirement to lay statement of reasons before the Dail	Yes: board may remove CEO but must provide CEO with written reasons.	CEO—Yes: incapacity or for stated misbehaviour; requirement to lay statement of reasons before both houses. Authority may also remove member with the consent of the minister
Restriction on regulator taking up position with regulated firm on leaving office	Yes, for 12 months after leaving office	Yes, for 12 months after leaving office	Yes, for 12 months after leaving office	Yes, for 12 months after leaving office		

"The processes of selecting, appointing (including reappointing) and removing regulators must strike a delicate balance between ensuring the accountability of regulatory authorities and their independence."[51]

[51] DPE, (2000), p 13.

Appointments procedures should ensure that persons with the requisite expertise and/or experience are selected to be regulators. It is important that they be afforded sufficient security of tenure to diminish the possibility of their being subject to undue pressures. At the same time, their tenure should be dependent on their continued suitability for office. The normal period of office for a regulator should be of sufficient length to ensure continuity of approach, without being so long as to stem the flow of fresh thinking. Procedures regarding reappointment should ensure the independence of the regulators and guard against the perception of "capture" by the (re)appointing authority. Accountability also requires that it must be possible for a regulator to be removed from office should the need arise, but the independence of the regulatory authority requires that such a removal involve a special and transparent procedure. Finally, there needs to be restrictions on regulators taking up positions with regulated firms on leaving office to guard against possible conflicts of interest.

Regulatory agencies are currently accountable to government through being required to work within a policy framework set by the minister and to report to the minister on their strategy and work. Such arrangements are designed to ensure a degree of democratic accountability. They can also enable ministers to exercise a degree of supervision over how the regulator discharges its functions and spends public money. Thus, such accountability arrangements may represent an important mechanism for ensuring that regulatory bodies operate efficiently and carry out their mandate effectively. Obviously there is a risk that such political accountability may call the regulator's independence and credibility into question, particularly if the minister is also the shareholder in the regulated firm. Thus, achieving the correct balance between regulatory independence and ministerial accountability is a difficult challenge. As previously outlined, it would appear inappropriate for regulators to be accountable to ministers with regard to specific decisions.

The agencies we have examined produce strategy statements, annual work plans and annual reports that are provided to the relevant minister. This can contribute to improved accountability although the extent of this will depend on the quality of such documents. The OECD has highlighted the absence of performance measures that focus on outcomes as a serious shortcoming throughout the Irish public service. Government departments are required to produce output statements and a similar requirement could be imposed on regulators.

Questions have been raised about the capacity of ministers and government departments effectively to oversee the activities of regulators because of information asymmetries that favour the regulator. The recent OECD report on the Irish public service, for example, stated that government departments needed to strengthen their capacity to monitor agencies.

"Departments also have a greater role to play in promoting agency performance. The traditional input-focused dialogue between agencies, departments and the Department of Finance should be replaced by a formal long-term performance dialogue, which entails a process of setting different types of targets and evaluation, and making links between inputs, processes, outputs and outcomes. This involves

supporting departments and other government bodies in the difficult task of developing measurable indicators, collecting data on them, making commitments to improvements and then being accountable for those gains. The immediate benefit will be greater understanding, consensus and experience about what is meant by managing performance. International models for building performance focus include reforms introduced by UK and the Netherlands."[52]

This in turn requires the development of performance measures based on achieving outputs and outcomes rather than compliance with processes. Statements of activity do not equate with measures of effectiveness.

There are also issues with building the capacity of line departments and agencies. In developing performance measures, departments depend on agencies for information. Therefore, like the Department of Finance, they need the capacity to understand and evaluate the information they receive if they are to make judgments as to how realistic proposed targets are, or as to the quality of the performance measures and data. Even if the interest is there, departments and agencies in some cases do not have the expertise or knowledge to develop performance measures or even effectively monitor performance. This can lead to the passive provision of data that has no real weight in the decision-making process. Building up skills at this level is essential for successful application of the guidelines on several of the performance initiatives.[53]

Parliamentary accountability

Accountability to the Oireachtas (the Irish parliament) represents another mechanism for holding regulators to account. Current arrangements require regulators to present annual reports and appear before relevant Oireachtas committees when requested. In addition, the accounts of regulatory agencies are audited by the Comptroller and Auditor-General who, in turn, reports to the Public Accounts Committee of Dail Eireann (the Irish House of Representatives). Furthermore, a new Oireachtas Committee on Economic and Regulatory Affairs was established in 2007.

Accountability to the Oireachtas might be seen as posing less of a threat to regulatory independence than ministerial accountability. Questions arise, however, about whether existing arrangements for holding regulators accountable to the Oireachtas are adequate.

J Westrup found that Oireachtas committees had failed to properly oversee the activities of regulatory bodies[54]. He observed that "the Oireachtas has shown little enthusiasm for carrying out its scrutiny role" and explained that "the apparent unwillingness of different Oireachtas committees to meet with the different regulators on even an annual basis is an indication of a reluctance to take seriously a scrutiny role". While such criticisms may be unduly harsh, the ability of Oireachtas committees effectively to hold regulators to account appears to be limited because they lack the necessary specialist knowledge to do so. Our discussions with stakeholders indicated that Oireachtas committees

[52] OECD, (2008), p 32.

[53] OECD, (2008), p 158.

[54] J Westrup, (2002), *Financial Services Regulation in Ireland: The Accountability Dimension*, Studies in Public Policy 10, The Policy Institute, Trinity College Dublin, p 55.

currently lack the resources and expertise to exercise effective accountability over regulatory agencies. Indeed, several members of different Oireachtas committees indicated that they believed that they lacked the necessary resources and support effectively to hold regulators to account. Such lack of knowledge and expertise can be overcome. For example, we have seen examples most notably in the UK of how parliamentary committees with adequate support staff can hold regulatory bodies to account. We note that the government's white paper on better regulation stated that:

"The resources of the Oireachtas and its committees for reviewing sectoral regulatory structures must be commensurate with their monitoring and accountability functions. In addition, there is a need for greater clarity and consistency when regulatory bodies are being established, as to how they relate to the Oireachtas, balancing autonomy in making regulatory decisions and their political accountability."[55]

The OECD questioned the capacity of Oireachtas committees to effectively hold public agencies to account, noting that they did not have the capacity in terms of staff or expertise to evaluate performance information. It also noted that there was considerable variation in the sitting days of committees and their ability to exercise an oversight role[56].

Judicial review

Regulators are accountable through the courts by being subject to a judicial review of their decision processes and they may also be subject to other appeals or review mechanisms in relation to their decisions.

Judicial review is essentially concerned with assessing whether or not the regulator followed due process and adopted fair procedures in reaching a decision. It thus acts as a check on possible abuses of power by regulatory bodies. It is not concerned with analysing the relative merits or otherwise of the decision. In other words, judicial review does not allow for a full review of decisions on the merits. Rather, the courts have tended to apply a degree of deference in judicial review cases, recognising the implicit expertise of the regulatory body, and are therefore generally reluctant to substitute their own view in place of a decision by a regulatory agency. Arguably there are good jurisprudential reasons for the courts adopting such an approach. In practice, however, this has come to mean that, in judicial review proceedings, the bar for overturning a regulatory decision has been set extremely high.

"To be reviewably irrational, it is not sufficient that a decision-maker goes wrong or even hopelessly and fundamentally wrong: he must have gone completely and inexplicably mad; taken leave of his senses and come to an absurd conclusion. It is only when this last situation arises or something akin to it that a court will review the decision for irrationality."[57]

Judicial review can also be a costly and time-consuming process and may delay the emergence of new competitors. For example, the entry to the market of a

[55] *Regulating Better*, p 30.

[56] OECD, (2008).

[57] Aer Rianta CPT versus The Commissioner for Aviation Regulation & Ors. High Court, J O'Sullivan, January 16th 2003.

third mobile-phone operator, Meteor, was considerably delayed as a result of a judicial review of the regulator's decision to award it the third mobile operator's licence. Regulatory appeals have also placed a considerable burden on the courts system. In a number of cases, judges have been asked by complainants to substitute their opinion for the decision of the regulator, even though this is beyond the scope of a judicial review.

Ways of reducing delays in judicial review proceedings were considered in the white paper, *Regulating Better*. This noted, for example, that a small number of judges have been appointed to deal with competition cases in accordance with the 2002 Competition Act and suggests that there is a need to consider whether further specialisation should be supported in relation to regulatory cases, because of the growing complexity of the issues involved. The white paper noted that it might also be possible to improve processes through better case management, including allocation of cases, limitation of opportunities for submissions and presentations on points of law so that delay could be reduced through more efficient administration of cases[58].

A fast-track process has been established in the Commercial Court. Judicial reviews of regulatory decisions can be dealt with under this process where they have significant commercial impact, but at the discretion of the Court. Thus a mechanism exists for judicial reviews of regulatory decisions to be dealt with speedily, although the more cases that fall to be dealt with under this procedure, the more difficult it will be to handle them quickly. The Competition Act, 2002, seeks to provide for a speedy mechanism to deal with appeals against decisions of the Competition Authority prohibiting a merger, recognising the need for a quick resolution in such cases. The Act thus provides that the High Court should hear and determine such appeals within two months in so far as is practicable. To date, only one such appeal has arisen, but the two-month time limit has not been met in that case, which is currently ongoing.

Judicial review acts as a constraint on the regulator abusing its powers, which in itself represents an important accountability mechanism. It does not, however, provide an effective constraint on regulators making wrong decisions, as the courts are not prepared to second-guess regulatory bodies[59].

Regulatory appeals

An effective appeals mechanism can provide an important check against incorrect regulatory decision making. The fact that decisions may be appealed against and re-examined increases the incentive for the regulatory body to ensure that its decisions are robust and well argued. Currently there are significant divergences in the types of appeals mechanisms that apply in the case of various regulatory bodies. The situation with respect to appeals is summarised in Table 9.

[58] *Regulating Better*.

[59] As pointed out in Chapter 3, the existence of information asymmetries and the threat of regulatory capture mean that the regulatory process is prone to serious risks of error, which can impose significant costs on the economy.

Table 9: Existing regulatory appeals provisions

CAR	Parties may ask the minister to establish an appeals panel for determinations relating to airport charges or air navigation charges for terminal services. Appeals panel can refer issues back to the Commission, but cannot substitute its decision for the determination of the Commission.
CER	Minister can establish an appeal panel to hear and determine an appeal against a decision: • refusing a licence, authorisation or consent; • a modification; or a refusal to modify a licence or give authorisation or consent.
ComReg	Affected party may appeal to the High Court.
CTR	A party refused a licence may appeal to the District Court.
Financial Regulator	Certain decisions may be appealed against to the Irish Financial Services Appeals Tribunal. Whether a decision is appealable against is defined in the relevant piece of legislation from which the decision derives, ie, depending on whether it is a banking, insurance or investment matter. Administrative sanction decisions may be affirmed, varied, substituted, remitted or set aside. Supervisory decisions may only be remitted or confirmed. A decision of the Tribunal may be appealed against to the High Court
HSA	• A person on whom an improvement notice is served may appeal to the District Court within 14 days and the judge can confirm, vary or cancel the notice; • A person on whom a prohibition notice has been served and who has appealed against the notice can apply to the Court to have its operation suspended until the appeal is disposed of; • An appeal can be made to the District Court within seven days by a person served with a notice and the judge can confirm, vary or cancel the notice and if confirmed, can suspend the operation of the notice for a set time; • Any person aggrieved by a District Court Order determining a complaint under the bill may appeal to the Circuit Court and the decision of the judge of the Circuit Court is final and conclusive; and • The minister may prescribe any work activity to which the provisions of the act apply as being an activity that may not be carried on except in accordance with the terms or conditions of a licence issued by the HSA or a person prescribed under the Act. A licence applicant may appeal against a licence decision to the High Court within ten days of receipt of the certificate or such further time as the High Court may allow.

Currently there are only limited provisions for appeals against regulatory decisions, other than by way of judicial review. In the case of ComReg and the HSA, appeals are through the courts. In the case of the CAR, the CER and the Financial Regulator there is provision in the legislation for certain decisions to be appealed against by means of an appeals panel. In the case of ComReg, an appeals panel mechanism was introduced and subsequently scrapped within a relatively short period of time[60].

As the table illustrates, there are wide variations in the types of decisions by the different regulators that can be appealed against. In the case of the economic regulators there is no provision for an appeal by customers against pricing decisions except in the case of the aviation regulator.

The government's *Regulating Better* white paper contained a number of commitments with regard to regulatory appeals:

"We will improve appeals procedures. There should be well-publicised, accessible and equitable appeals procedures that balance rights of appeal with the need for speedy action, in a fair manner. Where regulatory decisions are referred to the courts, there are particular requirements of speed and expertise."[61]

The proposals on regulatory appeals were further expanded on in the white paper, which stated that:

[60] This is described in more detail in Chapter 8, Telecommunications.

[61] *Regulating Better*, p 10.

"In the case of utilities regulators, one possibility might be to establish a single regulatory appeals body. Such an appeals body could call on a number of expert panellists with relevant knowledge and experience of sector-specific issues and/or competition law and policy, and/or economics, to adjudicate appeals. The regulatory appeals panel might facilitate a more expedient and cost-effective alternative to judicial review. Access to further court appeals would remain an option, but only on points of law. Powers of the single regulatory appeals body might include:

- *confirming or setting aside all or part of the regulator's decision;*
- *imposing, revoking or varying the amount of any penalty;*
- *granting or cancelling an individual exemption or varying any condition or obligation that relates to that exemption;*
- *giving such directions, or taking such other steps as the sectoral regulator could have given or taken; and*
- *making any other decision that the sectoral regulator could have made."*

The white paper acknowledged that there were challenges associated with establishing a regulatory appeals body. First, the right of appeal to the courts would still remain, as the courts can always review any administrative decision. Thus, the only effect of having a formalised appeals procedure may be to delay the final decision further. Second, the appeals procedures themselves may be used intentionally to delay a final decision, to protect the benefits accruing to the incumbent or dominant producer in the sector[62].

"If accountability is to be fully established, an innovative approach to regulatory appeals should be adopted to facilitate expedient, efficient and informed review of regulatory decisions. Ideally, the parties undertaking the review would have expertise in relevant areas, eg, competition law, economics and sector-specific issues, or direct access to such expertise. However, we must see to get the correct balance between the right to appeal a regulatory decision and undue delay in decision making and implementation. There are, therefore, a number of complex issues involved in establishing an efficient appeals procedure. The government is committed to reviewing the options available, in consultation with interested parties, and developing proposals for an improved approach."[63]

It is sometimes suggested that an appeals body would become the *de facto* regulator and that parties would not engage in the initial regulatory decision-making process, but preserve their ammunition for an appeal. Firms generally tend to want such issues decided speedily and it is not in their interests to act in such a fashion. In order to discourage vexatious appeals, appellants could be required to bear the cost of unsuccessful appeals.

[62] A number of submissions advocated the establishment of an appeals panel. See, for example, Irish Congress of Trade Unions, (1999), Governance and Accountability Arrangements in the Regulatory Process.

[63] Regulating Better, p 38.

Consumer panels

Regulating Better also referred to a potential role for consumer panels in improving regulatory accountability.

"*Accountability can also be strengthened through greater involvement of the consumer. The consultative processes in which the regulators engage would be strengthened by informed and well-researched submission and comment from sectoral consumer councils, user groups and business interests, as well as households, communities and disadvantaged groups. Where existing industry levies are collected, consideration will be given to using resources generated by these levies to support consumer councils and user groups.*"[64]

The two consultative panels in the case of the Financial Regulator have an important role in improving regulatory accountability. As pointed out previously, these panels have an advisory role to the minister in terms of approving the Financial Regulator's budget for the year ahead. Such arrangements can provide a mechanism to help ensure cost effectiveness. The Financial Regulator panels also have some resources to commission relevant research. Certainly such resources would seem to be required to support the provision of "informed and well-researched submission and comment" as suggested by the white paper.

Conclusions on accountability

Our views on accountability are as follows.

- Democratic accountability operates through accountability to ministers and to the Oireachtas. The practice adopted by regulators of publishing extensive amounts of information about their activities and decisions also promotes accountability through increasing transparency.
- Nevertheless, there appear to be certain weaknesses. It is unclear, for example, that government departments have sufficient knowledge and expertise to hold regulators to account, while there is a general consensus that Oireachtas committees require additional resources in order properly to hold regulators to account. The weaknesses in the accountability of the government/Oireachtas raise questions about their ability to prevent regulatory expansion.
- The roles of the Comptroller and Auditor-General, the Public Accounts Committee and the Committee on Economic Regulatory Affairs provide for a degree of accountability over regulators' spending of public money. The Financial Regulator's consultative panels have been useful in promoting budgetary discipline and this model might be applicable to other regulators.
- There is little accountability for incorrect regulatory decisions. Arguably, accountability for specific decisions should not be to the minister and/or Oireachtas as this would raise questions about regulatory independence and credibility. Incorrect regulatory decisions are costly to the Irish economy. Thus an effective appeals mechanism is an important check against regulatory errors. While this undoubtedly involves some delay and some possible cost (assuming the regulator's decision is upheld) such costs are short term in contrast to the

[64] *Regulating Better*, p 31.

costs of regulatory errors, which are likely to have a much longer-lasting impact. It also appears that courts are not well equipped to review individual regulatory decisions on their merits. This suggests that an independent specialist appeals body is required to deal with regulatory appeals.

Potential for restructuring

In 2000 the DPE considered three possible levels at which regulation could occur:

- industry-level regulation, where a separate regulatory body is established for each industry;
- sectoral-level regulation, where the remit of a sectoral regulator spans several industries in the same or converging sectors; and
- overall utility regulation, where a general utility regulator would have responsibility for overseeing the operation of all utility markets.

The report concluded that in circumstances where there are competing or complementary industries (eg, electricity and gas), industry-level regulation could be sub-optimal if it failed to take account of the totality of a particular market. Conversely, in conditions where the regulatory environment is changing rapidly, supra-sectoral regulation could result in a cumbersome regulatory structure spanning many markets, regardless of the compatibility of the industries involved, of their respective stages of evolution in the liberalisation process, or of their unique regulatory requirements.

A report by The Enterprise Strategy Group for the minister for enterprise and employment raised the issue of the proliferation, cost and lifespan of regulators[65]. The report called for the merging of existing regulators for networked sectors into a new multi-sectoral regulatory body.

Tuohy noted that the preferred option at that time was for regulation at the sectoral level, as it allowed for an approach focused on the particular circumstances of the various markets while also taking into account the competition/complementarity between industries operating (or potentially operating) in the same market. He suggested that as markets developed, the justification for detailed sectoral regulation may diminish and that this could enable the question of a supra-sectoral regulating authority to be examined at a future date, in the context of dealing with residual regulatory functions across the various sectors and achieving synergies.

Regulating Better reopened the issue about the appropriate number of regulatory agencies. It indicated that in the context of regulation, the "necessity" principle requires that regulatory policies and tools are deployed only when required and that the need for particular regulatory institutions is kept under regular review. Such ongoing review of the regulatory framework can help to

[65] Ahead of the Curve–Ireland's Place in the Global Economy, Dublin, Forfas 2004.

ensure that the range of regulatory institutions is optimal and that the accountability mechanisms are comprehensive. It therefore proposed to:

- *(a) "create new sectoral regulators only if the case for a new regulator can be clearly demonstrated in light of existing structures [Action 4.2.1]; and*
- *(b) "assess the possibilities for rationalisation of sectoral regulators including through the merger of existing regulators and/or through the sharing of common services [Action 4.2.2]".*

It further provided that integration of regulatory activity may be strengthened by a sharing of resources, especially in generic areas such as financial management, administration, human-resource management, data systems and legal services.

It is important to note that since this review was commissioned, the merger of the Competition Authority with the NCA and the incorporation of the CTR within the new Dublin Transport Authority were announced in the 2009 Irish government budget.

5. The international dimension

Introduction

A core element of the review has been to compare the regulatory environment in Ireland with that in a number of other countries. The geographic and sectoral coverage of the international benchmarking is summarised in table 10, below.

Table 10: Comparator countries and sectors

Country	Financial services	Energy	Telecommunications	Transport	Health and safety
Australia	●	●	●		
Denmark	●	●	●	●	●
France				●	
Germany	●	●	●		●
Luxembourg	●				
Netherlands	●	●	●		
Norway	●	●	●	●	●
Portugal		●			
Spain	●	●			
UK	●	●	●	●	●
New Zealand			●	●	●

In determining the countries selected for comparison, we aimed to choose a grouping that would cover a number of selection criteria:

- comparable with Ireland in terms of economic scale and performance;
- similar jurisdiction and legislative environments to Ireland, especially from within the EU;
- reputed to have an effective regulatory approach and structure;
- sufficient scale and experience from which to draw robust data and trends; and
- experience of innovative approaches to regulation, in terms of possible options for Ireland.

This chapter presents some background on the overall business and regulatory environment in the comparator countries. It helps to describe the national context and policy approach in which economic regulation has evolved in each of the countries selected. Table 11 shows how the countries have performed in two recent independent benchmarking studies of the business environment.

Table 11: Business environment rankings

Country	World Bank 2009	World Bank 2008	EIU overall 2009-13	EIU overall 2004-08	EIU private investment 2009-13	EIU private investment 2004-08
Ireland	7	7	12	9	4	7
Australia	9	10	7	13	4	7
Denmark	5	5	3	2	1	1
France	31	32	19	18	17	18
Germany	25	20	13	15	12	12
Luxembourg	50	45	-	-	-	-
Netherlands	26	27	8	8	4	4
New Zealand	2	2	14	12	12	12
Norway	10	9	16	16	17	19
Portugal	48	43	33	33	17	23
Spain	49	46	23	22	26	21
UK	6	6	11	10	1	1

Sources: World Bank Group, Doing Business 2009, September 2008; Economist Intelligence Unit, Business Environment Rankings, September 2008.

The World Bank's Doing Business index benchmarks business regulations and their enforcement in 181 economies. It uses ten indicators, covering factors such as the time and cost of starting, operating and closing a business, trading across borders and making tax payments. It does not cover the economic regulatory environment as defined in this review, as it is more concerned with the operational practicalities of establishing and running a business. However, it does provide an indication of the overall regulatory context and how supportive or otherwise it is of business development and growth. The latest rankings show Ireland faring well, in seventh place out of the 181 economies covered. Of the comparator countries only New Zealand, Denmark and the UK are in higher positions. The 2008 rankings are shown for comparison and indicate a stable position among these higher-rated countries—Ireland, the UK, Denmark and New Zealand have all retained their positions. Germany, Luxembourg, Norway, Spain and Portugal have all lost some ground, while Australia, France and the Netherlands have improved marginally.

The rest of the table presents the findings from the Economist Intelligence Unit's Business Environment Rankings. These rank 82 countries (not including Luxembourg), using ten indicators. In this index, the indicators cover more macro-level factors such as the political environment, economic and market conditions, foreign investment and trade policy, taxation and infrastructure. It also includes a specific indicator of policy towards private investment, in which regulatory policy is one of the factors measured. The rankings are therefore more related to the wider economic and fiscal policy context, as well as including specific reference to the regulatory environment. The table presents four extracts from the most recent rankings: the overall assessment of the business environment over the 2004-08 period; the outlook for 2009-13; the specific rankings for private enterprise policy for 2004-08; and the outlook on that measure for 2009-13. In overall terms, Ireland again fares well and is comfortably in the top quartile of countries covered. Only Denmark and the Netherlands are in higher positions of the comparator countries for the overall index for 2004-08. There is, however, an indication of Ireland's position slipping over the next five years, although it remains within the top three of the

countries selected. Ireland's position on the specific indicator for private enterprise policy is even stronger, in seventh place overall for 2004-08 and set to rise to fourth place going forward. Only Denmark and the UK rate more highly.

On these two indexes, therefore, Ireland comes out well relative to international comparisons. Its policy and regulatory environment scores well in terms of creating a supportive framework for enterprise and trade. While the two indices measure different factors, there is a strong degree of consistency on where our comparator countries sit in the relative rankings. The only countries ahead of Ireland on most measures from the sample are Denmark and the UK.

The following chapters look at the comparator countries, excluding Luxembourg, in a little more detail, describing the wider context and evolution of regulatory policy.

Australia

The Australian government has consistently applied a free-market, pro-competition philosophy to economic activity, traceable back to the Trade Practices Act 1974 (TPA). Companies are generally free to set prices, but a price-surveillance mechanism can be activated under provisions of the TPA. Individual states also have fair-trading acts that cover dealings between businesses and between business and consumers.

Two major institutions implement competition policy. The Australian Competition and Consumer Commission (ACCC) is the national competition and consumer-protection watchdog; it may also undertake price surveillance in areas of the economy where competitive pressures are lacking. The Australian Competition Tribunal is a review body for certain ACCC decisions; it may also make declarations relating to offshore mergers.

Reforms during the 1990s aimed to encourage competition in the non-traded areas of the economy. This was particularly true for telecommunications and utilities, where most of the infrastructure was until recently owned and operated by federal or state government monopolies. Initially, a review and advisory body, the National Competition Council (NCC), recommended which "essential facilities"—such as electricity grids, rail networks and natural gas pipelines—should be opened to rival service providers, but this function was subsequently shifted to the ACCC (via amendments to the TPA). When the ACCC declares a facility to be essential for competition purposes, users may negotiate terms of access to it and use the ACCC to resolve disputes. The NCC focuses on two main areas: it assesses the progress of governments in implementing competitive reforms and advises on the design and coverage of access rules under the national access regime. Following a review of all aspects of regulation in 1993, the government announced that any regulation that restricted competition must be clearly shown to be in the public interest[1]. Federal and state governments committed themselves to undertaking a review of all existing regulations.

[1] F G Hilmer, (1993), *National Competition Policy: Report by the Independent Committee of Inquiry,* Canberra, Australian Government Publishing Service.

The major industries affected by competition reform are telecommunications, airports, electricity and gas.

Denmark

Denmark has one of the world's most favourable environments for private enterprise following the extensive liberalisation of product markets and privatisation of state assets that has taken place under successive governments. Only a handful of companies remain in state hands, and those that do are expected to be sold to the private sector (stockmarket conditions permitting). Danish competition policy has many positive features, including comprehensive market regulation, effective protection of intellectual property and shareholders' rights, and the absence of price controls. The government rigorously enforces competition law, having given the Danish Competition Authority (Konkurrencestyrelsen) greater powers via amendments to the Danish Competition Act.

The electricity market has been fully opened to competition since January 1st 2003, and all consumers are free to choose their supplier. A year later the gas market was liberalised, well ahead of the EU timetable. Shortly after, in March 2004, the government restructured the transmission companies with the aim of promoting more open access. On January 1st 2005 responsibility for the national grid was transferred to a state-owned company, EnergiNet Danmark. This means a *de facto* separation between the overall transmission, which is now state-owned, and the production and trade of gas and electricity, which will remain commercial.

In 1996 Denmark became one of the first countries in western Europe to open up telecommunications to competition. The incumbent provider, TDC (which is owned by a consortium of investment funds), has been competing in both fixed and mobile services ever since. The National IT and Telecoms Agency was established in April 2002 as part of the Ministry of Science, Technology and Innovation. The agency carries out the government's policy initiatives, initiates and monitors progress in infrastructure development and liberalisation and, where applicable, grants licences to service providers. As a result of these reforms the Danish telecoms market is one of the most liberalised and competitive in the world.

France

Hostility to economic liberalisation runs deep in France. The country is consistently one of the most reluctant liberalisers of product markets in the EU. The policy environment has long been marked by the state's prominent role in directing economic development, *dirigisme*. The state's direct role in the economy has been reduced over the past two decades by privatisations, but the state continues to hold stakes in a range of companies, including GDF, EDF, France Télécom, Air France-KLM, Renault, EADS, Thales, Safran and Aéroports de Paris, and has full ownership of the railways and postal services. Privatisation has been driven more by the need to reduce government debt

than by any ideological belief in its merits. Indeed, the government continues to interfere in company decisions that in many other countries would usually be reserved for shareholders. Nonetheless, France is slowly liberalising under pressure from the EU's single-market rules.

In the telecoms sector an independent regulator was established in January 1997. Its functions were extended in 2005 and the organisation was renamed the Autorité de Régulation des Communications Électroniques et des Postes (Arcep). Arcep's tasks are numerous. It acts as a consultative body on draft legislation affecting the telecoms sector; it assesses and awards licences to operators; it approves the standard interconnection offers of dominant players such as France Télécom; and it supervises operators' compliance with the legislative provisions in force. Arcep also plays a role in settling disputes between operators and has a number of sanctions at its disposal—including fines and the withdrawal of licences—to enforce compliance with the law. Previously, the regulator came in for criticism for failing to exercise its powers more aggressively. This has changed under Arcep and the regulator's powers were strengthened under the communications law that came into force in 2005. Deregulation has clearly brought down prices.

In energy the state plays a prominent role. Not only does it retain large stakes in most of the country's leading energy companies—GDF, EDF and Areva—but government foot-dragging and a *de minimis* approach to the country's obligations under EU directives have slowed the liberalisation of the gas and electricity markets. France was late in implementing the EU's electricity liberalisation directive, and it has stuck to the least ambitious timetable allowed (in contrast with the UK, for example, which has long since opened its market completely to foreign competition[2]). In 2004 France opened its gas and electricity markets to competition for all commercial users, but the final phase of liberalisation, extending competition to the consumer market, only took place in mid-2007. The slow pace of liberalisation in France has caused periodic friction with France's EU neighbours, particularly as the state-owned EDF exploited early liberalisation elsewhere in the EU to acquire stakes in foreign electricity companies at a time when the latter could not do likewise in France. For example, the merger between GDF and Franco-Belgian utility, Suez, which was agreed in September 2007, was widely seen as an attempt to prevent Suez from falling into the hands of Italy's Enel.

France's competition rules are contained in the Code of Commerce, which is updated as required. The rules are enforced by the 16-member Competition Council (Conseil de la Concurrence—CC). Most of France's competition law is based on principles established by the EU. Antitrust authorities at the EU level have jurisdiction over mergers with turnovers exceeding a certain threshold. The CC may investigate the operations of public services, state-owned corporations and private companies. It rules on monopolies and market dominance, mergers and refusals to sell. It can impose fines and issue injunctions in competition cases found by its own staff or referred by the

[2] On this point, see S G Littlechild, (2003), Electricity; Regulatory Developments Around the World, in C Robinson, (2003), ed., *Competition and Regulation in Utility Markets,* London, Institute for Economic Affairs.

ministry, private companies, professional organisations or consumer groups. Decisions are subject to appeal in the courts.

Germany

Germany has one of the world's most active antitrust programmes. Its legal basis is the Law against Restraint of Competition, which prohibits horizontal agreements and controls vertical agreements that restrict competition and abuse of a dominant market position. It forbids concerted practices, establishes preventative and retroactive controls for mergers, and bans resale-price maintenance.

The other important law in this area is the Law against Unfair Competition, which was completely revised in 2004. It lifted most limitations on the ability of companies to offer rebates, and they no longer need to confine special sales to certain periods at the end of the winter and summer seasons. The law prohibits misleading advertisements and the exploitation of children's lack of experience. It also prohibits telephone marketing and unsolicited online advertisements (spam) unless customers agree to receive them (through an opt-in clause). In May 2008 the government agreed an amendment to the Law against Unfair Competition that would introduce a so-called blacklist of unlawful business practices, such as false claims to be a signatory of a certain code of conduct or using price reductions because of closure as bait, when in reality no cessation of business is intended.

The German electricity market was liberalised in 1998. This initially pushed down pre-tax prices sharply (energy tax rises led to a substantial increase in overall terms), but a large part of this has now been reversed. According to the Monopoly Commission, a government advisory body, insufficient regulation has led to a strong rise in profits for the major players and an increasing abuse of market power. Consequently, there seems to be considerable potential for renewed price cuts through improved regulation. Up to July 2005 electricity and gas markets were regulated by association agreements—that is, accords between the main associations of electricity users and suppliers—but this system was not particularly successful at stimulating competition. The main issue is the pricing of third-party access to networks, which still works against market entrants in Germany. In accordance with a new EU directive, but after a substantial delay, legislation took effect on July 13th 2005 that entailed a shift to regulation by a regulatory agency. The task was given to the Regulatory Authority for Telecommunications and Post (RegTP), which has been renamed the Federal Network Agency. The government had initially wanted to grant the regulator only weak competencies in the power market, but as a result of legislative negotiations between the government and the opposition, the approval of which was necessary in the Bundesrat (the upper house of parliament), the regulator's powers are stronger, so there should be a substantial stimulus to competition. Competition is even weaker in the gas market, as high third-party access rates have almost completely prevented the emergence of serious new players. The change in the regulatory regime might alter this situation, although the potential for price cuts through increased competition is less clear.

The fixed-line telecoms market was also liberalised in 1998. Prices have fallen rapidly. The regulatory authority (the Federal Network Agency) and government regulation are seen as generally seeking to strengthen competition in the interest of consumers, despite occasional efforts to favour the former monopolist, Deutsche Telekom (DT), in which the government still holds, indirectly, nearly a one-third stake.

Netherlands

The Netherlands's Competition Act of 1998 marked a significant turnaround in competition and merger control and brought national legislation in line with EU legislation. The Netherlands previously had the reputation of being a "cartel paradise", compared with other European countries, because of a Dutch policy that allowed cartels to exist as long as they were recorded in a government register (where details were kept secret) and as long as they were not explicitly banned. In contrast, most other European countries banned cartels unless explicitly permitted.

The Netherlands Competition Authority (Nederlandse Mededingingsautoriteit—NMa) was created in 1999 as a Department of the Ministry of Economic Affairs. The NMa has had the status of independent agency since July 1st 2005. It enforces the Competition Act of 1998, focusing on cartels, abuse of dominant positions, and control of mergers and acquisitions. A number of amendments to the Competition Act, which took effect on October 1st 2007, gives the agency enhanced enforcement and sanctioning powers.

The regulator, DTe (Dienst Toezicht en uitvoering energie), was integrated into the NMa in 2001 as a separate unit for the enforcement of gas and electricity laws. A new transport chamber was added to the NMa in 2004 as a watchdog for the railway, public transport and aviation sector. The post and telecoms regulator (Onafhankelijke post en telecommunicatie autoriteit—Opta) operates as an independent agency, although it often works with the NMa on investigations. The NMa and Opta also co-operate on the Consuwijzer, an information service started in July 2006 to advise consumers on their rights in commercial transactions. A new institution (part of the Ministry of Economic Affairs), the Consumers Authority (Consumentenautoriteit), started work on January 1st 2007, enforcing consumer-protection laws and dealing with collective claims on behalf of larger groups of consumers.

Considering the country's small market size and international competitiveness, the Dutch government takes a benign view of mergers and acquisitions. Large deals face more intense regulatory scrutiny at the EU level, where the European Commission has sole authority over certain expensive and/or cross-border transactions concerning several EU member states.

Another instrument at the disposal of the Dutch government concerning competition and pricing is the Price Control Act of 1961. This law gave the government substantial authority to control prices, although it has rarely exercised these powers.

New Zealand

The Commerce Act of 1986 provides a code of commercial conduct to promote competition. The Commerce Commission can prevent restrictive trade practices, scrutinise mergers and takeovers, and control prices in markets that lack effective competition. Parliament last amended the Commerce Act in May 2001, introducing new definitions for thresholds relating to anti-competitive behaviour and mergers, stronger penalties, new cease-and-desist powers for the Commerce Commission and new ways to implement price controls.

The Fair Trading Act of 1986 provides complementary legislation on unfair competition, consumer information, and product and service safety. It prohibits misleading conduct and false representations in the course of trade, along with certain trade practices—such as pyramid selling, bait advertising and trading-stamp schemes. It also provides for compulsory consumer-information standards, product- and service-safety standards, and recalls.

In addition to its traditional enforcement and adjudication role under the Commerce and Fair Trading Acts, the Commerce Commission must also regulate the electricity, telecoms and dairy markets.

The electricity sector was opened up to competition and private-sector participation in the late 1990s. Complaints about the volatility of electricity spot prices led to the setting up of the Electricity Commission. This body is responsible for setting the offer price in the wholesale market for reserve generation released in dry years. In 2003 the government issued a policy statement on the development of New Zealand's gas industry, in which it emphasised the need not only to establish an open-access regime for gas pipelines, most notably the Maui pipeline, but also to minimise the barriers faced by customers switching between retailers. Most of the leading oil and gas companies operating in New Zealand are in private hands.

New Zealand's telecommunications market was progressively liberalised from 1987 and by 1989 all statutory barriers to entry to any part of the industry had been removed. A number of communications operators entered the industry and in 1990 the government-owned national provider, Telecom, was privatised, although the government maintains a "Kiwi share" in the firm. Despite deregulation, privatisation and the entry of competitors, Telecom remained the dominant company, especially in the area of land-based communications. Legislation passed in 2001 provided for the establishment of a telecoms

commissioner within the Commerce Commission[3]. A major function of the commissioner is to resolve disputes over regulated services, most notably those regarding access to Telecom's extensive network. Telecom's major competitors are TelstraClear, formed when TelstraSaturn, the New Zealand subsidiary of Australia's dominant telecoms firm, Telstra, acquired the New Zealand operations of two UK-based firms, Clear and Vodafone.

Norway

The Storting (parliament) passed a new Competition Act in March 2004 (Act 12 of March 5th 2004), which took force on May 1st 2004. The new act, which replaced one from 1993, was further amended in December 2004 to require companies with a controlling interest in a business sector to provide information about the nature of the concentration if their combined income in Norway exceeded Nkr20m (about €2.3m at current exchange rates). Since January 1st 2007 the threshold has been Nkr50m. The Competition Authority (Konkurransetilsynet) said that the change is intended to make it easier to focus on larger companies and mergers where there is a greater risk of market dominance.

The Act on Competition Rules of the European Economic Area (EEA) Agreement (No. 110, of November 27th 1992) adopted the required provisions to enable the Surveillance Authority of the European Free-Trade Association (EFTA) and the European Commission to exercise their tasks in compliance with EEA competition rules. Norway's competition legislation reflects the drive to harmonise Norwegian legislation with the EU's competition directives. The act was fully implemented in Norway by July 1st 2005. The first government of Kjell Magne Bondevik, the former prime minister, reviewed competition policy and in 2000 succeeded in securing legal changes that authorised the Competition Authority to prohibit certain corporate acquisitions and to take appropriate related temporary measures, pending a final decision.

Because of the small size of the Norwegian market and the importance of gaining competitiveness vis-à-vis foreign companies both at home and abroad, the authorities generally look favourably on co-operation among local enterprises. Horizontal and vertical price fixing is prohibited, but exemptions on a case-by-case basis are often granted. Horizontal price agreements may be approved when they will result in better quality products and lower costs,

[3] A number of studies suggested that New Zealand's light-handed regulatory regime performed better than more heavily regulated regimes in terms of reducing costs and raising efficiencies. For example, D Boles De Boer and L Evans found that NZ Telecom's performance was superior to that of BT, while Ergas argued that the New Zealand regulatory regime had performed better than the Australian regime. The lack of a sectoral regulator was criticised, however, as contributing to lengthy delays as disputes on access pricing resulted in lengthy court cases. Howell also finds that during the period of light-handed regulation New Zealand's communication sector performed better than those countries with more heavily regulated regimes and suggests that the move towards greater regulation since 2001 has coincided with deterioration in economic performance and competition with each successive increase in regulation. D Boles De Boer and L Evans, (1996), The Economic Efficiency of Telecommunications in a Deregulated Market: The Case of New Zealand, *Economic Record*, 72 (March), 24-35. H Ergas, (1996), *Telecommunications Across the Tasman: A Comparison of Regulatory Approaches and Economic Outcomes in Australia and New Zealand*, Auckland, Centre for Research in Network Economics and Communications, working paper series. B Howell, (2007), *A Pendulous Progression: New Zealand's Telecommunications Regulation 1987-2007*, Wellington, New Zealand Institute for the Study of Competition and Regulation.

protect against unfair foreign competition, or serve the public interest in some other way. If unjustified, practices that adversely affect prices (such as resale price maintenance) or that discriminate against particular firms through refusal to sell would probably be banned.

Portugal

The Competition Authority (Autoridade da Concorrência) has strengthened its role in recent years, producing a number of important market and sectoral reports and expressing an opinion on several mergers and acquisitions.

Electricity markets are now fully open to competition, but Portugal has a derogation from the EU allowing it to complete gas market liberalisation two years after other member states. OECD studies suggest that energy prices charged to Portuguese businesses, particularly small and medium-sized enterprises (SMEs), continue to be far higher than the average charged in developed economies.

Portugal's telecoms market is still dominated by the former incumbent, Portugal Telecom (PT), although it was fully privatised in 2001, when the sector was opened to competition. Nevertheless, some six years after the full liberalisation of the sector, most of the new fixed-line operators have gone out of business, having failed to compete with the incumbent, which had 71.9% of all fixed lines in the fourth quarter of 2007 (although its share is declining). The share of minutes of traffic billed by PT has declined in recent years: from 82.2% in the third quarter of 2003 to 67.5% in the fourth quarter of 2007 (according to Anacom). Overall, Portugal has a total of 25 operators licensed to provide fixed telephone services.

Portugal's financial services industry has become more sophisticated and competitive as the country has deepened its integration with the European financial system following entry into economic and monetary union (EMU). The banking system and financial markets are efficient and well-regulated, and banks have maintained high profitability despite a weak economic environment in 2002-05. Portugal has adopted European norms for most of its financial services operations. Supervision of the financial sector is undertaken jointly by three bodies, which closely co-ordinate their activities. The Bank of Portugal (the central bank), is responsible for prudential supervision of all credit institutions, investment firms and other financial companies. The Instituto de Seguros de Portugal (ISP) oversees insurance and reinsurance firms and pension funds. The Securities Market Commission (Comissão do Mercado de Valores Mobiliários—CMVM) is responsible for overseeing the securities markets.

Spain

The march towards deregulation in Spain has had mixed results. Out of ideological conviction and concern over high inflation in the services sector, the former government of the centre-right Popular Party (Partido Popular—PP) privatised and liberalised postal services, electricity generation and distribution, telecoms, air transport, land use and petrol distribution—usually well ahead of

deadlines set by the EU. Spain was one of only six countries in 2005 that had completely opened its gas and electricity markets to wholesale competition, according to a study by the European Commission. However, these initiatives were offset by the emergence of private *de facto* monopolies to replace the formerly public ones in major areas.

Spain still has significant restrictions on domestic market freedom. Consumers complain that competition in the airline, telecoms and energy markets might exist on paper, but monopolistic practices persist. For instance, Telefónica still has more than half of the fixed-telephone market, and local monopolies of natural gas and electricity have retained their pricing power and found ways to restrict consumer choice. Air carrier, Iberia, another former state-owned monopoly, still controls most domestic traffic, but it is now facing increased competition from low-cost carriers, like Vueling (Spain), EasyJet (UK) and Ryanair (Ireland). The OECD ranks Spanish markets as much more restrictive—in terms of inward limits to competition—than the US, the UK, Ireland, the Netherlands, Germany and Austria, but less restrictive than France, Belgium, Italy and Greece. The present Spanish Socialist Workers' Party government has shown no signs of committing to continuing the liberalisation process.

The framework for competition policy in Spain has been set out and strengthened by a series of initiatives in recent years, including Royal Decree Laws 2/2001, 6/2000 and 6/1999, Law 52/1999 and Royal Decree 295/1998. These legislations prohibit practices intended to limit competition and the use of a dominant position to the detriment of the economy, consumers or competitors. They specifically forbid price-fixing, production limits, market division, unfair tactics to eliminate or injure competitors and forced tied sales.

Law 15/2007 provided for the creation in July 2007 of the National Competition Commission (Comisión Nacional de la Competencia—CNC). This single agency combined two previous specialised agencies charged with overseeing antitrust policy: the Service for the Defence of Competition (Servicio de Defensa de la Competencia—SDC), part of the Ministry of Economy and Finance; and the Tribunal for the Defence of Competition (Tribunal de Defensa de la Competencia—TDC).

The new CNC combines the tasks and responsibilities of the SDC and the TDC, including drafting reports, issuing opinions on proposed legislation, enforcing competition legislation and overseeing business practices. Several regional governments are creating their own competition courts, following a Supreme Court decision in 1999 declaring that regions had the authority to decide in all cases except those involving mergers and concentration.

UK

The main agencies responsible for overseeing competition policy are the Office of Fair Trading (OFT) and the Competition Commission (CC). The OFT became a corporate body in April 2003, with new powers under the Enterprise Act. The CC superseded the Monopolies and Mergers Commission in April 1999, in preparation for a new competition regime that took effect in March 2000. The OFT not only deals with competition issues, but also with consumer trade

practices, including advertising and labelling, resale price maintenance and some other aspects of consumer protection. The CC has around 50 part-time members, drawn from industry, trade unions and the academic world. It investigates matters arising from mergers, monopolies and anti-competitive practices. Under the Enterprise Act, such investigations usually result from a referral by the OFT.

The main provisions of the Competition Act 1998 came into force on March 1st 2000. The new regime, modelled on Articles 81 and 82 of the EU treaty, takes a prohibition approach. It bans anti-competitive agreements (like price-fixing and market-sharing cartels) and anti-competitive behaviour (like predatory pricing) by firms that dominate the market. The prohibitions apply regardless of company size. Certain types of agreement are exempt from the ban on anti-competitive agreements, notably vertical agreements between manufacturers and distributors, and those already made exempt by the EU's competition authorities.

The rules are enforced by the OFT, which has various powers of investigation, such as the right to enter and search premises. Companies that participate in cartels or abuse their market power risk fines of up to 10% of turnover in the UK for every year of infringement up to a maximum of three years. Hence, the penalties are tougher than at the EU level (which has a maximum of one year). Consumers and competitors affected by anti-competitive agreements and behaviour have the right to sue for compensation.

Most public utilities are regulated by special regulatory bodies, although the OFT and the CC also have supervisory roles. The Competition Act 1998 gave new powers to the utility regulators to investigate and act against anti-competitive activity. The UK system of economic regulation has already been described to some extent in Chapter 3. Formulae related to the retail price index determined controls on charges for water to domestic and small-business users. Charges paid by large-scale users are less heavily regulated. Retail price controls on British Telecom were lifted on August 1st 2006, although certain wholesale price controls remain in the telecoms market. Gas and electricity prices have been liberalised for all users.

Benchmarking criteria

We have used four broad sets of criteria to undertake the comparative analysis.

Cost-effectiveness of the regulator

We have gathered information on a number of variables under this heading, attempting to compare the internal operations of the respective regulators and in particular to establish their relative efficiency and cost-effectiveness. In terms of quantitative measures, we have asked for information on the numbers employed in each regulator, and on their income and cost structures. Comparing these with the scale of the industry that they are responsible for regulating gives some indication of relative efficiency. As far as possible, we have calculated the following ratios: regulator income per head of country population; regulator income per regulator employee; regulator income to industry income; and regulator staff numbers to total employed in the regulated industry.

Regarding more qualitative analysis, we have sought to compare factors such as the regulators' income sources and trends (for example, government grants and industry levies) and the stability and robustness of their regulatory code.

Table 12: Comparative price index

		2004	2005	2006	2007
	OECD 30	100	100	100	100
1	Denmark	137	139	142	150
2	Norway	130	134	136	144
3	Ireland	122	124	125	129
4	UK	113	115	118	126
5	Luxembourg	112	112	113	120
6	France	114	112	113	118
7	Netherlands	110	109	111	115
8	Germany	109	108	109	115
9	Australia	98	103	105	113
10	New Zealand	98	105	97	108
11	Spain	92	93	94	96
12	Portugal	87	86	87	91

The above table is taken from data published by the OECD on comparative price levels as derived using purchasing power parities. For each of the years observed, Ireland is ranked third in terms of the price of goods and services. In 2007 Ireland was 29% more expensive than the OECD average. However, Denmark and Norway were 50% and 44% more expensive, respectively. Portugal and Spain are the only comparator countries below the OECD average.

From this analysis it would be expected that regulation would cost more in Ireland than the non-Scandinavian countries, although this difference should be minimal compared with the UK and Luxembourg. The cost of regulation in Spain and Portugal would be expected to be considerably lower than in Ireland according to the comparative price index above.

In making international cost comparisons the average exchange rates for 2007 are used, as per table 13 below.

Table 13: Average exchange rates for 2007

Currency	1 Euro =
British Pound	0.68
Australian Dollar	1.63
New Zealand Dollar	1.86
Norwegian Kroner	8.0
Danish Krona	7.45

Governance and accountability

This was identified by the inter-departmental steering group for this review as an especially important area for international comparison. Governance covers the legislative and management structures under which the regulators operate. Accountability covers the means by which they report to and are held accountable by the relevant political authorities at ministerial and parliamentary level. The range of factors that we have sought to cover under this category includes:

- the regulator's legal status and if and how it has changed over time;
- the extent to which EU directives determine the regulator's remit;
- the frequency, scale and purpose of changes to remit over time;
- the formal and informal controls over such changes;
- the lines of accountability to departments, ministers and parliament and how these are exercised;
- the extent of ministerial power to issue directives to the regulator;
- the procedures for evaluating regulator performance; and
- the structure and effectiveness of appeals procedures.

Impact on regulated business

Under this heading we have sought to gather information on the impact of regulators on the industries and markets that they are regulating. This has involved trying to establish the scale of the industries involved—by revenue, employment, profitability, asset base. It has proved to be a complex exercise given the differences across countries in the definition of sectors actually under regulation. In energy, for example, different parts of the production and distribution systems are regulated in different countries. We have also tried to establish the extent to which regulators' objectives in relation to their industries vary. For example, some telecoms regulators have an objective to extend broadband penetration while some energy regulators have specific objectives in renewables.

We have gathered information on the level of legal and related activity generated by regulators and by industry responses to their decisions—legal challenges, appeals, fines. We have also examined the regulators' impact on markets, for example in terms of openness to international operators and to new, local market entrants.

Impact on consumer markets

In some sectors, regulators have a role in consumer protection and we have gathered information on how this role is conducted. We have sought data on, for example, the number of consumers of products and services under regulation and their consumption of those services. We have also sought to establish the trends in prices of the regulated products and services, as a guide to how competitive the markets are. And we have examined consumer choice issues such as the choice of suppliers and the ease of switching to new suppliers.

In order to gather the relevant material, a checklist was prepared covering the data and information required in each country and sector. The three main information sources approached were the regulators themselves, the relevant supervising government departments and representatives of the business community.

The checklist was used by Economist Intelligence Unit country analysts to structure their discussions and correspondence with the overseas contacts. Much of the quantitative data required was available from the websites of the relevant regulators and government departments. Wherever possible this was validated by direct contact with the organisations themselves. The qualitative

information required fuller discussion with representatives of the organisations and this was conducted through a combination of face-to-face or telephone interviews and extended email correspondence.

The results of the international research are presented primarily at a sectoral level—that is the level at which comparisons of regulator efficiency and impacts are most relevant. There is, therefore, a separate chapter covering each of the case study sectors.

There is considerable variation in the regulatory models across the countries examined. As suggested by our initial literature review, the models adopted need to fit into the wider economic, legislative and institutional structures in each country. The level of variation is therefore not surprising.

It does, however, pose many challenges when making comparisons. For example, in the energy sector some regulators supervise the whole supply chain while others cover only specific parts of it, such as the transmission network. In financial services, some countries have regulators that cover all parts of the industry while in others there are separate regulators for, for example, banking and insurance. There are also differences in the functions covered by financial regulators, with some countries separating responsibility for prudential supervision and consumer protection and others covering both within a single regulator. The locus of responsibility for consumer protection also varies by country and sector. Thus, the comparative work needs to take these multi-level differences into account.

6. Financial services

The 2003 Central Bank and Financial Services Authority of Ireland Act established the Financial Regulator with a mandate to supervise all financial institutions in Ireland and provide a consumer protection role for customers of financial service firms. The Financial Regulator is part of the Central Bank and Financial Services Authority of Ireland (CBFSAI). The Financial Regulator is responsible for regulating a wide range of financial institutions including credit institutions, insurance undertakings, various intermediaries such as mortgage brokers, collective investment schemes, credit unions, moneylenders, approved professional bodies, exchanges and bureaux de change. It also has considerable consumer protection functions.

Policy context

There could be no more challenging time to compare financial regulatory systems, with the global financial system in turmoil and its regulation subject to intense scrutiny and review. Traditionally, the focus of financial regulation has been on prudential regulation. Prudential regulation aims to maintain the integrity of the financial system by ensuring that institutions keep adequate levels of liquidity and do not become insolvent. The issue is not so much about the solvency of a particular institution, but the risk that the failure of one institution may undermine confidence in the financial system as a whole, giving rise to what is referred to as "systemic risk".

To some extent, of course, prudential supervision of financial institutions serves to protect consumers' interests. Ensuring the solvency of financial institutions clearly helps to protect depositors. There is, however, a potential conflict between prudential and consumer protection roles. For example, higher bank profits reduce the risk of insolvency. However, such profits might result from consumers paying higher prices than they would in a more competitive setting. Thus, a prudential regulator might favour less competition between financial institutions, even though this means higher costs for consumers, on the grounds that it will result in increased profitability and thus enhance the solvency of financial institutions. It is relatively unusual for prudential supervision of financial markets and consumer protection to be undertaken by the same body, as has happened in Ireland.

The other key choice in financial regulation is between a strict rules-based approach, setting firm and detailed rules for how financial institutions should operate, and a more light touch, risk-based approach that specifies desired outcomes, but neither defines how they should be achieved nor attempts to manage risk out of the system altogether. While the latter approach has been prevalent to date in the largest financial sectors, in particular the US and the UK, part of the likely fall-out from the recent upheaval in the market will be

firmer, more intensive regulation with a further strengthening of existing transnational frameworks.

Comparator countries

The regulatory arrangements for financial services were examined in eight other countries: Australia, Denmark, Germany, Luxembourg, Netherlands, Norway, Spain and the UK. A summary of the regulatory environment and arrangements in each is presented below.

Australia

There are two financial regulators in Australia. The Australian Prudential Regulation Authority (APRA) is responsible for the prudential regulation of the whole financial services sector, while the Australian Securities and Investment Commission (ASIC) is charged with protecting consumers across the entire sector. The APRA was established in 1998 and has independent status. The federal government has responsibility for setting prudential policy and the APRA performs its role within the statutory framework laid down by government. It is accountable to parliament through the Treasury and can be issued directives by the minister, although this power has not been used to date. The APRA's approach to prudential regulation has been risk- rather than prescription-based—that is, identifying desired outcomes from financial institutions rather than prescribing how these should be achieved.

The ASIC began operations in 1991 and was given its current powers and responsibilities in 1998, at the same time as the APRA was established. Like the APRA, it is an independent agency, reporting to Treasury ministers. It is also accountable through administrative and judicial review procedures. The ASIC's objectives are: to uphold the law uniformly, effectively and quickly; to promote confident and informed customers; to make company information available quickly and freely; and to improve the performance of the financial sector.

Denmark

The IMF's most recent stability assessment of Denmark's financial sector, in 2006, found that it was generally resilient and well supervised by Finanstilsynet, the Danish Financial Supervisory Authority (DFSA). The DFSA is an integrated agency, established in 1988, with prudential and consumer protection regulatory responsibility for the entire financial sector, including banks, mortgage providers, life assurance and pension funds, non-life assurance companies, investment companies, investment managers, insurance brokers, financial holding companies and the securities market.

Financial stability is not only a matter for the DFSA, but also for the central bank and relevant ministries. Therefore, the responsibility for financial stability is split between the DFSA, Danmarks Nationalbank (the central bank), the Ministry of Economic and Business Affairs and the Ministry of Finance. All have concluded a memorandum of understanding setting out their distinct responsibilities and expertise in the overall regulatory framework.

Germany

The German regulatory agency is the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin), established in 2002. Prior to this, there were three separate

regulators handling different sectors of the industry. BaFin is an independent body, subject to legal and technical oversight by the Ministry of Finance. It has prudential regulatory responsibility for all branches of the industry—insurance, banking and securities—with a broad remit to guarantee the stability of the financial system, protecting solvency and enforcing professional standards. It does not have a statutory consumer protection role but does play a part in consumer education.

Luxembourg

Luxembourg was selected for comparison for the specific purpose of examining the financial regulatory system's role in attracting overseas financial sector investment. Luxembourg has a large financial sector, mostly comprising subsidiaries and branches of foreign banks. For example, it is a major centre for offshore private banking, with around 15% of the global market.

Overall responsibility for regulating the sector rests with the minister for the Treasury. The Central Bank of Luxembourg (BCL) and the Financial Sector Surveillance Commission (CSSF) are the key regulatory agencies. The CSSF covers all financial services except insurance, which is covered by a separate body, the Insurance Commissariat (CAA). The current structure came into place in 1998, when Luxembourg joining the euro zone. The CSSF has prudential regulation responsibility for its sectors, but no consumer protection role.

Netherlands

The Dutch financial system is dominated by a relatively small number of large, global institutions. This, along with the general openness of the Dutch economy, makes the financial sector sensitive to global economic and financial trends. The Netherlands Financial Markets Authority (AFM) was established in 2002 as a successor to the Securities Board of the Netherlands. The AFM is responsible for consumer protection across the entire financial sector. It is not responsible for prudential regulation, which rests with De Nederlandsche Bank (the central bank).

Norway

The financial services sector in Norway is relatively small, but considered to be sound, well-managed and competitive. The regulator is the Kredittilsynet, or the Financial Services Authority for Norway (FSAN). As with Denmark, the FSAN is a government agency and reports to the Ministry of Finance. Although Norway is not a member of the EU, its participation in the European Economic Area (EEA) means that its regulatory system is closely aligned with EU norms. The FSAN has prudential regulation responsibility, but no statutory consumer protection function.

Spain

The financial sector in Spain comprises around 500 banks and 300 insurers, while the Spanish stockmarket is one of the largest in Europe. The financial regulatory code is characterised by a "three pillars" model whereby the banking, securities and insurance sectors are separately supervised. Regulation is ultimately the responsibility of the Ministry of Economy and Finance. The ministry drafts regulations that are put into practice by the separate regulatory bodies.

The Bank of Spain (the central bank) supervises all commercial and savings banks; credit co-operatives and institutions; factoring and leasing companies; mortgage providers; money market intermediaries; and guarantee-financing

companies. It also oversees the inter-bank loans market and certificates of deposit and foreign exchange. In exceptional circumstances the Bank can intervene in the operations of banks, both domestic and foreign. The National Securities Markets Commission (CNMV) has responsibility for prudential supervision and consumer protection in the stock, private bond and derivatives markets. The third pillar, the Directorate General of Insurance and Pension Funds (DGSFP), has responsibility for prudential supervision and consumer protection in the insurance and pension sectors and is part of the economy and finance ministry.

UK

The UK financial services sector is one of the largest and most diverse globally. It is also a huge contributor to the British economy, accounting for over 9% of GDP. The current framework rests upon a tripartite system of financial regulation. The Bank of England (the central bank) has operational independence to set interest rates and contribute to the maintenance of the stability of the financial system as a whole. The Treasury (the finance ministry) has authority to step in where necessary with support for fundamentally sound institutions. The Financial Services Authority (FSA) is the integrated regulator with responsibility for both prudential supervision and consumer protection across most financial services markets, with the exception of consumer credit and occupational pension schemes.

The FSA has largely adopted a light-touch, principles-based approach and until recently the financial regulatory system in the UK was seen as a model of good practice internationally—robust, transparent and sophisticated. The recent turmoil in the financial markets, which in turn has resulted in extensive state intervention and direct investment to save ailing banks in the UK, has damaged that reputation and will lead to changes in the framework.

Conclusion

In summary, the financial regulators in Ireland, the UK and Denmark have responsibility for both prudential and consumer regulation. The German regulator is primarily responsible for prudential regulation, but with a role in consumer education. In Norway and Luxembourg the regulators are only responsible for prudential regulation, while in the Netherlands the regulator only covers consumer protection with the central bank retaining the prudential role. In Australia there are separate regulators for prudential supervision and consumer protection functions. Lastly, in Spain there are three regulators, each with joint prudential supervision and consumer protection responsibility, but individually covering separate sectors of the industry.

Unusually, the Irish Financial Regulator also has responsibility for approving bank charges, imposing a fee for each application for an increase in charges or for the introduction of new ones. The rationale for the fee is that it is designed to cover the costs of processing the applications. While such regulation is designed to protect consumers, it may however, hinder innovation as institutions must notify the regulator and seek approval for charges for any new products.

Effectiveness and cost comparisons

In our meetings with stakeholders it was recognised that the combination of prudential supervision and consumer protection within the Financial Regulator had been an ambitious move. The general view at that time was that the unitary structure has been successful. In terms of consumer protection and advice it was felt that the Financial Regulator's price surveys and comparisons were useful and that the consumer protection code was seen to be working well.

Any comparison of the relative effectiveness of financial regulatory structures must be highly coloured by current conditions in the global markets and the factors that gave rise to them. In terms of prudential supervision, it is now clear that national and international financial systems proved almost fatally vulnerable to liquidity and solvency problems in the wake of the credit crisis. No particular regulatory structure among the comparator countries proved any more capable of protecting its financial system in such a complex and internationally interdependent situation. The core causes of the problems had generally escaped the radar of the regulators, and the regulatory regime in future is likely to be tighter and more international in nature.

There are aspects of the current Irish structure that may go with the grain of coming trends. In particular, the close organisational and administrative links between the regulator and the Central Bank should help to resolve some of the unclear and fragmented lines of responsibility and communication that are now being highlighted in other countries.

In recent months, however, serious questions have emerged regarding the effectiveness of the existing system of financial regulation in Ireland following revelations that over several years certain directors of a financial institution had concealed substantial loans from that institution. A subsequent report prepared for the board of the Financial Regulator found serious deficiencies in the response of the Regulator concluding that there had been:

"a breakdown in terms of internal communications and process and in the regulatory follow-up and response of the organisation. This resulted in a failure to take appropriate and timely actions in relation to what was a serious matter and to escalate the matter to the Authority."[1]

This episode may have serious negative consequences for how Ireland's regulatory system is viewed internationally. We do not see, on the basis of the comparative work, a case for major changes in the Financial Regulator's current structure and remit as a means of improving effectiveness. Clearly, however, this episode indicates that there is an urgent need for more effective monitoring procedures by the Financial Regulator and highlights the need for greater accountability. The Financial Regulator is currently committed to a comprehensive review of its strategic regulatory approach in light of developments in 2007 and 2008.

[1] CBFSAI statement of January 8th 2009.

In terms of consumer protection and information, the Financial Regulator's performance stands up well to comparison with any of the other regulators reviewed with a similar function.

Cost structure and comparisons.

Details of the Financial Regulator's income are given in Table 14.

Table 14: Financial Regulator income 2004-07 (€'000)

	2004	2005	2006	2007	% of total 2007	% change 2004-07
Industry levy	19,082	20,366	21,394	22,309	41.9	16.9
Surplus		1,686	2,110	2,193	4.7	
CBFSAI subvention	17,643	20,364	24,364	25,375	47.1	43.8
Other		1,003	2,887	3,329	6.3	
Total	**36,725**	**43,419**	**50,755**	**53,206**	**100**	**44.9**

Source: Financial Regulator Annual Reports.

The Financial Regulator's total income in 2007 amounted to €53m, which represented an increase of 45% compared with 2004. Interestingly the industry levy element of total income increased by only 17% over this period, while the CBFSAI subvention increased by 44%. In 2007 the subvention accounted for 47% of the Financial Regulator's total income and the levy for 42%, with the balance being made up of other income and the previous years' surplus[2].

Table 15 looks at how the levy is split between the different constituents of the financial sector.

Table 15: Composition of Financial Regulator levy 2004-07 (€'000)

	2004	2005	2006	2007	% of total 2007	% change 2004-07
Credit institutions	6,022	6,713	7,423	8,174	36.6	35.7
Insurance undertakings	3,701	4,270	4,854	4,707	21.1	27.2
Intermediaries	2,855	2,954	2,888	2,071	9.3	-27.5
Securities and investment firms	2,106	1,438	1,445	1,653	7.4	-21.5
Collective investment schemes	3,678	3,963	3,529	4,318	19.4	17.4
Credit unions	1,005	1,057	1,298	1,417	6.4	41.0
Moneylenders	119	109	158	187	0.8	57.1
Approved professional bodies	87	38	20	22	0.1	-74.7
Exchanges	90	95	101	168	0.8	86.7
Bureaux de change	19	19	28	40	0.2	110.5
less provision/write-offs	600	290	350	448	2.0	-25.3
Total	**19,082**	**20,366**	**21,394**	**22,309**	**100**	**16.9**

Source: Financial Regulator Annual Reports.

[2] The levy of each credit union is currently capped at 0.01% of total assets with any shortfall in total levies raised from credit unions (as compared with the 50% cost of their supervision) incorporated within the CBFSAI subvention. As agreed with the minister of finance, the CBFSAI has borne the full cost of certain securities market supervision activities carried out with the Financial Regulator since 2006. This partly explains why the subvention accounts for slightly more than 50% of income.

Some 37% of the total industry levy in 2007 was paid by credit institutions, with insurance undertakings accounting for a further 21% and collective investments schemes 19.4%. According to the Financial Regulator, any increase in the proportion of the levy borne by one industry sector reflects an increase in the amount of supervisory activity attributable to that sector.

Table 16: Financial Regulator expenditure by area of activity 2004-07 (€'000)

	2004	2005	2006	2007	% distribution 2007	% change 2004-07
Prudential	20,560	23,749	27,349	29,681	56.4	+44.4
Consumer	12,237	14,009	15,369	16,212	30.8	+32.5
Registrar of Credit Unions	2,242	2,548	2,957	3,385	6.4	+51.0
Other	0	1,003	2,887	3,329	6.3	n/a
Total	**35,039**	**41,309**	**48,562**	**52,607**	**100**	**+50.1**

Source: Financial Regulator Annual Reports.

The Financial Regulator's total operating costs in 2007 amounted to almost €53m which, as noted in Chapter 4, made it the largest of the regulatory bodies examined in this review. Its operating costs per employee amounted to €153,000, significantly lower than any of the other regulatory agencies reviewed apart from the Health and Safety Authority (HAS). This may partly reflect the attribution of the cost of shared services undertaken by the Central Bank on behalf of the Financial Regulator. Expenditure on prudential regulation in 2007 amounted to almost €30m, up by 44% compared with 2004 and representing 56% of total expenditure. The Financial Regulator spent over €16m on consumer information and protection, up by 33% from 2004 and accounting for almost 31% of its total expenditure[3]. Spending on credit union regulation amounted to €3.4m, which was 51% higher than in 2004.

Table 17: Breakdown of expenditure 2007 (€'000)

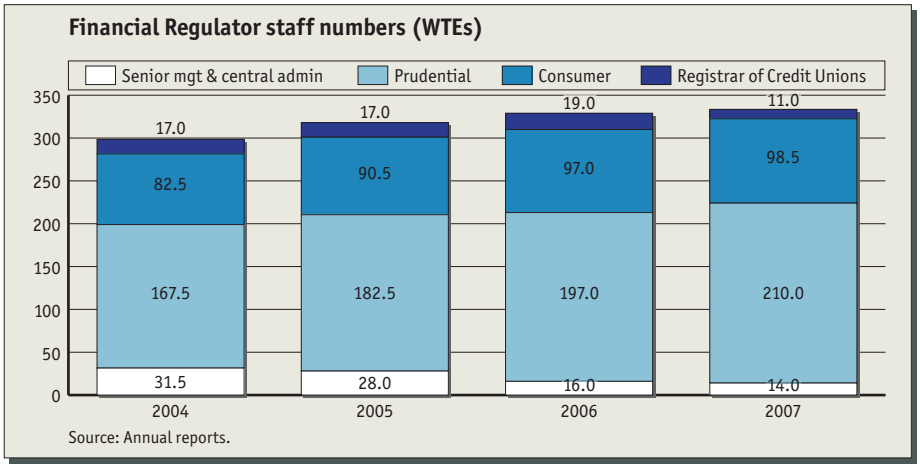
	Prudential		Consumer		Registry of Credit Unions		Total	
	€('000)	%	€('000)	%	€('000)	%	€('000)	%
Payroll	15,782	53.2	6,362	39.2	1,817	53.7	23,961	48.6
Non-pay	1,425	4.8	3,954	24.4	201	5.9	5,580	11.3
Support departments	3,826	12.9	1,730	10.7	436	12.9	5,992	12.2
Shared services	8,648	29.1	4,166	25.7	931	27.5	13,745	27.9
Total	**29,681**	**100**	**16,212**	**100**	**3,385**	**100**	**49,278**	**100**

Source: Financial Regulator Annual Report 2007.

Note: Other expenses (€3.3m) relating to fees collected by the Irish Stock Exchange are not included in the above table.

Salary costs accounted for around 49% of total expenditure, although there was some variation between the three areas of activity, with salary costs lower in the case of consumer protection and non-pay costs correspondingly higher than in prudential activities and credit union regulation.

[3] This figure compares with the National Consumer Agency's budget for 2008 of €9.5m



The Financial Regulator's staff numbers have increased from 299 in 2004 to 334 in 2007, a rise of almost 12%. In 2007, 210 (63%) staff were engaged in prudential supervision and 80 (23%) on consumer protection. Senior management and other centralised functions accounted for just 3% of total staff numbers[4].

Table 18 compares Financial Regulator average payroll costs per employee with those of the other regulators. It shows the percentage difference between average payroll costs per employee in the Financial Regulator and in each of the other regulated sectors analysed.

Table 18: Financial Regulator average payroll costs compared with other regulators

CAR	Electricity	Gas	Communications	Postal services	CTR	HSA
+0.9	-13.8	-4.8	-11.5	-8.2	+57.6	+4.4

Average payroll costs per person in the Financial Regulator compared favourably with most of the other agencies reviewed and were significantly lower than in gas, communications and postal services, but above those in the CAR, CTR and HSA.

The following tables present our data on international comparison of regulator costs. The first table below presents three ratios related to the regulators' income: regulator income per head of country population; regulator income per regulator employee; and regulator income to gross value added of the industry.

[4] These staffing figures do not include staff engaged in shared services with the CBFSAI.

Table 19: Income ratios, 2007

Country	Ireland	Australia	Denmark	Germany	Luxembourg	Netherlands	Norway	Spain	UK
Regulator Income, €m[5]	53	*225 (A$366m)	21 (Dkr160m)	123	**39	75	25 (Nkr198m)	***60	446m (£303m)
Regulator income per head of population, €	13.0	11.0	3.9	1.5	81.3	4.5	5.4	1.5	7.3
Regulator income per employee, €'000	154	140	109	72	126	172	113	101	179
Regulator income to industry income[6]	1:339	1:317[7]	1:484	1:745	1:228	1:405	1:372	1:684	1:308

* Australia includes income for both financial regulators, APRA and ASIC.

** Luxembourg includes income for both regulators, CSS and Insurance Commissariat.

***Spain income only for CNMV (stock and bond market regulator).

The UK has the largest regulatory budget at €446m, which, apart from the relatively large size of the British economy, is also influenced by London being the leading global centre for financial services. Disregarding Luxembourg as an outlier because of its low population, Ireland emerges as the most resource-intensive on the first income measure with an income of €13 per head of population. Australia is also relatively resource-intensive at €11 which may be influenced by the existence of two separate financial regulators. Disregarding Spain since the data refers only to the stockmarket, Germany has the lowest regulator income per head of population at €1.5, which is significantly less than all other regulators.

Regulator income per employee is highest in the UK at €179,000. Ireland is approximately the median result on this measure with a budget of €154,000 per employee. Germany is least costly with an income of only €72,000 per employee, far lower than any of the other regulators.

Luxembourg is the most resource-intensive when considering the regulator's income against the gross value added of the financial intermediation sector. On this measure, the Luxembourg regulator has €1 in income for every €228 of value added by the industry. Germany's budget is only €1per €745 value added by the industry. Ireland is comparable with Australia on this measure and is relatively well balanced in terms of regulator income to industry gross value added. Overall, the cost of financial regulation does not appear to be closely related to the general cost of goods and services shown in the OECD comparative data in Table 12.

[5] Income data sourced from 2007 annual reports.

[6] Gross value added for the financial intermediation sector (Nace J) Eurostat data 2007: Ireland €18bn, Denmark €10.4bn, Germany €91.6bn, Luxembourg €8.9bn, Netherlands €30.4bn, Norway €9.2bn, Spain (2006) €41bn, UK (2005) €137.4bn.

[7] Australian industry data provided by APRA-financial sector income A$116bn.

Table 20: Employment ratios

Country	Ireland	Australia	Denmark	Germany	Luxembourg	Netherlands	Norway	Spain	UK
Regulator staff numbers[8]	344	*1,610	197	1,700	**310	434	220	***592	2,489
Regulator employment growth over 5 years (%)	12	15	14	13	44	49	24	****8	8
Regulator employment to industry employment[9]	1:270	1:251[10]	1:438	1:785	1:132	1:613	1:259	1:824	1:490

* Australia includes staff numbers for both regulators, APRA and ASIC.

** Luxembourg includes staff numbers for both regulators, CSS and Insurance Commissariat.

*** Spain includes CNMV employees and IMF estimate of 241 DGSFP employees in 2006. Data does not include regulatory employees in the central bank.

**** Relates only to CNMV.

The UK financial regulator has significantly more staff than the other regulators, with 2,489 employees. However, growth in staff numbers has been lowest in the UK over the last five years, at 8% (Spanish data relates only to the stockmarket regulator). The Netherlands has witnessed the fastest growth in employment, at 49%. Over the 2004-07 period, Ireland has increased staff numbers by a steady 12%. Luxembourg is most resource-intensive when comparing regulator employment with employment in the financial services industry, where for every one person employed by the regulator, 132 people are employed in the financial services industry. Disregarding Spain, Germany is least resource-intensive on this measure, employing one person for every 785 employed in industry. Ireland is comparable with Norway and Australia, being relatively heavily resourced on this measure, with one person employed for every 270 employed in industry.

Overall, the tables above offer a solid resource comparison across the various country regulators, with the exception of Spain. Ireland has the largest regulator income per head of population. Denmark is a similar sized country and has the same broad functions but requires less than half of the Irish income. The Dutch and Norwegian regulators are not responsible for both operational supervision and consumer protection, but would still appear significantly less resource-intensive than Ireland. However, it is important to note that the financial sector in Ireland contributes a significantly greater proportion to the economy. Looking at the ratio of regulator income to sector gross value added could therefore provide a more accurate picture, and Ireland is about average on this measure. In terms of staffing, Ireland would appear to be marginally towards the more resource-intensive end of the scale, but not to any degree that would raise

[8] Staff numbers sourced from 2007 annual reports.

[9] Numbers employed in the financial intermediation sector (Nace J), Eurostat data 2007; Ireland 93,000, Denmark 86,000, Germany 1.336m, Luxembourg 41,000, Netherlands 266,000, Norway 57,000, Spain 488,000, UK 1.219m.

[10] Australian employment data provide d by APRA, 404,000 employed in financial intermediation.

concerns. Overall, the Financial Regulator would appear to be broadly in line with the comparator countries in terms of the resources at its disposal.

Governance and accountability

The Financial Regulator has a full-time chief executive along with a board comprising some executive membership and some shared membership with the board of the CBSFAI. It also has two consultative panels, one representing industry interests and the other consumer interests. Overall, our meetings with stakeholders suggested that this model had worked rather well. Some felt that the CBFSAI and Financial Regulator boards included too few individuals with a financial sector background. It was suggested that it was possible to combine public interest with having a background in the financial sector. In our view, this issue relates purely to the composition of the board rather than to the appropriateness or otherwise of the governance model chosen. Recent experience suggests, however, that the composition of the CBFSAI and Financial Regulator boards may need to be reviewed and consideration needs to be given to including more individuals with detailed knowledge and expertise in financial services, while ensuring that this would not give rise to any potential conflicts of interest.

At the time that the Financial Regulator was established it was envisaged that communication between the industry and consumers and the regulator would be improved by the establishment of consultative panels, and that the statutory ombudsman scheme would ensure that consumer complaints were dealt with effectively. Our discussions with stakeholders indicated that the two advisory panels had played a useful role. They were seen largely to work as a clearing-house mechanism. They have some input into the Financial Regulator's budgetary process and were seen to have worked with the regulator to improve budgetary reporting. Each of the consultative panels has access to some consultancy resources, giving them scope for commissioning necessary research and thereby improving their ability to play a useful advisory role to the regulator.

Governance and accountability issues are essentially qualitative in nature and there are no benchmarking metrics to apply here. The qualitative comparisons do, however, reveal some important differences between the countries examined, and we discuss them under the main headings of: legal status, EU influence, changes to remit, lines of accountability, performance evaluation and appeals procedures.

Legal status

The formal legal status of the financial services regulators in each country is summarised in the table below. One of the characteristics of effective regulation identified from our literature search was the ability to operate independently from government, and it is this degree of independence that we have sought to test here.

Table 21: Financial regulators' legal status

Country	Regulator	Legal status
Ireland	Fin.Reg.	Part of central bank
Australia	APRA	Independent public body
	ASIC	Independent public body
Denmark	DFSA	Part of Ministry of Economics and Business Affairs
Germany	BaFin	Independent public institution
Luxembourg	CSSF	Independent public institution
Netherlands	AFM	Independent administrative authority
Norway	FSAN	Part of Ministry of Finance
Spain	CNMV	Independent public agency
	DGSFP	Part of Ministry of Economy and Finance
UK	FSA	Independent, non-governmental body

Most of the regulators in the countries covered fall into two main categories in terms of their legal status: independent public bodies or departments of a government ministry. Only in Ireland does the regulator sit within the central bank. The Norwegian and Danish regulators are part of a government department and this follows a typically Scandinavian model of regulation. The insurance regulator in Spain, the DGSFP, is also part of a ministry although a change in this is likely under planned new legislation. The most common position is for the financial regulator to be an independent public agency, as is the case in Australia, Germany, Luxembourg, the Netherlands and the UK.

The question then arises of whether the regulators' legal status is actually significant in terms of its degree of independence to operate. There is no evidence from our research to suggest that this is the case. Those regulators who are established as independent bodies are nevertheless subject to the legal statutes under which they were set up, they must report to their relevant government ministry, they generally have their board appointed by government and are subject to ministerial directives. Meanwhile, the Scandinavian regulators, although formally part of a government department, are empowered to operate with a significant degree of operational autonomy from their ministry.

The Financial Regulator's position as part of the Central Bank is unique among the sample of comparator countries. Again, there is no evidence from our research that this makes the Financial Regulator any less autonomous in its operation than the overseas comparators. As indicated earlier, one of the possible outcomes in those countries most affected by the current turmoil in the financial markets—the UK in particular—is a demand for better communication between the financial regulator and the central bank. It is possible that there will be a similar move in Luxembourg, where the gap between the central bank and the regulator has long been identified as a potential risk. In this regard, therefore, the Irish model may be regarded as an example of good practice for others to follow.

Although not directly related to legal status, the regulators' source of funding can be an indicator of independence from government control. In most of the countries covered the financial regulator is wholly funded by some form of levy on the regulated sector. The exceptions are Australia, the Netherlands and Ireland. In the Netherlands, two-thirds of funding is from an industry levy. Only

in Australia were the regulators more dependent on direct government funding than in Ireland (over 90% dependent in the case of both the APRA and ASIC). Given the degree of control that governments may be able to exercise irrespective of the regulator's legal status, the practical significance of not being dependent on public funding may be questionable. However, the ability to show a lack of reliance on public funds can be a useful means of improving the perception of independence. In the Irish context it is therefore worth considering the case for moving towards fuller industry funding. This would need to be balanced against the risk that 100% industry funding may be perceived to prejudice the Financial Regulator's consumer protection role.

EU influence

All regulators within the EU are required to implement and comply with those European Commission directives that are relevant to the financial sector. The UK's FSA estimates, for example, that 70% of its policy work is driven by Commission requirements. Even Norway, through its membership of the EEA, is obliged to conform to Commission norms. There was no evidence from our research of financial services regulation in any of the EU comparator countries being differently structured or implemented in relation to EU directives. To that extent, therefore, EU influence is a neutral factor in benchmarking the countries covered.

Changes to remit

The most regularly quoted reason for a change in any of the financial regulators' remit was a change in EU policy—all EU members and Norway are obliged to implement these. In most countries, any further changes require amendments to the underlying legislation that established the regulator. There is therefore a degree of parliamentary control and discretion over such changes, which in turn gives some degree of formal control and public accountability over remit changes. In practice of course, and this was highlighted in most countries, it is the relevant minister who has the power to propose legislative changes to parliament.

Lines of accountability

A frequently expressed concern about all regulators, not just in Ireland and not just in financial services, is over the extent to which they are truly accountable to government and parliament. In Chapter 3 we highlighted the need to combine operational independence with clear lines of accountability. These issues were explored in the international research and some clear similarities and differences in practice emerged.

The most obvious similarity was that whatever the legal status of the regulator, there was a clear line of accountability to a government minister, usually in the finance ministry or equivalent. This took a number of forms. In the Scandinavian model, for example, it involved a direct line of reporting to the minister of the department in which the regulator was located. However, in the other countries it was also clear that ministers had substantial, effective control over matters such as legal frameworks, corporate governance, board appointments and performance appraisal.

The pattern of accountability to parliament was more varied. In most cases, this line of accountability was largely exercised through the relevant minister. Any direct reporting to parliament was of a more mechanical nature, for example the submission of annual reports. The clearest exception to this was in the UK,

where the FSA is called to give evidence at least annually and often more frequently to the Treasury Select Committee. This is one of the more powerful government committees. It is backed by research resources and can be a challenging medium of scrutiny. There is a clear sense that the FSA needs to be "at the top of its game" when called before the Committee.

Given the direct and indirect power of ministers to influence or direct the remit of the regulators, a strong line of accountability to parliament is an important counter-balance. It can offer some control over ministerial interference and is also more publicly accountable. It can only be effective, however, if the relevant committee has the resources and knowledge properly to scrutinise the work of the regulator.

Another aspect of governance and accountability that emerged in the research was the use of separate scrutiny and advisory panels. In both Ireland and the UK, there are two independent panels covering industry and consumer interests, respectively. Their members are appointed by the responsible minister and they are there to advise and comment on the regulator's work. In Germany there is an administrative council of industry representatives to assess BaFin's work. In Denmark, the minister appoints three independent councils covering different sectors of the industry to oversee the work of DFSA. In Denmark's case the line of accountability to these councils is an especially strong one, countervailing to some extent the direct line of reporting to the minister. Where such panels or councils exist, and operate effectively, they do make an important contribution to regulatory accountability.

Performance evaluation

We found considerable variation in the extent and formality of performance evaluation among the financial regulators. The most detailed approach that we identified was in the UK. An evaluation system introduced in September 2006 is based on the FSA's core objectives, combines high-level outcome measures with activity and process measures (such as service standards), and also combines detailed quantitative metrics with more qualitative assessments (with the latter considered more important). In the Netherlands, the AFM similarly has a mix of quantitative and qualitative measures of outcomes, activities and processes. It also undertakes a regular survey of stakeholder feedback. The DFSA in Denmark agrees an annual performance contract with the minister. In Australia, the APRA is required to report annually on the prudential performance of the institutions that it regulates. At the other extreme, the German regulator has no quantitative or publicly available performance measurement process and there is no formal system of measurement in Luxembourg.

It is hard to see how governance and accountability of regulation can be properly exercised without a formal, systematic approach to performance evaluation. The British approach is the most detailed one that we identified, although it is too early in its application to judge how effective it has been.

Appeals procedures

In all the countries examined it was possible ultimately for decisions of the financial regulator to be appealed against to the courts and for decision-making processes to be subject to judicial review. There were variations in what intermediate stages of appeal were possible before going to court, for example

by appealing initially to the relevant minister or to an independent commissioner. The extent of appeals made varied widely. For example, in Norway no appeals against regulator decisions have been made in the last five years, while over the same period in Denmark 53 appeals have been made. This is unlikely to be explained by the Danes being more prone to questioning decisions than the Norwegians—it is more likely to reflect differences in the cost or accessibility of the appeals process.

Impact on regulated business

Regulation of the financial sector does not fit the conventional definition of economic regulation. With markets mostly fully liberalised, certainly in the countries covered in this review, the usual case for regulation—to supervise the commercial operations of a relatively small number of firms and to create or mimic competitive market conditions—does not apply. There are some exceptions to this, not least in Ireland itself with the Financial Regulator's responsibility to regulate bank charges to safeguard the interests of consumers.

In this sector regulation is more usually concerned with prudential regulation to ensure adequate levels of liquidity and solvency within the financial system. It is also concerned with operational regulation of businesses within the sector, for example to ensure fair trading practices and protect consumer interests.

There are important differences in both the overall policy towards financial regulation in the countries covered and in the operational details of how regulation works. With regard to overall policy, the UK and Luxembourg have adopted a "light touch" approach. The FSA in the UK, for example, sets the principles that it expects companies to operate within, rather than laying out detailed rules. It takes a risk-based approach, prioritising potential risks and intervening only where the benefits of doing so will outweigh the costs. This approach is considered to have enabled the UK, and London in particular, to build and maintain its position as Europe's premier financial hub. Luxembourg similarly has adopted a light touch, with the specific intention of building an international financial sector on a scale way beyond that which its domestic market could ever sustain—there are financial businesses from over 50 countries operating in Luxembourg. While both countries have had demonstrable success in growing their financial sectors—an objective shared by Ireland—the current turmoil in financial markets will change the overall philosophy of regulation, and as indicated earlier there is likely to be a shift towards more tightly enforced regulation[11].

In terms of operational detail, there are variations in the powers available to financial regulators to impose fines and penalties. In the UK, Netherlands, Spain and Norway, the regulators can impose fines. The FSA, for example, imposed 26 such fines during January-August 2008, averaging around €570,000 each. In other countries, Denmark and Germany for example, the regulator has no power to impose fines, a sanction reserved to the courts. In Australia, the

[11] While "light-touch" regulation may help to attract international financial businesses, regulatory credibility is also an important element in developing a strong financial services industry.

APRA's principal sanction is to disqualify individuals who breach the regulations. There have been around 120 cases in the five years to June 2007.

Impact on consumers

As with the impact on industry and business, financial regulation in the countries covered has less of a role in creating a competitive environment on consumers' behalf than is the case with utility regulators. In some cases, however, the regulators do take an explicit interest in consumer protection both directly and through co-operation with their national competition authority or consumer council. The latter is particularly the case in Denmark and Norway. A distinguishing feature of the Irish approach is the Financial Regulator's investment in providing information to consumers. Feedback from research respondents within Ireland on how the Financial Regulator exercises this role has been positive and we have not seen evidence from elsewhere of it being pursued as effectively as in Ireland. There is, of course, a question about whether this is a role for the regulator or for the competition or consumer authorities, but it is certainly regarded as a priority role for the Financial Regulator.

7. Energy

The Commission for Energy Regulation (CER) is the independent statutory body responsible for regulation of the electricity and gas industries in Ireland. In addition to its economic regulation functions it has a number of additional responsibilities. For example, it has recently been assigned responsibility for safety in the electricity and gas sector as well as for regulating and approving electrical contractors and gas fitters.

Policy context

The energy market (and therefore those who regulate it) is facing major challenges at present. Current issues include import dependence, climate change, the economic and social effects of volatile energy prices and the large investment requirement of network utilities. These are all placing new demands on companies and regulators alike. Strong policy drives are underway in the EU to increase the production of renewable energy, to achieve the completion of the internal energy market, reduce carbon dioxide (CO_2) emissions and make the EU more energy-efficient. Concerns about security of supply have also led to a greater focus on relations with supplier countries. The European Commission's package of proposals on the third internal market include provision to increase the powers of national energy regulators, establish a common set of functions and powers, and improve co-operation between the national regulators.

The unprecedented increases in global energy prices witnessed over the past year have also brought increased public scrutiny on the energy regulatory framework. While the global oil price has, at time of writing, declined sharply once more, public concern has been voiced surrounding the degree of effective competition among the main suppliers. Regulatory authorities are having to account to their governments for spiralling energy costs at a time of economic downturn. This challenging environment will probably test the independence of energy regulators as governments look for ways to ease the burden on consumers of rising gas and electricity costs.

In addition to their economic regulatory functions, most energy regulators in our international survey have varying combinations of wider responsibilities covering areas such as security of supply, consumer protection, reduction in CO_2 emission and encouragement for the renewable energy market. The components of this mix of responsibilities vary in terms of the weight attached to them and make accurate like-for-like comparison difficult. However, few, if any of the regulators covered have a purely economic regulatory function.

Comparator countries

The comparator countries for the energy sector have been Australia, Denmark, Germany, the Netherlands, Norway, Portugal, Spain and the UK. (In the case of the UK, there is a separate regulator for Northern Ireland so for the purposes of this chapter we refer only to the position for Great Britain.) We should note here that the legal forms of the energy regulators in Australia, Germany and the Netherlands are especially interesting, with varying combinations of links to the competition authorities and to other sectoral regulators. A summary of the regulatory structures in each country is provided below.

Australia The Australian Energy Regulator (AER) is a federal body responsible for economic regulation and for compliance with electricity and gas laws and rules. It is located within the Australian Competition and Consumer Commission (ACCC), although is a legal entity in its own right. An ACCC commission member sits on the AER board and project staff can be seconded between the two organisations. Thus, a single body, the ACCC, administers both competition law and economic regulation. The stated rationale for this arrangement was to reflect the importance of regulatory decision-making being influenced by a competitive, community welfare and economy-wide culture. Other considerations were consistency in decision-making, avoiding regulatory capture, skill synergies and administrative savings. The AER was established in 2005, following a review of energy regulatory arrangements in 2002 that recommended a move towards national energy institutions rather than the multiplicity of regional or provincial regulators that prevailed before. Its core aims are to promote efficient investment, operation and use of energy services to the long-term benefit of consumers.

Denmark The Danish Energy Regulatory Authority (DERA) is appointed by the minister for climate and energy. It was established on January 1st 2000, amalgamating the former Electricity Price Committee and the Gas & Heating Price Committee. DERA regulates across the supply chain covering production, transportation and supply by monitoring the prices and terms of supply fixed by the monopoly companies—including the terms applying to access to transmission and distribution networks. In Denmark, district heating covers more than 60% of space heating and water heating. Denmark was a pioneer in developing wind power technology and in 2007 wind power provided almost 20% of Denmark's electricity, significantly higher than any other country.

Germany Energy regulation in Germany is the responsibility of the Federal Network Agency for Electricity, Gas, Telecommunications, Post and Railway (Bundesnetzagentur, or BNetzA). Thus it sits within a "super regulator" encompassing a number of industries. BNetzA is a separate federal authority within the remit of the Ministry of Economics and Technology. Energy was incorporated in BNetzA's remit in 2005. Its regulatory responsibilities are defined in the Energy Industry Act, and involve ensuring a secure, low-priced, consumer-friendly, efficient and environmentally compatible supply of electricity and gas for society as a whole. BNetzA is also responsible for ensuring compliance with EU directives.

Great Britain

Ofgem is the regulator for the gas and electricity markets in Great Britain (with a separate regulator for Northern Ireland). Ofgem protects consumers by promoting competition where appropriate and regulating monopoly transporters of gas and electricity. Participation in electricity and gas markets requires a licence that is issued, modified, enforced or revoked by Ofgem. The UK was the first country to liberalise gas and electricity markets through privatisation, competition and open access to networks. Since the late 1990s domestic gas and electricity customers have been free to choose who supplies their gas and electricity. In 2002 Ofgem concluded that the market was sufficiently competitive to remove price controls for domestic retail customers. Ofgem has also withdrawn regulation from the metering market although the competitive practices of market players are subject to detailed monitoring by the regulator.

Recent hikes in the oil price have contributed to large increases in the price of gas and electricity in Great Britain. In response to mounting consumer and public concern over the competitiveness of the market, Ofgem launched an investigation into the energy supply market in January 2008. Publishing its findings in October 2008, Ofgem reported that the market is working well in important respects and that there was no evidence of a cartel and no evidence of prices rising by more than can be justified by wholesale costs. However, the regulator did raise the concern that competition is not yet fully effective in all sectors of the market and, as a result, some customers are doing less well out of competition.

Netherlands

The Dutch regulator, Energikamer (EK), sits within the Dutch Competition Authority, the NMa—it is described as a separate chamber within the NMa. This is a similar structure to that in Australia. The NMa has since 2005 been a separate government agency reporting to the Ministry of Economic Affairs. EK's objective is to make energy markets work as effectively as possible and involves safeguarding access to networks, maintaining sufficient transparency and protecting consumers from potential malpractice resulting from the dominant position of suppliers. It therefore evinces a strong consumer protection role alongside its economic regulatory function, reflecting its location within the NMa.

Norway

The Norwegian Water Resources and Energy Directorate (NVE) is part of the Ministry of Petroleum and Energy, and is responsible for the administration of Norway's water and energy resources. The goals of NVE are to ensure consistent and environmentally sound management of water resources, promote an efficient energy market and cost-effective energy systems, and contribute to the economic utilisation of energy. Although Norway is the third-largest exporter of gas in the world, domestic consumption of gas is negligible with hydro-electricity accounting for almost all power generation.

Portugal

The Energy Services Regulatory Authority (ERSE) is a public body provided with administrative and financial autonomy as well as its own assets. Its duties include protecting the rights and interests of consumers with regard to prices, services and quality of service. It is also required to foster the provision of clear

information to energy consumers. ERSE is independent in the exercise of its functions, within its statutory framework. In July 2002 ERSE's remit was extended to include the regulation of the gas market together with the existing regulation of electricity markets. As an emerging market, Portugal benefited from an EU derogation and only introduced the legislation for liberalisation of the gas market in 2006. The gas market is therefore in the early stages of ownership unbundling.

Spain

The National Energy Commission (CNE) is the regulatory body for Spain's energy markets and is attached to the Ministry of Industry, Tourism and Commerce. The goals of the CNE are to ensure the existence of effective competition in Spain's gas, electricity and oil markets, and to ensure that the markets work in an objective and transparent way. The CNE has two consultative boards providing advice, one for electricity and one for hydrocarbons.

Effectiveness and cost comparisons

Competition

Economic regulation of the electricity and gas sector needs to address two distinct issues:

- access charges for use of the natural monopoly transmission and distribution networks;
- prices to customers in those markets where competition is deemed inadequate.

In Ireland the household sector and a large proportion of small and medium-sized enterprises (SMEs) remain effectively dependent on the Electricity Supply Board (ESB) for electricity supplies. Despite the full opening of the market to competition, to date no suppliers have sought to supply domestic consumers or very small businesses. In contrast, there is a high degree of competition in the markets for medium and large industrial electricity users with several competing players. A broadly similar situation applies in the gas market. Again, there is considerable competition in the market to supply medium- and large-scale gas users. However, there is little competition in the market for supplying small-scale gas users—both business and households—with the state-owned Bord Gais (BGE) still having a virtual monopoly in this area[1].

The CER has decided that it is no longer necessary to regulate gas and electricity prices to medium and large industrial users and price regulation now only applies in the case of small domestic and business customers. Rolling back regulation in markets where effective competition has developed is an appropriate and welcome response—where effective competition exists, it is more efficient than regulation.

However, given the current lack of effective competition in the gas and electricity markets for households and small firms, there is a need for continued

[1] In a number of towns in the west of Ireland, the gas supply business is operated by a private sector firm, Flogas.

regulation of the prices charged to such customers. The need for regulation of those markets may decline if effective competition emerges, although it appears unlikely that this will happen in the near future[2]. Regulation of charges and other conditions for access to the transmission and distribution networks will continue to be required[3].

Prices

The CER has been subject to a significant degree of criticism since its establishment. This has mainly arisen because of large increases in electricity and gas prices since responsibility for regulation was assigned to the CER. A number of stakeholders, particularly representatives of business and consumers, that we met in the course of preparing this report were critical of the high level of Irish energy prices. We have therefore explored this issue in some detail, comparing price trends in Ireland with other countries.

B Tuohy observed that the liberalisation process in the energy market had not been without its difficulties and its critics, and that electricity prices had increased substantially. Competition has been limited to a few large players and it was not clear if there had been many benefits to consumers as a result of industry liberalisation. The Irish Business and Employers Confederation (IBEC) claimed that the energy market was not working and that a new approach was needed to ensure security of supply at a reasonable cost[4]. The National Competition Council stated bluntly that:

"Better regulation is needed in sectors such as energy, telecoms and professional services to ensure more vigorous competition and drive down the cost of doing business in Ireland."[5]

As noted earlier, a high proportion of business firms included in the Department of the Taoiseach's "*Business Regulation Survey 2007*", identified energy regulation as a priority for government intervention. A sizeable proportion cited the cost of energy and/or its impact on their own costs as the reason why they believed such action was necessary.

The chart below illustrates trends in Irish gas and electricity prices for household customers since 1990. Gas prices to household consumers in 2007 were 82% higher than in 2002. In the case of electricity the price to households increased by 56% over the same period. The chart shows, however, that electricity and gas prices had remained largely unchanged over a period of

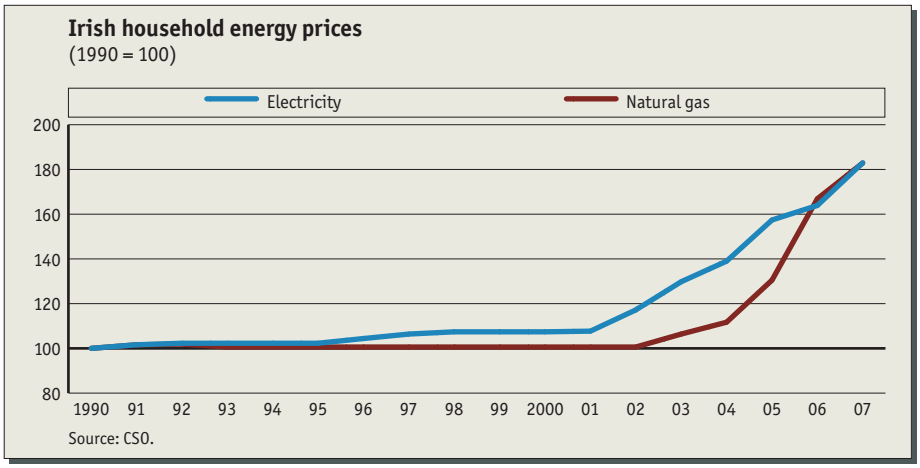
[2] The CER has indicated that some firms have expressed some interest in entering this market.

[3] In the electricity sector, responsibility for operation of the transmission system has been assigned to Eirgrid, which is independent of the ESB, the incumbent generator, although a subsidiary of the latter firm, ESB Networks, retains ownership of the grid. In the case of gas, BGE remains a vertically integrated firm. Where the incumbent firm also retains control of the transmission network it has an obvious incentive to discriminate against competitors. This makes the job of the regulator particularly difficult as it can be hard to police such behaviour effectively. However, even if the transmission system were completely separate, access charges would still need to be regulated to prevent it taking advantage of the natural monopoly, although the task of the regulator might be made easier since an independent grid operator would have no obvious incentive to discriminate between users of the grid.

[4] *Irish Times*, February 9th 2004.

[5] National Competitiveness Council, (2004): NCC Statement on Prices and Costs 2004, September 2004, p ii.

almost 12 years up to 2002[6]. During this period successive ministers had refused several ESB requests for higher electricity prices. Energy prices, particularly in the case of electricity, were thus arguably kept artificially low for more than a decade before the CER was established. This also resulted in significant underinvestment in infrastructure in electricity[7]. Such factors must obviously be borne in mind when assessing the CER's regulation of energy prices.



Cross-country comparisons indicate that Irish industrial and household electricity prices are among the highest in the euro area. Going back to 2004, for example, the National Competitiveness Council (NCC) reported that Irish industrial electricity prices were among the most expensive in the EU, while UK electricity prices were 40% lower than in Ireland for firms consuming 10 gwh[8]. A report published by Deloitte stated that Irish electricity prices were notably higher than those of other European countries. Based on international comparisons for 2004, it stated that:

"Ireland is consistently ranked among the top three most expensive countries for industrial consumers of electricity in Europe[9]*."*

Irish industrial electricity prices have increased by a further 30% since then.

Table 22 compares Irish electricity prices with average electricity prices in EU member states for different categories of industrial user. The table is taken from the Deloitte Report and the figures relate to 2004/05.

[6] While the chart only covers the period since 1990, electricity prices were unchanged throughout the 1980s so in effect prices remained flat over a 20-year period.

[7] Over the 1999-2007 period €4.9bn was invested in the network. Much of this involved necessary upgrading with 44% of lines refurbished between 2001 and 2006, while the overall length of the network increased by only a relatively small amount. See D Cagney, (2008), *Energy Regulation – Staying Within the Three Pillars,* DEW Annual Economics Policy Conference, Kenmare, mimeo. The investment programme has resulted in improved performance of the network. According to the CER, customer minutes lost have been reduced from 463 in 2002 to 194 in 2007, and verified voltage complaints have been reduced from 2,842 in 2002 to 1,496 in 2007.

[8] NCC statement on prices and costs 2004, September 2004. Ireland was the second most expensive out of ten countries for firms purchasing 10 gwh; third most expensive (out of nine countries) for firms purchasing 25 gwh and third most expensive (out of eight countries) for 70 gwh.

[9] Deloitte, Review of the Electricity Sector in Ireland, December 9th 2005, p 9. The report also found that for small domestic consumers prices are the second highest in Europe and 51% above the European average.

Table 22: Irish and EU average electricity prices for industrial customers 2004/05 (€/kwh)

Category	Ireland	EU	Ireland's Position
Small	0.1791	0.1323	**2nd highest—35% above EU average**
Medium	0.1021	0.0811	**3rd highest—26% above EU average**
Large	0.0805	0.0663	**3rd highest—21% above EU average**

Source: Deloitte.

In the case of small industrial customers, Irish prices were the second highest in the EU and were 35% above the EU average. For medium and large industrial customers, Irish electricity prices were the third highest in the EU and 26% and 21%, respectively, above the EU average. Deloitte also found that charges for the use of the electricity transmission and distribution network were above the European average, despite measures of quality for the distribution network performance being markedly below international standards.

More recent data for the EU27 shows that in January 2007 Irish household electricity prices were eighth highest in the EU, although this was in part because of taxes in Ireland being relatively low, with pre-tax Irish prices being higher than in all member states apart from Italy and Luxembourg. Industrial electricity prices in Ireland were the second highest in the EU27 in January 2007, exceeded only by Italy, while the tax-exclusive price in Ireland was the highest in the EU[10].

Similarly, a report by Sustainable Energy Ireland (SEI)[11] confirms that Irish energy prices are high compared with other EU member states. Electricity prices for Irish industry in the second half of 2007 were between 3% and 52% higher than the EU average, depending on consumption levels. For the consumption bands that most Irish industrial customers fall within, Irish prices were 23-29% higher than the EU average. The National Competitiveness Council reported that Irish industrial electricity prices were the second most expensive in the EU 15 in 2007[12].

The following tables show the situation in Ireland compared with the euro area and some individual countries—the UK, Denmark, Norway, Portugal and Spain.

Table 23: Household electricity prices €/Kwh

	2007	2007/06	2007/03	2007/EU15
EU15	0.1205	10.1%	16.3%	
UK	0.1254	29.1%	30.8%	3.9%
Denmark	0.1170	17.4%	23.5%	-3.0%
Netherlands	0.1400	16.0%	44.3%	13.9%
Norway	0.1361	23.6%	-13.2%	11.5%
Portugal	0.1420	6.0%	13.0%	15.1%
Spain	0.1004	6.8%	15.1%	-20.0%
Ireland	**0.1465**	**14%**	**45.6%**	**17.7%**

Source: Eurostat.

[10] D Cagney, (2008).

[11] Sustainable Energy Ireland, Understanding Electricity and Gas Prices in Ireland, September 2008.

[12] National Competitiveness Council: Annual Competitiveness Report, Volume 1 Benchmarking Ireland's Performance, Dublin, Forfas, January 2009.

Household electricity prices in Ireland increased by 14% during 2007 and were 17.7% above the euro area average price. Electricity prices in Ireland were therefore the highest of all the comparator countries in 2007, while Spanish prices were lowest, although as noted in Chapter 3 this was because of a government decision to reject price increases proposed by the regulator, which has resulted in the European Commission launching proceedings against Spain. Since 2003 Irish prices have also increased by the fastest rate, at 45.6%.

Table 24: Industrial electricity prices €/Kwh

	2007	2007/06	2007/03	2007/EU15
EU15	0.0837	9.27%	29.17%	
UK	0.0950	18.90%	76.25%	11.89%
Denmark	0.0638	-11.88%	-8.46%	-31.19%
Norway	0.0724	39.23%	29.29%	-15.61%
Portugal	0.0860	5.26%	27.79%	2.67%
Spain	0.0810	-1.34%	53.41%	-3.33%
Ireland	**0.1125**	**12.73%**	**47.64%**	**25.60%**

Source: Eurostat.

Industrial electricity prices in Ireland increased by 11% during 2007 and were 26% above the euro area average price. They were the highest of all the comparator countries in 2007, while Danish prices were lowest. Since 2003 UK prices have increased most, by 76%.

Table 25: Gas prices €/GJ

	2007	2007/06	2007/03	2007/EU15
EU15	12.17	17.1%	45.4%	
UK	11.20	42.8%	70.8%	-8.7%
Denmark	13.64	3.5%	63.8%	10.8%
Netherlands	12.30	10.9%	50.6%	1.1%
Portugal	13.22	-4.4%	4.1%	7.9%
Spain	12.27	4.4%	17.7%	0.8%
Ireland	**14.74**	**33.8%**	**102.8%**	**17.4%**

Source: Eurostat.

Note: No gas market in Norway.

Gas prices in Ireland increased by 33.8% in 2007 and were 17.4% above the euro area average price. Gas prices in Ireland were therefore the highest of all the comparator countries in 2007, while UK prices were lowest. Since 2003 Irish prices have also increased the most rapidly, at 102.8%. There are no Eurostat data for industrial gas prices in Ireland over this period. However, the Energy Green Paper noted that between 2000 and 2004 gas prices to Irish industrial consumers increased by 100%[13]. SEI also found that gas prices for industrial customers were above the EU average in all cases except for the biggest users of gas. It also noted that prices were significantly higher than in the UK although both countries are part of the same regional market. It offers a number of possible explanations for this, but no definitive conclusions.

[13] Energy Green Paper, p 36. In contrast, prices to domestic consumers increased by 29% over the same period.

"This may be due to the size of the gas market in each jurisdiction and economies of scale and possible currency exchange-rate anomalies."[14]

While the rise in energy prices since 2002 can at least partly be explained by the failure to increase prices over the previous 20 years, that failure does not explain why Irish energy prices are higher than in most other EU member states in absolute terms. A primary objective of economic regulation is to prevent a dominant producer from exploiting consumers by charging excessive prices. Regulation attempts to ensure that prices would not exceed those that might be expected to result from a competitive market. Consequently, evidence that energy prices in Ireland are high by international standards raises potential questions about the effectiveness of the regulatory regime in the absence of some alternative explanation for such high prices. The regulator's job is not to set artificially low prices, but to ensure that customers are not paying more than they would in a competitive market[15].

The Republic of Ireland clearly has an electricity market that is relatively small by international standards, although Deloitte dismissed claims that it was too small for the development of an effective, competitive market[16]. To some degree that debate has been overtaken by events, with the establishment of a single electricity market (SEM) for the island of Ireland.

Deloitte reported that the fuel mix of installed generating plants in the Republic of Ireland was the principal factor in Ireland's high generation costs and that fuel mix alone accounted for 70% of the differential between Irish and European generation costs[17]. More recent analysis confirms that 70% of the price differential in the case of Ireland is the result of the fuel mix of generating plants[18].

While fuel mix explains a significant part of higher electricity prices in Ireland, it is clearly not the only factor. Table 26 provides some comparative data on electricity-generation costs. The table shows that overall generation costs in 2005 were 44% above the EU average and 29% higher than in the UK. Fuel costs were 73% above the EU average, while non-fuel costs were 27% higher than the EU average and 33% higher than in the UK.

Table 26: Generation costs (excluding capital charges), 2005 (€/mwh)

	Ireland	UK	EU15	% difference Ireland versus EU15
Average fuel cost	27.57	21.69	18.37	+73
Non fuel cost	14.22	10.66	10.73	+27
Total	**41.79**	**32.35**	**29.10**	**+44**

Source: ESBI, Summary Comparison of Irish and European Generation Costs, June 2005, cited in Deloitte, p 226.

[14] Sustainable Energy Ireland, (2008), p 20.

[15] Competitive markets result in prices that reflect the underlying costs of production.

[16] Installed conventional generation capacity in 2008 was 7,577 mw, with peak demand of 5,085 mw.

[17] They point out that fuel mix is controllable, but only in the medium to longer term.

[18] Cagney, (2008), citing International Energy Agency, *Ireland 2007 Review*, Paris, OECD.

Deloitte, for example, reported that:

"Detailed benchmarking of the generation, transmission and distribution businesses of the ESB reveals that there is excess cost, poor availability performance and outdated working practices remaining in the business, which contribute to higher costs."[19]

Deloitte also reported that labour costs in ESB's power plants were 20-30% higher than in EU comparator countries. They also reported that ESB's power stations experienced poor availability, with an average of 80%, compared with 90% elsewhere. According to Deloitte these factors added €100m to Irish generation costs[20]. ESB's cost of capital was found to be low by EU standards[21].

Unit costs of gas transmission were reported to be three times the corresponding charges in Great Britain, while distribution and meter reading unit costs were respectively two and half times and twice the level of those in Britain.

The evidence shows that Irish energy prices are higher than in other EU member states. In the case of electricity, a substantial part of this differential—up to 70%—is explained by the fuel mix of generating plants. At the same time, the evidence suggests that inefficiency has contributed to a significant extent to higher Irish electricity prices.

"Electricity prices remain high in comparison with other EU countries and third countries with similar small markets. Higher input costs and low availability of power-generation plants contribute to higher production costs."[22]

The latest NCC report on competitiveness acknowledges that Ireland's generating fuel-mix is one of the major reasons for the uncompetitive level of Irish electricity prices, but also identifies low levels of spare generation capacity, poor availability of generation plants and limited competition in generation and supply as contributing to Ireland's high electricity costs[23].

In order to address the high cost of electricity it was decided to establish the SEM, which commenced operations in November 2007. A cost-benefit analysis of the impact of the SEM undertaken prior to its establishment suggested that it would lead to a marginal fall in end-user prices[24].

Regulatory practices

While Irish electricity prices are relatively high by international standards, a significant proportion of this is because of an adverse fuel mix. Nevertheless,

[19] Deloitte, p 85.

[20] If such inefficiencies had been reduced in the period since 2005, one might have expected that the proportion of the price differential relative to other EU states accounted for by the fuel mix of generating plants would have increased, but as noted the International Energy Agency data cited by Cagney above suggests that it has remained at 70%.

[21] Deloitte, p 74.

[22] Department of Communications, Marine and Natural Resources, *Energy White Paper: Delivering A Sustainable Energy Framework for Ireland—The Energy Policy Framework 2007-20,* Dublin, DCMNR, March 12th 2007.

[23] NCC, (2009).

[24] The report points out that such results are subject to considerable uncertainty as is the case with all such long-term projections. Some of the cost savings are assumed to arise from arrangements within the SEM which are designed to provide ESB Power Generation with incentives to increase plant availability. NERA: A Cost-Benefit Study of the Single Electricity Market A Final Report for NIAER and CER, November 30th 2006.

the evidence suggests that a significant proportion of the excess costs is a result of inefficiency. This raises some questions about the regulatory regime. In Chapter 3 we noted that the economic literature highlighted regulators' inability to achieve first-best outcomes because of information asymmetries, which enabled the regulated firm to set prices above cost and gain a socially costly rent from its activities[25].

"Truly competitive markets do two things at once; they provide full-powered incentives (1) to hold price down to marginal cost and (2) to minimise cost. Regulation can do one or the other but not both. It must always make a trade-off because suppliers always know the market better than regulators."[26]

Thus, to some degree, the fact that prices are higher than they should be is a result of deficiencies in regulation as a mechanism for ensuring efficient prices rather than being attributable to the regulator.

"Against this backdrop of, on the one hand, political commitment to competition but on the other hand, a structure that mitigates against competitive outcomes, the regulator has faced very challenging issues in the discharge of his role."[27]

That having been said, certain aspects of the regulatory regime merit some comment. The CER has adopted a policy of reviewing gas and electricity prices annually by analysing the cost structure of the regulated firms. Such an approach seems to ignore the information asymmetry problem. It is unclear whether the regulator possesses sufficient information to decide if costs are justified or not, ie, it cannot prevent gold-plating, nor is the regulator likely to have superior information about the scope for efficiency savings. It also provides no incentives for the regulated firms to cut costs. In such circumstances prices are unlikely to differ from what an unregulated monopolist would charge. The CER has argued that it has sought to secure greater efficiencies and to reduce the costs of the electricity and gas transmission and distribution systems in the context of its five-year revenue reviews.

We also noted in Chapter 3 that setting price increases across a basket of products was seen as having significant advantages over regulating individual product prices. It simplifies the task of the regulator, while allowing regulated firms to vary individual product prices subject to an overall price constraint that is likely to promote efficiency and increase overall welfare. The CER has sought to regulate prices at a detailed level[28]. Obviously, such detailed regulation has cost implications.

The CER requested that both the ESB and BGE prepare proposals on how the electricity and gas markets should be regulated and then sought submissions on these proposals from third parties. This effectively allowed the incumbent firms

[25] See Laffont and Tirole, 1993, and Laffont, 1994.

[26] S Stoft, (2002), *Power System Economics*.

[27] Deloitte, *Review of the Electricity Sector in Ireland, Final Report,* December 9th 2005, p 15.

28 As well as the overall increases in tariffs the Commission reviewed and determined the structure of each tariff.", CER (2001).

to set the regulatory agenda and gives rise to a real risk of regulatory capture (see Chapter 2[29]).

The CER has also on occasion granted price increases greater than those sought by the ESB. It has justified this on the grounds that higher prices are required to attract new entrants to the market. This has certainly led some to question the merits of introducing competition if it is likely to result in higher prices. As noted earlier, regulatory commitment and credibility is vital for entry in markets such as electricity generation, ie, potential entrants must be convinced that the regulator will not change the rules once they have entered the market. A regime that involves annual price reviews would appear to lack credibility.

Competition

The Irish government has stated that it is committed to opening up the electricity and gas markets to competition.

"The government is committed to ensuring that real competition is delivered in Irish electricity and gas markets."[30]

The CER states on its website that:

"The Commission for Energy Regulation (CER) is the independent body responsible for overseeing the liberalisation of Ireland's energy sector."

Progress to date in introducing competition has been relatively slow at the domestic and small industrial and commercial (I&C) level. However, resonable progress has been made at the medium and large I&C level. The industrial electricity market has gradually been opened up to competition on a phased basis, beginning in February 2000[31]. The market was fully opened to competition in 2005. There are currently six entities (including two ESB entities) active in the industrial and commercial supply market. ESB Customer Supply is the regulated public electricity supplier (PES) and is the supplier of last resort. ESB Independent Energy (ESBIE) is a wholly owned subsidiary of the ESB. The other suppliers include the state-owned BGE, Energia (a wholly owned subsidiary of Viridian Power & Energy), Airtricity and CHPower.

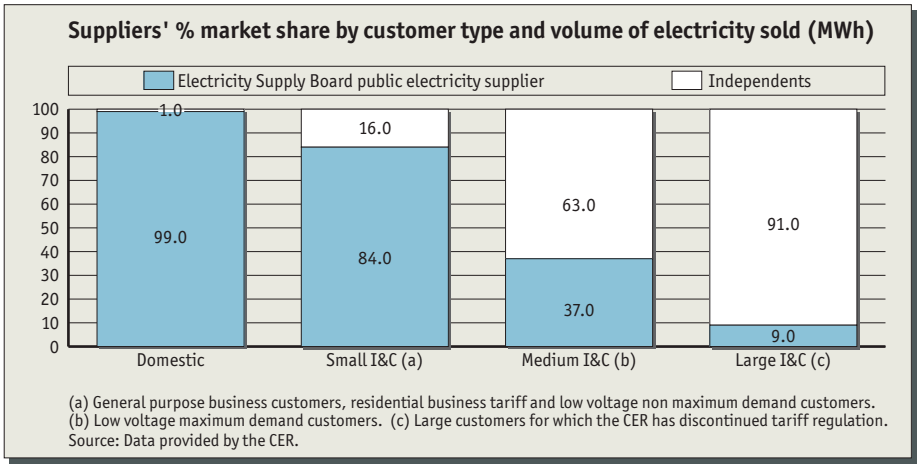
The chart below provides some details of suppliers' market share by customer type[32]. The chart shows that the ESB PES provides 99% of all electricity to domestic customers and 84% of all electricity to small I&C customers.. In the market for medium I&C customers, independent suppliers have managed to gain a 63% market share. In the market for large I&C customers independent suppliers dominate the market with 91% market share.

[29] See, for example, CER: *End to End Regulation of ESB,* January 2004.

[30] Department of Communications, Marine and Natural Resources, *Towards a Sustainable Energy Future for Ireland,* DCMNR, October 1st 2006.

[31] EU directive 96/62 required member states to open up 28% of their markets to competition with effect from February 1998, but the Irish government obtained a derogation delaying this for two years.

[32] The chart relates to both business and household customers.



To date there has been limited new entry in electricity generation, a situation that compares poorly with many of the comparator countries, for example Australia, Denmark and Norway. As a result, the ESB still controls the bulk of generation assets. More significantly it controls the bulk of price-setting plants.

In fairness, the CER has taken steps to try and promote greater competition in the market. The entry of firms into the supply market was facilitated in the past by an auction system that allowed firms to bid for electricity from the ESB, thus allowing them to build a customer base in advance of building power stations. The CER also required the ESB to divest around 1500 mw of capacity in return for approval of the development of a new gas-fired generation plant at Aghada.

The government of the Republic of Ireland and the Northern Ireland Executive agreed to establish the SEM. The CER and its counterpart in Northern Ireland have overseen the establishment of the SEM, which came into being in 2007. The development of the SEM should, at least in theory, also increase the level of competition in the market. Since the establishment of the SEM some new firms have entered the generation market with Endesa purchasing a number of generating plants from ESB and Scottish and Southern acquiring Airtricity. There are some indications that the establishment of the SEM may prompt further market entry. As noted, it was estimated that the SEM would lead to a marginal fall in electricity prices. D McIldoon, however, has argued that the SEM needs to be reformed if customers are to benefit[33].

Several reports, however, have highlighted the fact that, in the absence of significant structural reforms, the SEM is likely to give rise to a duopoly. The divestments that the CER has imposed on the ESB fall significantly short of what such reports have indicated is required in order to develop effective competition within the SEM[34]. Mechanisms have been put in place within the SEM to prevent ESB Power Generation from exploiting its market power, although, as with any such arrangements, whether they will prove effective

[33] He argues that electricity prices in the SEM are higher than they need to be. D. McIldoon, (2008), Northern Ireland Electricity Consumers—Orphans in the Storm.

[34] See, for example, D McIldoon, (1999), The Single Energy Market in Ireland, *Irish Banking Review,* winter: 2-10; IPA Energy Consulting, PB Power Ltd and Energy Links Consultancy, *Final Report on North/South Energy* Studies, August 2001; Deloitte (2006).

over time remains to be seen. The issue of wider structural reform is a matter for the government rather than the regulator. We simply wish to point out that, without more competition, electricity prices are likely to remain higher than they otherwise would and that the best efforts of regulators are likely to be insufficient to prevent Irish business and households having to pay higher prices for electricity than would be the case in a more competitive market.

Scottish experience prior to the establishment of an SEM for Great Britain may serve to illustrate the point. Historically, capacity constraints meant that the Scottish market was separate to the rest of Britain. Following privatisation, a competitive wholesale market failed to develop in Scotland because of a structure put in place at privatisation that consisted of two vertically integrated incumbents. Previously, domestic prices were 7% lower than in England and Wales, but by 2003 they were 9% higher.

"*While the administered arrangements and yardstick incentive-based regulation have delivered significant benefits to Scottish customers, these arrangements are an imperfect substitute for effective competition.*"[35]

Security of supply

It has been suggested that in analysing the cost effectiveness of the CER, account must be taken of the fact that it is responsible for security of supply. There is evidence that competitive markets may not adequately address the issue of security of supply[36]. Thus, all regulators must, to some extent, address this issue. As highlighted earlier, concern with security of supply is not unique to the CER, but is a responsibility of most of the energy regulators that we examined in the international comparisons.

All of the comparator countries are dependent to varying degrees on energy imports of oil, gas, coal and electricity. While individual countries may be self-sufficient in one of these energy sources this does not make them immune to concern surrounding security of energy supply. The UK is an example of a country that has gone from being a net exporter of gas in 2003 to importing approximately 30% of gas demand in 2007 showing how quickly the supply position can change. Action at European level has included explicit provisions for security of supply included in EU directives on oil, gas and electricity. In addition the third legislative package on EU electricity and gas markets has proposed that individual energy regulators be given a clear mandate to co-operate with each other to ensure competitive, secure and environmentally sustainable internal electricity and gas markets.

Cost comparisons

The CER had total operating costs of €14.6m in 2007, of which €11.4m was attributable to electricity regulation and the balance to gas regulation. This is lower than most of the other regulatory agencies examined in Ireland with the exception of the Commission for Aviation Regulation (CAR) and the Commission for Taxi Regulation (CTR), both of which are much smaller bodies. Operating costs per employee amounted to €279,000 for electricity and

[35] Ofgem (2002), *The Development of British Electricity Trading and Transition Arrangements (BETTA), A Consultation Paper,* London, Ofgem, p 13.

[36] See Newbery, (2005).

€179,000 for gas. Average payroll costs per employee in 2007 amounted to €92,000 for electricity and €82,000 for gas. The following table compares average payroll costs for the CER with those of the other regulatory agencies examined.

Table 27: Difference in CER average payroll costs vis-à-vis other regulators.

	CAR	Electricity	Gas	Communications	Postal services	CTR	Fin.Reg.	HSA
Electricity	+17.1	0.0	+10.4	+2.7	+6.6	+82.9	+16.0	+21.2
Gas	+6.1	-9.5	0.0	-7.0	-3.5	+65.6	+5.1	+9.7

Average payroll costs in the CER are generally above those in the other regulatory agencies. This is particularly so in the case of electricity regulation where average payroll costs are higher and, in many cases, significantly higher than in other regulated sectors.

The next tables present our preliminary comparative data on cost-effectiveness. On the issue of like-for-like comparison, most international energy regulators have combined responsibility for electricity and gas markets and in general, the mix of functions in CER is similar to most other national energy regulators. However, there are some differences that have implications for cost comparisons. For example, although Norway is one of the largest global exporters of gas, little is actually consumed in Norway—there is therefore no gas market to regulate. Since the vast majority of electricity in Norway, though, is produced from hydropower, the NVE has an additional function as the administrator of Norway's water resources. Norway is also regionally fragmented, with over 150 regional network companies increasing the monitoring and auditing requirements.

In Spain, the regulator has the additional duty of overseeing the petroleum market. Moreover, approximately 60% of the gas consumed in Spain is in the form of liquefied natural gas (LNG). This has implications for regulation, including the need for eight transmission systems compared with one in Ireland. In Australia, energy market reform has increased the AER's responsibilities to encompass regulation of distribution network businesses, previously regulated at state level. The reform programme has stalled however, with retail markets continuing to be regulated by state and territory governments. The implementation of a single national legal framework for regulating retail market services is not now scheduled to commence until September 2009. There remain staff employed in the regional regulators and this should be considered when looking at the AER figures since they will underestimate the true costs of administering regulation nationwide. The AER has estimated the total income and staffing numbers of the regional regulators to be approximately equal to its own levels.

In some of the comparator countries, different sectoral regulators have been combined under a single legal entity, such as BNetzA in Germany. The costs and staffing levels of such entities will therefore cover more than just energy regulation and should be adjusted accordingly. However, BNetzA does not break resources down into its separate functions in gas, electricity, telecoms, post and railway regulation, therefore rendering it difficult to make comparisons with the CER. The CER also has a wider energy regulatory remit since BNetzA is not

responsible for setting retail price controls. Considering the range of sectoral functions covered and the size of the German economy, €147m seems a relatively low-cost regulatory regime. However, considering the slow pace of regulatory reform in Germany compared with the European average it would be wrong to equate low cost with effectiveness.

In the Netherlands, energy and transport regulation are administered as separate chambers within the competition authority. We have, however, been able to isolate the energy-specific costs and it is these that are used in the tables. Similarly, while the Australian regulator is also part of the competition authority, the figures used refer only to its energy-specific activities.

The following tables present comparative data on regulator costs. BnetzA does not publish data on resources specific to energy regulation. We have included its income and employment data in the tables in order to give an indication of scale, but we have not used them for comparison purposes.

Looking first at the metric for regulator income per head of population, Ireland rates as the most costly at €3.80. On this measure, the Australian regulator is least costly with a budget of only €0.66 per head of population in 2007. However according to the AER if the regional regulators are included, the figure of €0.66 would approximately double to €1.30. Ireland again is ranked lowest when assessed in terms of income per employee at €264,000. Portugal follows close behind at €224,000, which is more costly than the OECD data in Table 12 would suggest. Disregarding Australia because of its regional regulators, Denmark is least resource-intensive with a budget of €109,000 per employee.

Comparing regulator income to the wider energy sector, the CER has a budget of €1 for every €147 of gross value added in the electricity, gas and water supply sector. This is significantly more resource-intensive that the other regulators for which there are data. The Eurostat data do not cover electricity and gas supply separately from water supply for all the comparator countries. On all cost measures, Ireland is the most resource-intensive.

Table 28: Income ratios

Country	Ireland	Australia (1)	Denmark	Germany	Netherlands (3)	Norway	Portugal	Spain	GB
Regulator income, €m[37]	15.6	13.5m (A$22m)	4.0 (Drk30m)	147	11.1	7.5 (Nkr60m)	9.0	27.8	57.4 (£39m)
Regulator income per head of population, €	3.80	0.66	0.72	n/a	0.67	1.63	0.85	0.69	0.97
Regulator income per employee, €'000	264	108	109	n/a	159	170	136	132	195
Regulator income to industry income[38]	1:147	n/a	1:820	n/a	1:919	1:800	1:422	1:594	1:636

The next table compares data related to employment levels: the number of staff employed by the regulator; the rate of growth in staff numbers over the last five years; and the ratio of regulator employment to regulated industry employment.

Table 29: Employment ratios

Country	Ireland	Australia	Denmark	Germany	Netherlands	Norway	Portugal	Spain	GB
Regulator staff numbers[39]	59	125	37	2,500	70	44	66	210	295
Regulator employment growth over 5 years, %	51%	310%	n/a	n/a	n/a	n/a	n/a	21%	1%
Regulator employment to industry employment[40]	1:200	1:400[41]	1:397	n/a	1:503	1:296	1:358	1:395	1:476

Ireland employs more staff than Denmark and Norway despite having a lower population. Employment has remained stable at the British regulator over five years, which may reflect the relative maturity of the British energy market. Employment in the recently established Australian energy regulator has increased by 310% in three years. In Ireland, staff numbers have increased by 51% in the last five years. The Irish energy sector has undergone significant change during this time, in particular with the development of the all-Ireland electricity market. For every 200 employees in the energy sector in Ireland the CER employs one member of staff. The corresponding measure in the Netherlands is one regulator employee per 503 employed in the energy sector. The CER has the most employees per industry employment of all the comparator countries. In

[37] All income data sourced from 2007 annual reports except: Australia and Norway provided by regulators and the Netherlands figure represents expenditure data provided by the competition authority, NMa.

[38] Gross value added for the electricity, gas and water supply sector (Nace E) Eurostat data: Ireland 2007 €2.3bn, Denmark 2007 €3.3bn, Netherlands 2007 €10.2bn, Norway 2007 €6bn, Portugal 2006 €3.8bn, Spain 2006 €16.5bn, UK 2005 €36.5bn.

[39] Staff data sourced from 2007 annual reports except Australia and Norway provided by the regulators.

[40] Numbers employed in the electricity, gas, steam and hot water supply sectors (Nace 400) Eurostat data 2007; Ireland 11,800, Denmark 14,700, Netherlands 35,200, Norway 13,000, Portugal 23,600, Spain 82,900, UK 140,500.

[41] Australia data provided by the regulator, 50,000 employed in energy sector.

addition, the CER's expenditure on consultancy fees was significantly more than on salaries and pensions in 2007, although as explained earlier this relates to one-off resource required to develop the SEM. Data on consultancy spend are more difficult to source for the comparator regulators, but those available show it to be considerably less than spend on salaries.

It is important to emphasise that the above measures do not reflect the effectiveness of the CER. They do, however, enable comparison of cost structures and in this respect it appears that the CER is more heavily resourced than most of the comparators. The generally strong performance of the Netherlands on these measures may be some testament to the efficiency gains of having a more integrated structure. The opaqueness of the German data unfortunately does not enable us to test that elsewhere.

Governance and accountability

Legal status

The formal legal status of the energy regulators in each country are summarised in Table 30.

Table 30: Energy regulators' legal status

Country	Regulator	Legal status
Ireland	CER	Independent public agency
Australia	AER	Part of the Australian Competition and Consumer Commission
Denmark	DERA	Independent agency, with secretariat reporting to competition commission
Germany	BNetzA	Independent agency, also covering post and telecommunications
Netherlands	NMa	NMA is the Competition Authority, also regulating transport
Norway	NVE	Part of Ministry of Petroleum and Energy
Portugal	ERSE	Autonomous public agency
Spain	CNE	Separate legal entity, attached to Ministry of Industry, Tourism and Commerce
GB	Ofgem	Independent non-ministerial government agency

The table reveals considerable variety in the legal status and independence of the energy regulators. In Ireland, Great Britain and Portugal they are independent public agencies. In Norway, the regulator sits within the relevant government ministry. In Denmark, the Netherlands and Australia there are close links to the competition authority—in the case of the latter two the regulator is in fact an integral part of the authority. In the Netherlands and Germany, the regulator is organisationally linked to other sectoral regulators—transport in the case of the Netherlands and post and telecoms in Germany.

Regulation of the energy market in Great Britain has the longest history and a strong record in creating a liberalised, competitive environment. Ofgem also appears from our research to have a greater degree of independence than most of the other regulators identified. We have no basis to assume a direct correlation between the two, but independent regulation is recognised as a key success factor in creating competitive utility markets. The British experience supports that conclusion, with Ofgem widely recognised as a benchmark for energy regulation. Germany provides a useful comparator. The country has lagged behind in liberalisation of energy markets, and independent regulation was only introduced around three years ago.

EU influence

The European Commission requires each member state to have an independent regulator for the gas and electricity market. It does not, however, specify in detail what their responsibilities or structure should be. This leaves room for interpretation at country level with, for example, the regulators embedded within a government department in Denmark and elsewhere in Scandinavia. The Scandinavian regulators do emphasise the degree of operational independence that they have and this appears to satisfy the Commission's requirements.

The Commission also established ERGEG, a group representing all EU energy regulators. It is the official advisor on energy to the Commission. Its principal function is to draft implementation measures that the Commission will introduce on a mandatory basis. The ERGEG will also propose voluntary measures as an alternative to the mandatory approach.

We have no basis to say that EU governance procedures affect any member state more than another in this area. All member states have a duty to comply with EU regulations, with this extending even to Norway. We therefore see the influence of the EU on governance and accountability as a neutral factor for comparative purposes.

Changes to remit

We found no evidence of the energy regulators being subject to regular or inappropriate changes to their remit, irrespective of their individual legal structures. In Great Britain and Denmark the relevant minister has no power to instruct the regulator. Changes to Ofgem's remit can only be made through legislation, for example the Energy Act of 2004 added a new duty regarding the promotion of sustainable energy resources. In Australia, any changes to the core responsibilities of the AER also require changes to federal law as well as agreement from state ministers. In the other countries reviewed, the more direct reporting lines to ministers increase the possibility of forced changes in remit, but these were not cited as either regular or disruptive occurrences.

Lines of accountability

In all the examples covered so far, the energy regulator has a clear line of accountability to the relevant government minister. This is exercised in a number of ways, most of which are common across the comparator countries—appointment of board members, approval of budgets, submission of at least annual reports. In Great Britain, Ofgem's founding legislation established that it and the minister should have common objectives and general duties in relation to energy market policy, thus ensuring a consistency of approach without requiring direct ministerial control. In Norway, such control is more directly enforced with the minister able to approve, reject or amend individual regulatory decisions. In Denmark, the regulator is obliged to report any emerging sensitive issues to the minister. Most regulators referred to additional lines of accountability to parliament, the judiciary and government auditors, although the relationship with ministers was generally seen as the key reporting line.

Performance evaluation

Generally, there was little evidence of the energy regulators adopting robust, systematic performance-evaluation procedures. Those that did exist were

largely based on indicators identified by the regulators themselves, and most of those related to activity measures, for example on service standards, rather than to measurement of outcomes within the regulated market. In Australia, however, the AER's performance-reporting requirements fall within the ACCC's wider responsibility and are explicitly tied to the AER's core objectives in encouraging competition, ensuring access and monitoring prices. It appears there that the wider responsibilities of the competition authority have created a more explicit, outcome-related performance-monitoring system.

In Great Britain, Ofgem outlines its performance targets as part of its annual corporate plan with deliverables and indicators linked to the core objectives of: creating competition, regulating networks, European energy market liberalisation, sustainable development, reducing fuel poverty and better regulation. In Spain an annual performance plan is developed by the CNE in co-ordination with the appropriate ministry. The ministry subsequently assesses the performance of the regulator in relation to this plan. In Norway the office of the auditor-general uses performance audits to investigate specific areas under the remit of the regulator where there is a perceived risk of deficiency. In Denmark performance targets have been set for almost a decade, in dialogue between employees and management.

Appeals procedure

Of the countries reviewed so far, only Denmark has a separate board of appeals for hearing appeals against DERA decisions. There is further recourse possible through the courts beyond this board. In Great Britain, decisions on competition-related decisions can be appealed to the Competition Appeals Tribunal. In the other countries, appeals are directly through the judicial system.

Impact on regulated business

Regulators impose controls on the commercial operations of energy companies through various combinations of price, revenue and rate-of-return limits. They are continually aiming to balance the need to protect consumer interests with the need to encourage operators into the market for competition reasons by enabling a sufficiently attractive return on investment. Experience across the comparator countries has been varied. In Great Britain, Ofgem sets price controls in its regulated sectors and these are reviewed every five years. The gas market has become reasonably competitive, electricity less so. Denmark in contrast recently rated highest in an independent study examining competitive intensity in the electricity market, and third best in the gas market behind Belgium and the UK. In Norway, NVE amended its revenue-cap model in 2007 to address industry concerns that it was too restrictive to enable a reasonable rate of return.

Information from the regulators on the allowed real rate of return on capital investment has been inconsistent. This reflects a number of factors: unwillingness to provide information, the differing interpretation of cost of capital; and the differing approaches to economic regulation. Consequently, cross-country comparisons are difficult to make. The following table summarises the responses received for the energy sector.

Table 31: Current allowed real rate of return

Country	Gas	Electricity
Ireland—post-tax[42]	Transmission and distribution: 5%	Transmission and distribution: 4.9%
Great Britain—post-tax[43]	Transmission: 4.4% Distribution: 4.3%	Transmission: 4.4% Distribution: 4.8%
Denmark—Not specified if pre- or post-tax[44]	Transmission and distribution: 6.6%	Transmission and distribution: 6.6%
Netherlands—Not specified if pre- or post-tax[45]	Transmission and distribution: 5.5%	n/a
Germany*—Not specified if pre- or post-tax[46]	Transmission and distribution: 9.3%	Transmission and distribution: 9.3%
Australia**—Not specified if pre- or post-tax[47]	n/a	Transmission: 5-10% Distribution: 8-12%
Norway	No gas market	n/a
Portugal	n/a	n/a
Spain	n/a	n/a

*German data only relates to cost of equity, which is more expensive than cost of debt.

**Australian data refers to actual returns yielded rather than allowed rate of return set by regulator.

As shown in the table above, the Great British regulator, Ofgem, has set the lowest allowed rate of return for both gas and electricity. Ireland has the second-lowest allowed rate of return for both electricity and gas at 4.9% and 5%, respectively. However, the rates of return are broadly similar across Ireland, Great Britain, Denmark and the Netherlands with a lower cost of capital largely reflective of more recent price controls.

[42] Ireland data sourced from regulator website—www.cer.ie—price control documents.

[43] GB data sourced from regulator website—www.ofgem.gov.uk—price control documents.

[44] Denmark data provided by the regulator.

[45] Netherlands data provided by the regulator.

[46] German data provided by the regulator.

[47] Australian data provided by the regulator.

8. Telecommunications

ComReg is responsible for the regulation of electronic communications and postal services. It is an independent statutory body established under the Communications Regulation Act, 2002. As noted in Chapter 4, it replaced the previous regulatory body, the Office of the Director of Telecommunications Regulation (ODTR). ComReg's remit as set out in the 2002 Act includes:

- the regulation of electronic communications networks and services including fixed line, mobile-phone networks and services and broadcasting networks;
- management of radio spectrum and;
- the regulation of postal services.

ComReg is responsible for the implementation of three major acts in the arena of telecommunications, 13 in the area of wireless telegraphy and spectrum management, and numerous statutory instruments covering all three sectors. Its remit therefore involves a range of issues that go beyond the scope of pure economic regulation.

Policy context

The telecoms sector globally has been characterised by major shifts in markets, products and technology in recent years. Regulatory interventions have also played an important part in both leading and responding to market changes. These shifts have been driven by the continuous spread of broadband Internet connections and by the roll-out of new products and services that these connections make possible. These "converged" products will continue to drive the sector's growth, and range from increasingly sophisticated consumer handsets such as Apple's iPhone to ultra-light computers with high-speed web links. Rapid technological changes mean that telecoms, broadcasting and computer services have effectively evolved into a single industry. This process of convergence and the rapid pace of technological change distinguish telecoms from the other sectors covered in this report. Growth in telecoms spending is likely to outstrip GDP growth for the next four to five years, although with much stronger growth in emerging economies than developed ones. Meanwhile, the supply side of the market has been characterised by increasing levels of competition including new entrants from emerging countries with global market ambitions.

All of this poses important challenges for national regulators, including fundamental questions about their role and purpose going forward. At the very least, regulators need to be sufficiently flexible to keep pace with a rapidly changing market and technical environment—one where the market drivers and operators are increasingly global in nature. Competition has developed far more

quickly and the process of rolling back regulation is far more advanced than in the case of the other sectors that are reviewed in this report. This has led many commentators to argue that economic regulation is no longer required in the communications sector and that general competition law is sufficient[1]. Regulators in some jurisdictions have been criticised for hindering the development of competition[2].

The EU has already significantly scaled back regulation in the communications sector. Under the terms of the EU Framework Directive for Communications, ("the Framework Directive"), which came into force in July 2003, national regulatory authorities (NRAs) in the electronic communications sector may only regulate in the case of markets where competition is deemed inadequate. The Framework Directive provides that competition may only be deemed inadequate where one or more undertakings are found to enjoy significant market power (SMP). The Directive further provides that SMP should be defined as equivalent to the competition law concept of dominance[3].

This effectively means that regulators within the EU may only regulate those communications markets where one or more undertakings are shown to have a dominant position. The regulator must define a relevant market and establish whether or not one or more undertakings are dominant in that market[4]. The results of any such analysis must be submitted to the European Commission, which has published detailed guidelines to be applied by NRAs for the purpose of defining markets and establishing dominance. The Framework Directive also provides that NRAs must obtain the views of National Competition Authorities on such issues.

EU case law requires that in order to establish that two or more companies can be regarded as jointly dominant it is necessary to establish that they have tacitly colluded. Establishing tacit collusion raises a number of complex issues, not least because in some instances it can be difficult to distinguish between tacit collusion and a non-co-operative Nash equilibrium[5]. The essential point for the purposes of this report, however, is that firms cannot be considered to be jointly

[1] See, for example, M Cave, and L Prosperetti, (2001), The Future of European Communications Regulation: An Assessment of the European Commission's 1999 Communications Review in C Robinson ed., *Regulating Utilities: New Issues New Solutions*, London, Institute for Economic Affairs; R W Crandall, (2003), An End to Economic Regulation, in C Robinson ed., (2003), *Competition and Regulation in Utility Markets*, London, Institute for Economic Affairs; G Knieps, (2006), The Different Role of Mandatory Access in German Regulation of Railroads and Telecommunications, *Journal of Competition Law & Economics*, 2(1): 149-58.

[2] See, for example, P MacAvoy, (1996), *The Failure of Antitrust and Regulation to Establish Competition in Long-Distance Telephone Services*, Cambridge Ma, MIT Press; R Harris and C J Kraft, (1997), Meddling Through: Regulating Local Telephone Competition in the United States, *Journal of Economic Perspectives*, 11(4); and J G Sidak, (2004), The Failure of Good Intentions: The Collapse of American Telecommunications After Six Years of Deregulation, in C Robinson ed., (2004), *Successes and Failures in Regulating and Deregulating Utilities, Lessons from the UK, Europe and the USA*, London, Institute for Economic Affairs.

[3] The Directive identified a small number of markets that NRAs were obliged to regulate, although this number has been scaled back with 11 out of 18 markets removed in December 2007.

[4] The Framework Directive defined a limited number of markets that NRAs were required to investigate to ascertain whether or not one or more firms were dominant in those markets.

[5] In December 2004 ComReg adopted a decision to the effect that Vodafone and O2 were jointly dominant in the market for mobile access and call origination. The parties appealed against the decision and ComReg agreed to withdraw it after the first day of the appeal hearing before the Electronic Communications Appeal Panel (ECAP).

dominant on the basis of having a high combined market share, ie, the fact that there may only be a limited number of competitors in a specific market, of itself, does not constitute sufficient grounds for an NRA to regulate that market. Thus, ComReg's ability to impose regulations is severely curtailed under the EU rules, particularly where no single firm enjoys a dominant position.

Comparator countries

We are comparing Ireland with seven other countries in the telecoms chapter of the research—Australia, Denmark, Germany, the Netherlands, Norway, the UK and New Zealand. The regulatory structure in each is summarised in this chapter.

Australia The Australian Communications and Media Authority (ACMA) is responsible for the regulation of broadcasting, the Internet, telecoms, radio communications, consumer and technical matters. The ACMA was formed in 2005 as a merger of the Australian Communications Authority and the Australian Broadcasting Authority. The Australian Consumer and Competition Commission (ACCC) regulates competition in the telecoms industry. Its major functions in relation to the industry are the administration of the telecoms access regime and regulation of anti-competitive conduct. The ACCC also has responsibility for postal regulation. The Department of Broadband, Communications and the Digital Economy provides advice on all regulatory policy aspects of the telecoms, radio communications and postal sectors. Under the regulatory framework, industry self-regulation is encouraged in all areas, including access, technical standards, interconnection standards and consumer service standards. The regulators have powers to intervene if self-regulation is not working effectively in specific instances. As covered in the previous chapter, the ACCC also has responsibility for the Australian Energy Regulator (AER). In the case of the AER, however, it is a separate legal entity within the structure of the AER, while telecoms regulation is more fully integrated within the ACCC.

Denmark The industry regulator in Denmark is the National IT and Telecom Agency (NITA). It is a regulatory authority under the Danish Ministry of Science, Technology and Innovation. With regard to its role in telecoms, NITA is an independent body and the minister is precluded from intervening in the conduct of its business. Two years ago, NITA was given responsibility for defining policy in the IT and telecoms sector. This relative degree of independence from direct ministerial control reflects the government's view that the market in Denmark functions well, without a need for government-level direction. NITA also recognises that increasing technological convergence in the industry requires a legislative framework that is clear, predictable and technology-neutral. The Danish market was fully liberalised in 1996, earlier than the EU deadline for doing so, although the incumbent operator, TDC, retains the lion's share of the fixed-telephony market.

Germany In Germany, the telecoms sector is regulated by the Bundesnetzagentur (BNetzA). This is the Federal Network Agency for Electricity, Gas, Telecommunications, Post and Railway—a "super regulator" in the sense of

having integrated responsibility for a number of regulated sectors. BNetzA is a separate, federal authority within the remit of the Ministry of Economics and Technology. The integrated structure is relatively recent—the former authority for telecoms and the postal service was given responsibility for regulating electricity and gas in 2005 and then for the railway network in 2006. In 2007 additional consumer protection functions in telecoms were given to BNetzA.

Netherlands The Dutch telecoms regulator is OPTA, established in 1997. OPTA is a non-departmental agency of the Ministry of Economic Affairs, and operates as an independent regulator. It is responsible for ensuring compliance with relevant EU directives, promoting competition and ensuring choice and fair prices for consumers. It has an operating protocol with the Dutch Competition Authority, the NMa, defining their respective roles. OPTA is also responsible for regulation of the postal sector.

Norway The regulator for telecoms in Norway is the Norwegian Post and Telecommunications Authority (NPT). It is an autonomous administrative agency of the Ministry of Transport and Communications, following the Scandinavian model of regulators being part of a government ministry but operating independently. The NPT is self-financed, primarily through fees and charges. The NPT's mission includes the objective of securing end users access to high quality basic postal and telecommunications services at reasonable charges by promoting effective competition in the postal and telecoms markets.

UK Telecoms in the UK is regulated by the Office of Communications (Ofcom), established in 2002. The UK was the first EU member state to liberalise its telecoms market, in 1983, and EU regulations have in fact been developed in the light of the UK experience. Ofcom inherited the duties of five predecessor regulators and is now the combined regulator for television, radio, telecoms and wireless communications. Ofcom is funded through fees from industry for regulating broadcasting and communications networks, and a government grant. As an independent government agency, Ofcom is sponsored by the Department of Business Enterprise and Regulatory Reform and the Department of Culture Media and Sport.

New Zealand In New Zealand, regulation of the telecoms sector rests with the Commerce Commission (CC). The CC is an independent Crown entity. It was established by government statute but operates independently—it is not subject to government direction. It has overall responsibility for promoting competition and fair trading in all markets. Within that remit, it has specific regulatory responsibility for telecoms, electricity and the dairy industry. The governor-general, on the recommendation of the minister for communications, appoints a telecoms commissioner who becomes a commissioner of the CC. Thus, regulation of telecoms in New Zealand is incorporated within their competition agency, which in turn is an integrated regulator for a number of industry sectors. This degree of integration offers an interesting model for other countries, especially smaller ones.

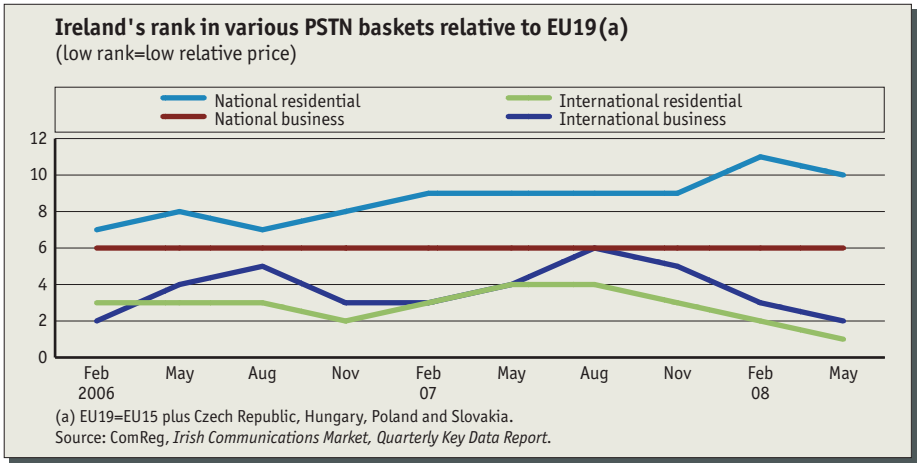
Effectiveness and cost comparisons

In assessing the question of effectiveness in telecoms regulation we consider trends in prices, the level of competition and innovation. We then examine the comparative costs of administering regulation

Pricing

Communications prices have fallen significantly while the range of services has expanded dramatically as a result of technological changes. Irish telecoms prices have fallen in real terms over the past decade while operators are reporting increased traffic and falling revenue[6]. In cross-country comparisons prices of telephony services in Ireland generally compare relatively favourably with those in other EU member states.

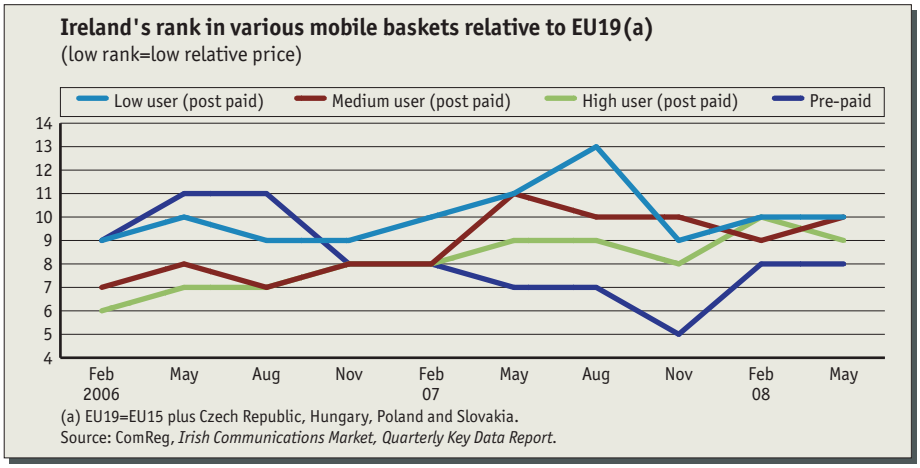
ComReg regularly publishes data compiled by the OECD that compare prices between 19 EU member states. These comparisons are based on various product baskets designed to reflect different combinations of phone usage.



Comparisons for public switched telephone network (PSTN) services show that prices in Ireland rank at the lower end of the scale in terms of international call charges for both residential and business customers, coming lowest and second lowest, respectively, in those markets in the most recent comparisons. In terms of national calls for business customers, Ireland has been ranked sixth cheapest since February 2006. Ireland's position in terms of national residential call charges slipped from seventh to 11th between February 2006 and February 2008, although Irish prices are still below the EU average.

In the case of mobile telephony Ireland again compares relatively favourably with other EU member states with rankings between eighth and tenth of the 19 countries covered depending on the particular price basket used. Ireland's relative position has varied over time in all categories, but for most of the period covered it has tended to remain in the middle of the range in most cases.

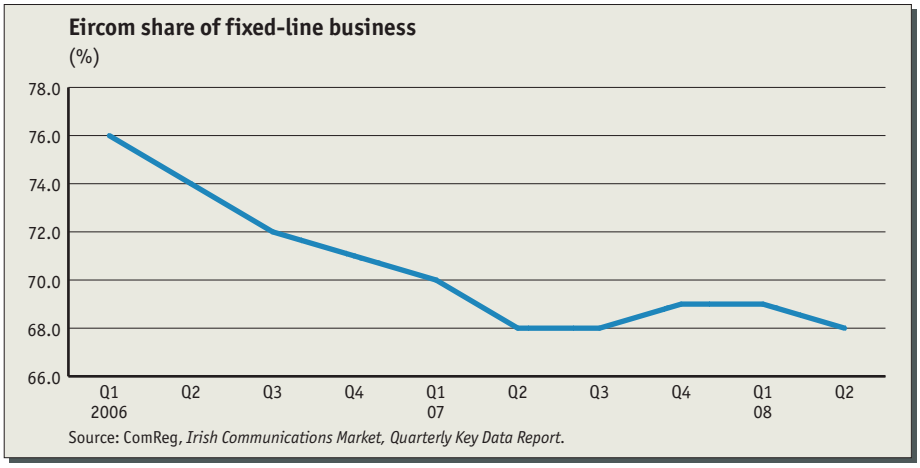
[6] A Chisholm, (2008), How Should We Evaluate Regulatory Impact in Hard Times Like Now?, *Competition,* 16(2), 47-50.



On pricing, Ireland therefore compares reasonably well with other EU member states [7].

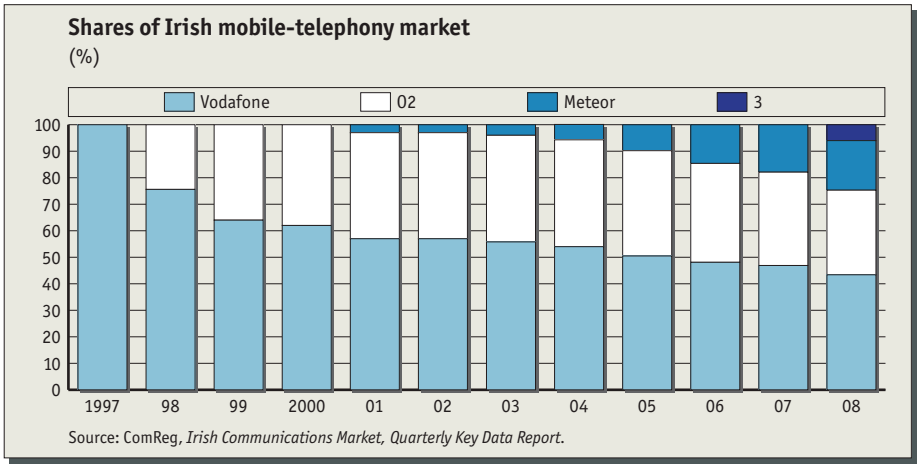
Competition

The level of competition in telephony services has increased over time. Since the market was liberalised the incumbent Eircom's market share of the fixed-line market has fallen, although it still accounted for 68% of this market in the first quarter of 2008, 8% lower than two years earlier. This figure is broadly in line with the experience in other countries.

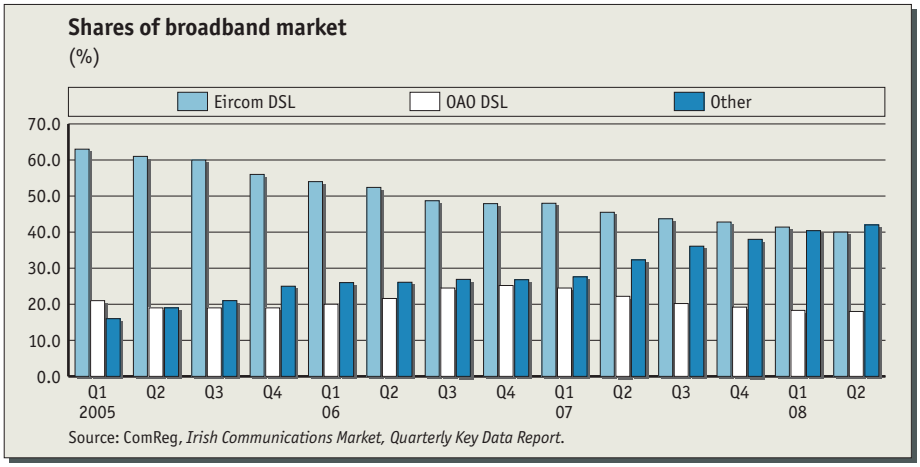


Competition in mobile telephony services has increased considerably over the past decade. A second mobile operator entered the market in 1998. Legal challenges to the award of a third licence to Meteor delayed its entry until early 2001, while a fourth operator, 3, has also entered the market. The incumbent, Vodafone (formerly Eircell), has seen its market share fall from 100% at the beginning of 1997 to 43% in the first quarter of 2008. The second operator, O2, managed to secure 40% of the market by mid-2002, but its share had fallen back to 32% by the beginning of 2008. Meteor has managed to gain 19% of the market, while 3 has secured 6%.

[7] The National Competitiveness Committee (2009) argues, however, that mobile communications costs in Ireland compare unfavourably with those in other countries.



The chart below gives details of market shares in broadband. The market share accounted for by Eircom's digital subscriber line (DSL) services has fallen sharply from 63% at the beginning of 2005 to 40% in mid-2008 with the main gains being made by providers using other non-DSL platforms including mobile broadband; their market share exceeded that of Eircom in mid-2008.



The evidence indicates that competition has developed, although again technological developments have played a significant role in that development. ComReg's role has arguably been somewhat mixed. It issued additional mobile-phone licences, which increased the number of firms in that sector from two to four. Decisions such as the requirement for full mobile number portability probably contributed to the successful expansion of Meteor in the mobile-phone market[8]. At the same time it sought to retain regulation in mobile telephony by arguing that Vodafone and O2 were jointly dominant in the market, claiming, *inter alia*, that Meteor and 3 would not exercise a competitive constraint over the two larger operators. In just over three years since that decision, which was annulled, Meteor and 3 have gained a significant share of

[8] Meteor entered the market at a time when mobile penetration levels were relatively high, so in order to grow market share it had to attract customers of the two incumbent operators. Ireland requires portability to be effected within two hours. Chisholm (2008) cites research indicating that this reduced average prices by around 8-9% in the short-run and by 12-15% in the long-run.

the market at the expense of Vodafone and O2. This illustrates the point that in a rapidly developing area like communications a cautious approach to regulation may be appropriate.

Innovation and product development

ComReg has adopted a number of measures designed to foster innovation and these have had positive impacts in terns of competition and consumer welfare. The Fixed Wireless Access Local Area (FWALA) scheme accounted for a year-on-year increase in subscribers of 17.4% between the second quarter of 2007 the second quarter of 2008[9]. ComReg has issued 226 FWALA licences to 16 different operators, which are providing broadband services to over 121,000 customers (corporate, small and medium-sized enterprises and residential) across Ireland. These account for 14% of broadband subscriptions excluding mobile broadband. All FWALA licences are issued on a low barrier and technology-neutral basis, thus encouraging innovation.

ComReg's Test and Trial Spectrum licensing scheme, which was launched in 2006, is especially designed to encourage companies to test and develop their technologies in Ireland. As of July 2008 ComReg had issued 42 test licences and 30 trial licences under this scheme. It has been instrumental in pioneering the use of Mobile Communications on Aircraft, WiMax and mobile TV, and has been publicly praised by users such as O2, Ericsson and Vodafone as well as attracting significant international interest from other regulatory authorities.

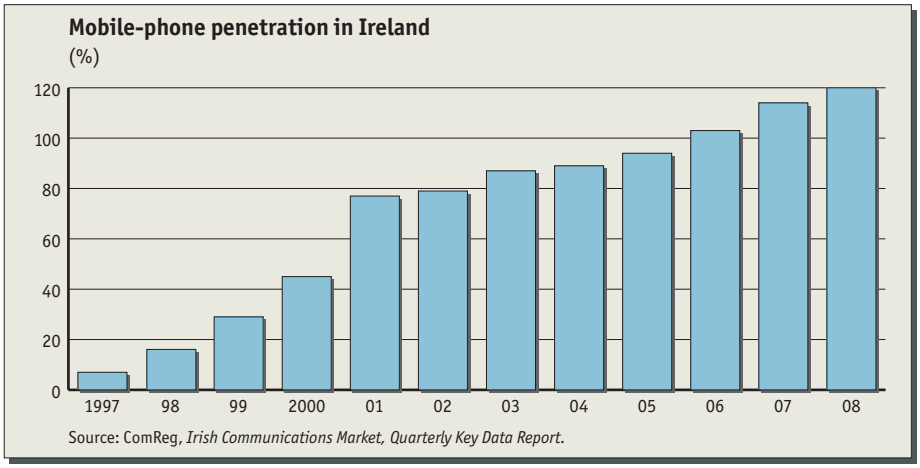
The European Commission has taken a positive view of ComReg's work. For example, the 12th Implementation Report (2006) states that:

"ComReg has adopted a pro-active approach to addressing a broad range of issues, from spectrum management to innovative services and consumer protection" ... "Many market players praised ComReg for its flexible and attractive trial licences regime. An interesting and useful initiative is the co-ordination by Ofcom (the UK national regulatory authority) and ComReg of their respective procedures in issuing spectrum authorisations covering the whole island."

Further indications of innovation are the growth in mobile-phone and broadband penetration.

The following chart illustrates the rapid growth in mobile-phone penetration in Ireland. In 1997 the level of mobile penetration—the proportion of the population with a mobile phone—was as low as 7%. It exceeded 100% in 2006 and latest figures show mobile penetration rates of 120%. This compares favourably with most other EU member states, most of which have penetration rates of between 110% and 125%, although there are a small number of cases with penetration rates both above and below this range. Nevertheless, it seems fair to say that the level of mobile-phone penetration is broadly in line with that of most EU member states.

[9] ComReg Quarterly Review (08/75) September 2008.

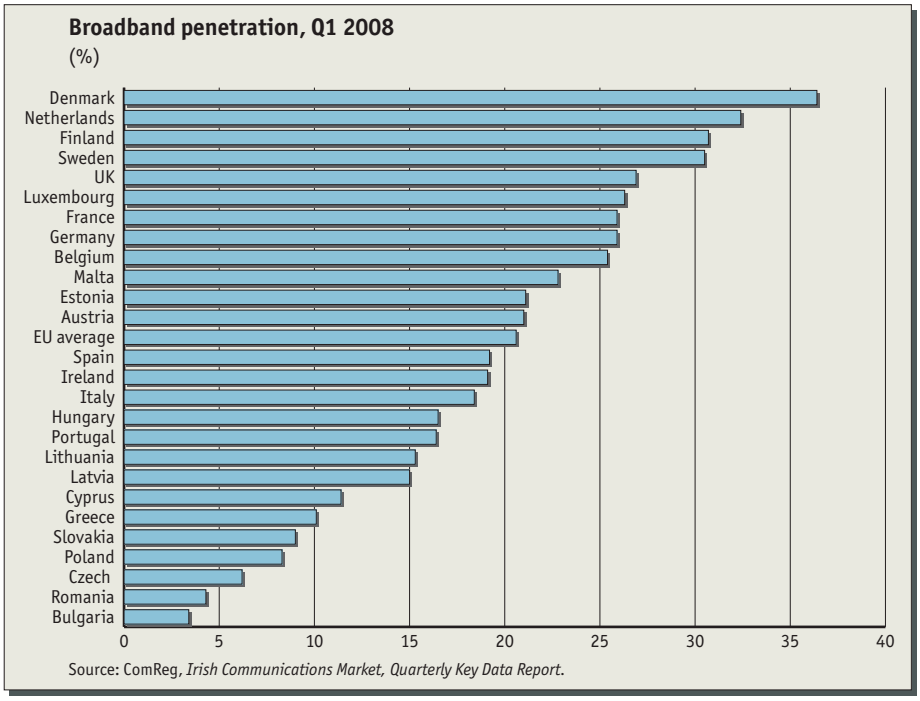


Data for the first quarter of 2008 shows that the level of broadband penetration in Ireland was just over 19%, slightly higher than Italy and just below Spain, and below the overall EU average of 20.6%[10].

Concerns have been expressed about the slow pace of broadband roll-out in Ireland. Regulators in many EU member states have sought to rely on local loop unbundling and other measures to promote service competition as a means of encouraging broadband roll-out. There are mixed views on the effectiveness of local loop unbundling as a tool to promote competition and infrastructure based investment[11].

[10] The comparisons exclude mobile broadband.

[11] P T Spiller and C G Cardilli, (1997), The Frontier of Telecommunications Deregulation: Small Countries Leading the Pack, *Journal of Economic Perspectives*, 11(4): 127-38. J Hausman and J G Sidak (2005), Did Mandatory Unbundling Achieve its Purpose? *Journal of Competition Law and Economics*, 1(11): 173-245. R Crandall and L Waverman, (2006), The Failure of Competitive Entry into Fixed Line Telecommunications: Who is at Fault?, *Journal of Competition Law and Economics*, 2(1):113-48. The former study examined experience in the US, Canada, Germany, the UK and New Zealand. It found that in the UK network competition rather than local loop unbundling played an important role in the development of broadband and argues that there is a serious question about whether mandatory unbundling was necessary for broadband development in the UK. According to Crandall and Waverman, apart from Germany and the UK many EU member states relied on local loop unbundling to promote broadband development. They found, however, that until relatively recently EU broadband penetration rates had been fairly low, which regulators blamed on incumbents. They conclude, however, that promoting service competition through strategies such as local loop unbundling was unsuccessful in both the EU and North America and had resulted in a substantial waste of capital.



Postal services

Liberalisation of postal services is lagging that in telecoms, with full liberalisation not scheduled until 2011. The focus of regulation for the postal service in the partly liberalised market is the maintenance of the Universal Service Obligation (USO) and ensuring that An Post (Irish postal service) prices are geared to cost.

There are indications of significant inefficiencies in the sector, with An Post consistently falling short of the service-level targets set by the regulator. Latest figures show that 80% of mail was delivered by the next working day, compared with a ComReg target of 94%. Some 98% was delivered within three working days compared with a target rate of 99.5%. The latest figures show an improvement in the next-day delivery rate from 78% three months earlier, but figures are still well below the target[12].

Adequacy of mandate

We consider the adequacy of ComReg's mandate here, as an element within the overall review of effectiveness. In 2007 ComReg's powers were expanded, enabling it to apply competition law in the communications sector concurrently with the Competition Authority. It is unclear to what extent enabling ComReg to apply competition law enhances its powers. The EU telecoms framework allows ComReg to introduce *ex ante* regulation where a firm or firms are dominant. Competition law in contrast does not prohibit the holding of a dominant position, but only prohibits the abuse of such a dominant position. In addition, in Ireland decisions on breaches of competition law, including abuse of dominance, are matters for the courts. Like the Competition Authority, where ComReg believes an undertaking has abused a dominant position, it must prove its case before the courts. Admittedly, the courts may impose substantial fines for breaches of competition law, but only following a criminal

[12] Figures taken from ComReg media release, September 4th 2008.

prosecution. Thus, it is unclear that the power to apply competition law really enhances ComReg's powers to any practical extent. In those circumstances it seems reasonable to ask whether it makes sense for ComReg to seek to replicate the Competition Authority's expertise in competition law.

ComReg has more limited regulatory powers in the case of postal services. For example, until relatively recently it has had limited powers to sanction An Post for failing to achieve quality targets, something that An Post has repeatedly failed to do. ComReg has recently been given enhanced powers to impose sanctions on An Post for poor performance. As far as pricing is concerned, An Post cannot raise prices without ComReg's approval. This tends to limit ComReg to the largely reactionary role of adjudicating on applications for price increases by An Post. This type of regulation suffers from a number of shortcomings, which have already been identified elsewhere in this report, resulting from the existence of information asymmetries, the lack of incentive for the regulated firm to reduce costs and increase efficiency, among others.

Cost comparisons

In making cost comparisons with other countries it is important to establish how ComReg's remit compares with the other regulators. ComReg is responsible for the regulation of:

- telecoms;
- radio communications;
- broadcasting; and
- the postal sector.

The Norwegian Post and Telecommunications Authority has regulatory responsibilities for the telecoms and postal sectors. Ofcom in the UK has responsibility across communications including telecoms, radio communications and broadcasting regulation. A separate agency, Postcom, regulates the UK postal network and its resources are included in our cost comparisons.

In Australia the ACMA is responsible for the regulation of telecoms, radio communications, broadcasting, the Internet and consumer and technical matters. Also in Australia the ACCC has a wide range of functions including responsibility for the economic regulation of telecoms under a framework of industry self-regulation. Regulation of the postal network is also conducted by the ACCC. The resources used for comparison are those of the ACMA since the ACCC does not provide a breakdown of its resources by activity.

In Denmark, the National IT and Telecoms Agency regulates the telecoms sector and also has responsibility for defining IT and telecoms policy. Responsibility for postal regulation rests with the Road Safety and Transport Agency and we have no breakdown of these specific resources.

In the Netherlands, OPTA regulates the electronic communications and postal sectors. Responsibility for spectrum management rests with a separate agency, Agentschap Telecom, and its resources are included in the comparisons.

In New Zealand the CC has responsibility for regulation of the telecoms sector as well as the energy and dairy sectors. The resources data that we use here refer only to their telecoms regulation activities. A separate government agency, Radio Spectrum Management, is responsible for spectrum management and its resources are included in our comparisons. The Ministry of Economic Development has responsibility for postal regulation and it has not been possible to source a breakdown of those specific resources.

In Germany, BNetzA covers gas, energy, telecoms, post and railway regulation. Since the regulator does not break down income between the various functions, cost comparisons with ComReg are not appropriate. The regulator did, however, provide the number of staff working specifically on telecoms regulation.

Ireland is therefore best matched with the Norwegian regulator in terms of functions. With the exception of postal regulation, the UK regulator is also closely comparable.

The following tables present our data on international comparison of regulator costs.

Ireland has the highest level of regulator income per head of population at €9, which is closest to Denmark at €7, but significantly higher than the other regulators. The Danish regulator, however, has a more narrowly defined remit than ComReg, not having responsibility for the postal sector. New Zealand has the same population as Ireland, but a far lower regulator income at €2.30 per head. Again, the New Zealand regulator has fewer functions to discharge than ComReg, not having responsibility for postal regulation. Norway is a good comparator in terms of country size and regulator functions, and has approximately half the resources of ComReg on this measure. Australia is relatively low cost on this measure at €2.40 per head of population.

Table 32: Income ratios, 2007

Country	Ireland incl post	Australia	Denmark	Germany	Netherlands incl post	Norway incl post	New Zealand	UK
Regulator income, €m[13]	*36.7	49.1 (A$80m)	38.3 (Dkr285m)	**147	***43.8	22.4 (Nkr179m)	****9.5 (NZ$17.6m)	*****222.4 (£151.2m)
Regulator income per head of population, €	9.0	2.4	7.0	n/a	2.6	4.9	2.3	3.7
Regulator income per employee, €'000	334	98	136	n/a	111	147	164	253
Regulator income to industry income[14]	1:112	[15]1:447	1:141	n/a	1:278	[16]1:223	[17]1:307	1:301

* ComReg data does not include €52m spectrum income that is payable to a central fund.

** Income figure covers energy, telecoms, post and railway regulators.

*** Includes income of the communications regulator, OPTA (€16.8m), and the radio communications agency, Agentschap, (€27m).

**** Includes income of the communications regulation department of the CC (NZ$8m) and the total expenses of the radio spectrum management agency (NZ$9.6m).

***** Includes income from the postal regulator, Postcom.

Measuring costs by income per employee also puts Ireland as the most resource intensive at €334,000 per employee. This is over three times more income per employee than the Australian regulator, albeit that the latter does not regulate the postal sector and we do not have the relevant figures for that sector. The UK is closest to Ireland on this measure with an income per employee of €253,000. The Netherlands has approximately one-third of the resources of ComReg on this measure. The final efficiency measure again scores Ireland poorly, with a budget of €1 for every €112 of industry income, which is closest to Denmark, at €1 for every €141 of industry income. This contrasts with New Zealand and Australia, where the regulators' income is respectively 307 and 447 times less than the industry income. On all income measures, therefore, Ireland is the most resource-intensive. The data is in line with the OECD comparative price index in Table 12, where Scandinavian countries and Ireland are the most expensive.

In contrast with the comparator regulators, ComReg's income far exceeds its expenditure, with non-spectrum net income of €35.5m and total expenditure of €19m in 2007. The balance of income over expenditure is payable to a central fund. The large discrepancy between income and expenditure may not accurately reflect the true cost of running the regulator. For this reason, it may be more appropriate to look at expenditure instead of income for ComReg. On this measure, ComReg's expenditure per head of population is €4.7, which is similar to Norway and considerably lower than Denmark. However, ComReg

[13] Income data sourced from 2007 annual reports except New Zealand data provided by regulator.

[14] Turnover of the telecommunications sector: European Commission, 13th progress report 2006: Ireland €4.1bn; Denmark €5.4bn; the Netherlands €12.2bn; UK €67.1bn.

[15] Australian sector income data provided by regulator: 2005, A$35.8bn.

[16] Norwegian sector income data provided by regulator: 2007, €5bn.

[17] New Zealand sector income data provided by regulator: 2007, NZ$5.4bn,

remains relatively resource-intensive compared with the other regulators. ComReg expenditure per employee is €174,000, which is significantly lower than the UK and comparable with New Zealand. ComReg's expenditure to industry income at €1:214 is less resource-intensive than Denmark and similar to Norway, but higher than the other regulators.

Table 33 compares data related to employment levels: the number of staff employed by the regulator; the rate of growth in staff numbers over the last five years; and the ratio of regulator employment to regulated industry employment.

The number of staff at the Irish regulator increased by 6% between 2004 and 2007. The UK has witnessed a 12% increase in staff numbers since 2003, similar to Denmark's increase, while the Netherlands has reduced its number of employees by 17% and Norway reported a slight decline in numbers. Historical employee numbers have not been forthcoming from the New Zealand, Australian or German regulators.

For the purposes of comparability and standardisation, industry employment includes postal sector workers, in accordance with Eurostat data. The Netherlands, UK and Norway are therefore the best comparators. ComReg compares favourably with Norway and Australia, with far fewer regulator employees to industry employees. However, ComReg is significantly more resource-intensive than the UK communications and postal regulators and is also more resource-intensive than the Dutch regulator on this measure. Neither New Zealand nor Australia has a postal regulation function and yet they represent the opposite extremes in staff numbers. With one employee for every 345 industry employees, ComReg is approximately the median result.

Table 33: Employment ratios

Country	Ireland	Australia	Denmark	Germany	Netherlands	New Zealand	Norway	UK
Regulator staff numbers[18]	110	500	282	450	*394	**58	152	***878
Regulator employment growth over 5 years	6% (2004-07)	n/a	11%	n/a	-17%	n/a	Slight decline	12%
Regulator employment to industry employment[19]	1:345	[20]1:150	1:188	1:1244	1:393	1:620	[21]1:225	1:615

* Includes staff from the communications regulator, OPTA (122), and the radio communications agency Agentschap Telecoms (272).

**Includes staff from within the communications regulation department within the CC (22), and the radio spectrum management agency within the Ministry of Economic Development (36).

*** Includes staff from the communications regulator Ofcom (812), and the postal regulator Postcom (66).

[18] Staff data sourced from 2007 annual reports except: Germany and New Zealand provided by the regulators.

[19] Number employed in post and telecoms sector—Eurostat data 2007: Ireland 38,000; Denmark 53,000; Germany 560,000; the Netherlands 155,000; Norway 34,000; UK 540,000.

[20] Australian communications sector employment data provided by the regulator—2005: 75,000 employees.

[21] New Zealand telecoms sector employment data provided by the regulator—2007: 36,000 employees.

Governance and accountability

Legal status

Of the countries reviewed in this chapter, only the UK and Ireland have an independent telecoms regulator, in the sense of there being a corporate body with an exclusive focus on the sector. In the Netherlands, OPTA is an autonomous body, but established as an agency within the relevant ministry. In the Scandinavian countries, the regulator is part of the responsible ministry. In New Zealand and Australia, the competition agency regulates telecoms as it does for energy. In Germany, the sector is also regulated by the same body that is responsible for energy.

Table 34: Telecommunications regulators' legal status

Country	Regulator	Legal status
Ireland	ComReg	Independent agency
Australia	ACMA	Statutory authority reporting to the federal Department of Broadband, Communications and the Digital Economy
Denmark	NITA	Agency of the Ministry of Science, Technology and Innovation
Germany	BNetzA	Independent agency, also covering energy
Netherlands	OPTA	Non-departmental agency of the Ministry of Economic Affairs
Norway	NPT	Agency of the Ministry of Transport and Communications
New Zealand	Commerce Commission	Independent competition agency, regulating a number of sectors
UK	Ofcom	Independent agency

EU influence

The European Commission plays an important role in determining regulatory requirements in the industry. Currently, for example, there are major pressures from the Commission on the charging policies of telecoms operators for call roaming and routing charges. National regulators in member states will be required to implement any directives flowing from the Commission's conclusions on these issues.

The European Competitive Telecommunications Association (ECTA) publishes a scorecard comparing the regulatory environments in 18 EU member states and Norway (EU19). It is particularly concerned with the effectiveness of regulators in promoting the objectives of the EU regulatory framework, and so is rather different in focus from this project. Its results are nevertheless of interest. The 2007 scorecard shows the UK, Netherlands, Denmark and Norway as the highest-ranking countries in terms of promoting the EU regulatory objectives. Ireland was 12th out of the 19 countries surveyed. The weaknesses identified by ECTA were not so much in the structures and procedures for regulation in Ireland, but in the outcomes achieved, for example in broadband infrastructure, mobile and business services.

Changes to remit

In New Zealand, the minister sets the overall policy for the CC, but has no powers to change its remit without legislative change. Having said that, there have been considerable changes to the CC's responsibilities towards the telecoms sector. Initially, it could only intervene if parties requested that it resolve a dispute. It can now regulate actively across the whole sector. It has also been given a broader scope to monitor the industry. These changes were prompted by a perception that the initial regime had not delivered sufficient competition in telecoms markets, and they bring the regulatory function closer

in scope to what would normally be expected elsewhere. As pointed out earlier, it has been suggested that increased regulation has had an adverse impact on the sector[22].

In Norway, the NPT's remit changes in line with legislative developments. If there were a perceived need for new powers, this would take place after a discussion in parliament. This occurred with the adoption of the legislation on electronic signatures in 2001, for example. In the UK, Ofcom has a broader remit to regulate content as well as infrastructure, reflecting its responsibility for broadcasting.

In Australia, there are tight controls over remit changes. These require the approval of both houses of parliament and therefore cannot be made directly by the executive. There have, however, been some significant changes to remit that have gone through parliament. These mostly affect the ACCC's accountability and we return to them in the next chapter. In September 2005 ACMA gained the power to accept enforceable undertakings about compliance with the 1997 and 1999 Telecommunications Acts.

Lines of accountability

The CC in New Zealand is an independent public agency, responsible to the minister for economic development. Its main accountability document is its annual report, which is provided to the minister and presented to parliament. It also makes quarterly reports to the minister. In the UK, Ofcom is a statutory corporation and is required to report annually to parliament. The Communications Act 2003 states that Ofcom is subject to inspection by the National Audit Office and is accountable to the Public Accounts Committee for propriety and value for money. While Ofcom is independent of government, secretaries of state will answer questions in parliament about Ofcom: another process of indirect accountability.

The NPT in Norway reports three times a year to the responsible ministry. This generally does not involve justifying decisions in individual cases, but is more concerned with administrative and economic/budgetary issues. It also publishes an annual report. The NPT is able to challenge government policy when appropriate. For example, it recently argued that a government objective to encourage competition in telecoms infrastructure made no sense given Norway's geography and the large number of small, remote communities—competition was more appropriately encouraged in service competition.

As indicated above, the ACCC has had some remit changes designed to improve its accountability. One is the granting of the power to demand information from regulated companies, as a means of countering the information asymmetry problem. Another is an obligation to report its pricing principles and methodology in order to increase transparency and reduce the incidence of disputes. It also now has the power to make and change its own procedural rules, a power granted to better enable it to keep pace with the rapidly changing telecoms sector. The ACMA is required to maintain a register of all directions received from the Ministry and has received six such directions in 2007, five in 2006 and one in 2005. Examples include directions to publish

[22] See Howell, (2008).

reports, investigate market developments, to provide advice to the Ministry and to consider whether to exercise its legislative powers.

In Germany, there is a direct line of accountability to parliament through an Advisory Council. This consists of 16 members of parliament from both houses. It is empowered to make recommendations on the appointment of BNetzA's president and two vice-presidents. It may request information from BNetzA at any time and offer its opinion on BNetzA activities and decisions. This appears to provide a much more direct and sector-specific line of accountability to parliament than is evident elsewhere.

In the Netherlands, OPTA has a similar three-member commission to that of ComReg. It also has a clear protocol with the Dutch competition authority, the NMa, defining respective roles and responsibilities.

Performance evaluation

Regarding performance management, Ofcom has a range of key performance indicators to measure how it is delivering its services. Together with financial performance they provide a measure of internal efficiency and effectiveness. A "simplification plan" sets out what Ofcom has already done, and plans to do, to reduce regulation. Its annual report provides information on completed, new and ongoing initiatives, and the extent to which these have reduced—or are expected to reduce—regulatory burdens by removing, reducing or simplifying regulation.

In contrast, the NPT has no performance targets other than its general mission statement. The government requires the NPT to report on its success in achieving its primary aims as defined in acts of parliament, but these are qualitative and the NPT itself considers them too vague. The NPT would prefer to have quantitative performance targets, but in the absence of these the NPT's performance is a political judgement based on discussions with the relevant ministry. Similarly, BNetzA appears to have limited performance evaluation procedures—it submits a biennial activity report to the federal government, which then informs parliament of its views. In Australia, the ACCC adopts a similar approach to performance reporting as it does in energy regulation through the AER. It is required to report on regulatory outcome-related performance, for example in ensuring fair pricing for business customers and improving the level of competition in the market. The ACMA sets a number of key performance indicators such as time limits to process licence, permit and number applications.

OPTA in the Netherlands takes a different approach to performance evaluation. It relies on the ECTA scorecard referred to earlier, as well as the European Commission's annual report on implementation of directives. Other than that, there is a formal review of all OPTA's activities on a four-yearly basis by the Ministry of Economic Affairs. OPTA also made the point that since its decisions were open to challenge in the courts, this was the ultimate judge of their performance. So there is a reliance on third party, international performance benchmarking allied to a regular fundamental review of remit and performance by the ministry.

Appeals procedures

Appeals procedures have been an especially contentious area for telecoms regulation in Ireland. An Electronic Communications Appeal Panel (ECAP) was

established in 2003. This provided for a three-person ECAP to hear and decide on appeals against decisions by ComReg. Previously, appeals against these decisions were heard only in the courts. The new approach was designed to enable appeals to be dealt with more quickly and cheaply than the courts system allows. The ECAP was quasi-judicial in nature, independent in the performance of its functions and could determine its own procedure. The ECAP was subsequently abolished in June 2007, however, with appeals against decisions by ComReg reverting back to the courts. The stated reason for its abolition was that it had proved too slow in reaching decisions.

ComReg called for the abolition of the ECAP. In response to a consultation document on regulatory appeals published by the Department of the Taoiseach, it argued that:

"The Commission for Communications Regulation (ComReg) is of the view that appeals mechanisms should be accountable, expeditious, consistent, informed and transparent. ComReg assessed the current appeals mechanism provided for by the electronic communications framework to see if it satisfied these principles and identified some areas of concern. In particular, ComReg is concerned that the current electronic communications appeals process is inappropriately slow. The overriding concern is that the delay in reaching decisions under the current appeals process has meant that it is difficult to match market, technological and other changes in the electronic communications sector and to deliver the benefits of competition to consumers."[23]

During its existence, the ECAP dealt with only two substantive cases, thus providing a somewhat limited sample on which to assess its effectiveness. In the first of these it overturned a decision by ComReg that mobile-phone operator, "3", was dominant in the market for call termination on its own network and expressed strong criticism of ComReg. In the second case, involving an appeal against a decision by ComReg that Vodafone and O2 were jointly dominant, after the first day of the appeal hearing ComReg agreed to the annulment of the decision and to pay the appellants costs—effectively, conceding that it was wrong[24]. Obviously it is important that appeals procedures operate speedily and efficiently. To the extent that appeals delay the implementation of regulatory decisions this involves some costs, assuming that the regulator's decision is upheld. Regulatory errors also impose significant costs. The lack of an effective appeals mechanism is likely to be more costly than any delays caused by appeals. Any delay resulting from an appeal is temporary, whereas bad regulatory decisions impose ongoing costs. The appeal against the award of the third mobile licence to Meteor undoubtedly took some considerable time to be resolved, and led to significant costs as it delayed the entry of a third operator, thereby limiting competition in the market. It should be noted, however, that the appeal in that case was to the courts rather than to a specialist appeals panel.

[23] ComReg, 2006, *ComReg's response to the Consultation Paper on Regulatory Appeals,* Dublin, ComReg.

[24] One of the current report's authors advised one of the appellants, Vodafone, in that case.

Looking internationally, the New Zealand CC has only had one decision on telecoms challenged since 2001. It cannot directly impose fines or penalties—these are imposed by the courts.

In Norway, decisions can be appealed to the relevant ministry. There is also a possibility of ministerial and parliamentary reviews, but this does not happen with any frequency. All decisions may be brought before the ordinary courts. This route has been tested only once, but was rejected. At present, the Ministry of Transport and Communications is the appeals body. It therefore has the power to overturn decisions, and its decisions are final. In practical terms, this has generally not been a problem—the ministry usually supports NPT decisions—but the current system is perceived to undermine the formal independence of the NPT. The NPT would itself like to see the creation of an independent appeals body. In the last five years, on average between five and ten of the NPT's decisions each year have been appealed to the ministry, which. has, by and large, confirmed them with occasional minor adjustments.

In Australia, all ACCC decisions are subject to judicial review by the Federal Court. Certain decisions can be subject to merit review by a separate competition tribunal. Certain ACMA regulatory decisions can be appealed to the Administrative Appeals Tribunal.

Impact on regulated business

As indicated above, the UK was one of the early movers in liberalising the telecoms market. The size of the telecoms sector in 2006 is estimated to have been £47bn (€53bn at current exchange rates). Of this, £38.5bn comprised retail expenditure on telecoms services, with the remaining £8.5bn consisting of wholesale activity (such as capacity provision by entities such as British Telecom, BT, for pure service providers). Ofcom has taken a much firmer line with BT than its predecessor, Oftel. Pressure from Ofcom in 2004 led BT to cut the prices that it charged rival telecoms operators for access to its last-mile copper connections to households (local loop unbundling). Ofcom also ordered BT to cut the costs of transferring the customers of Internet service providers (ISPs) to rival operators, thereby making it easier for ISPs to sever their ties with BT. In a bid to speed up local loop unbundling, Ofcom reached an agreement with BT in 2005 to create a new business unit, Openreach, to run the "last mile". Openreach is obliged to treat BT and its competitors equally.

The Norwegian telecoms market is relatively open, reflecting Norway's obligations under the European Economic Area (EEA), which extends the European single market to Norway. Foreign investors are not required to obtain government authorisation before buying limited shares of large Norwegian corporations. However, both foreign and Norwegian investors are still required to notify the government when their ownership in a large company exceeds specific threshold levels of 33%, 50%, or 67%. The government can initiate a closer examination if they believe the acquisition could have a substantial negative effect on the company, trade or the public interest. Barriers to entry—such as number portability, access rights and spectrum allocation—are

considered low. There are over 220 companies competing to provide telecoms services in a country of 5m people.

In New Zealand, broadband, fixed-line, mobile and wholesale sectors are 100% open to competition, although in practice competition in some sectors is low because of the small number of market participants—this is particularly the case in the wholesale market, where the incumbent operator owns much of the telecoms infrastructure.

Impact on consumers

The New Zealand CC has set prices for key regulated services since 2001, including interconnection, resale, bitstream, local loop and backhaul prices. Average retail prices fell during 2007 and mobile-phone usage continues to increase—to 104% by the end of 2007. There is evidence, however, that for some elements of charging, consumers in New Zealand are paying more than international standards.

In the UK, wholesale price reductions by BT, allied to the introduction of a price-capping regime by Ofcom, have resulted in a sharp increase in the number of unbundled lines since late 2005. By the end of March 2007, 72% of UK households and businesses had been physically disconnected from BT's local lines and connected to an unbundled exchange (an increase from 45% in March 2006). This was achieved through the unbundling of just 25% of BT's 5,600 local exchanges.

In Norway, fixed-line prices have been broadly stable over the past five years, although some of the most expensive types of calls have come down in price. Mobile prices have on average fallen by around 60% over the past five years and short message service (SMS) prices are down by 40-50% over the same period. Regarding consumer choice, Telenor, in which the state retains a majority share, is still dominant with 68% of turnover in that segment. Competition in the mobile market is much stronger. It is easy to switch suppliers—numbers have been portable within a five-day limit since 2001. The NPT works closely with the consumer ombudsman to ensure compliance. A Consumer Complaints Board (CCB) was created in 2006, providing consumers with a means of registering complaints about electronic communication services where these have already been rejected by the service provider. In 2007 the CCB received 414 complaints and found in favour of 51% of the complainants, either completely or in part. It became compulsory for providers to participate in the CCB following an amendment to the Electronic Communications Act at the start of 2008.

9. Health and safety

The inclusion of the health and safety sector in this review is somewhat anomalous, given the specific operational responsibilities of health and safety agencies and their reach across all sectors of the economy. Their functions do have a potential economic impact—negative if they impose burdens on businesses that affect their competitiveness and positive by improving capacity utilisation as a result of lower accident and illness rates or by lowering social welfare costs. They are not, however, economic regulators in the conventional sense and have no role in price or competition matters. This particular chapter therefore covers a more limited range of issues than the other sectoral chapters. In particular, we have not included specific sections on the impact of regulation on industry or consumers.

The role of the Health and Safety Authority (HSA) in Ireland is to enforce legislation on health and safety issues at work throughout the economy. It is an independent statutory body originally established in 1989. Its activities are now governed by the provisions of the Safety, Health and Welfare at Work Act, 2005. It reports to the minister for enterprise, trade and employment. The HSA has a full-time chief executive with a part-time tripartite board that includes employer and trade union representatives along with a number of ministerial representatives. In our discussions with stakeholders, this governance model was seen as appropriate to the rather unique circumstances of that agency.

The HSA is responsible for monitoring compliance with health and safety legislation in the workplace and can take enforcement action (up to and including prosecutions). It is also the national centre for information and advice to employers, employees and the self-employed on all aspects of workplace health and safety. The HSA also promotes education, training and research in the field of health and safety.

There are a wide range of activities that fall under the HSA's remit including:

- promotion of good standards of health and safety at work;
- inspection of all places of work and monitoring of compliance with health and safety laws;
- investigation of serious accidents, causes of ill health and complaints;
- undertaking and sponsoring research on health and safety at work;
- developing and publishing codes of practice, guidance and information documents;
- providing an information service during office hours; and
- developing new laws and standards on health and safety at work.

Around 207,000 employers come within the HSA's remit, with 88% employing fewer than ten employees, along with 227 self-employed individuals, a significant proportion of whom work in agriculture[1].

There are various other bodies with sector-specific safety responsibilities and there are clear overlap/interface issues arising between them and HSA. To date there has been no attempt to map out clearly the overlap in areas of responsibility. The HSA is currently undertaking such an exercise. While in some respects there are overlaps between the activities of the HSA and other bodies that regulate safety in specific industries, there are differences between the role of the HSA and that of other bodies. The HSA investigates accidents from the point of view of establishing whether the law has been broken, whereas other sector-specific agencies are more concerned with identifying whether there are ways of improving safety requirements.

This scope for overlap with other bodies was evident in other countries. In Denmark for example, health and safety responsibility for the maritime sector, aviation, offshore installations, radiation and fire safety all rest with different departments and organisations. Similarly, in New Zealand, there are separate authorities that administer health and safety law in the maritime and aviation sectors.

Over time the HSA has acquired a range of peripheral responsibilities. It is sometimes a port of convenience for assigning new responsibilities. This has resulted in "mission creep".

Comparator countries

The comparator countries selected for the health and safety case study were Denmark, Germany, New Zealand, Norway and the UK.

Denmark The Danish Working Environment Authority is an agency directly under the remit of the Ministry of Employment, with responsibility for the enforcement of the Working Environment Act of 1999. This includes all business and public-sector places of work, including self-employment, work in private households, aviation and shipping. The Authority has the right to impose fines (average Dkr25,000, or about €3,360 at current exchange rates) and issue non-binding guidelines. Its legal status has not changed in the last five years, but the Working Environment Act was amended in 2004 to provide for unannounced screening visits to every enterprise within seven years.

Germany The Federal Institute for Occupational Safety and Health (BAuA) is an autonomous agency under the jurisdiction of the Ministry of Labour and Social Affairs. It has over 600 staff and the latest annual budget figure available, for 2006, is €47.3m, funded mainly directly from the ministry. In addition to the conventional health and safety responsibilities, BAuA stresses its role within the wider economy in supporting industry competitiveness and in relieving

[1] Senior Labour Inspectors Committee (SLIC) Evaluation of the Irish Labour Inspection System, June 18th-27th 2007, October 9th 2007.

pressures on the social welfare system. However the BAuA does not enforce regulation or carry out inspections.

New Zealand The enforcement of workplace health and safety in New Zealand is carried out by a service department within the national Department of Labour, not by an autonomous agency. The department has a governance committee chaired by the secretary of labour, which determines strategic direction and sets and monitors performance targets. The department's mandate is governed by the Health and Safety Act. This was last amended in 2002. The Act sets out the general duties of the department, and these are in turn supplemented by regulations, codes of practice and guidelines.

Norway The Norwegian Labour Inspection Authority, founded in 1893, is a governmental agency under the Ministry of Labour and Social Inclusion. This means that formally the ministry may instruct the Authority on every aspect of its work. However, the Authority is in practice afforded a large degree of independence and autonomy in professional matters. There has been no change in status or major modification in areas of responsibility over the last five years, other than the need to adapt to monitoring new areas of occupational health and safety. To change the remit of the Authority the Storting (the Norwegian parliament) must pass an act. The budget for the Authority for 2008 has been set at Nkr361m (€41.2m at current exchange rates), an increase of 7% on the previous year and an increase of 36% since 2003.

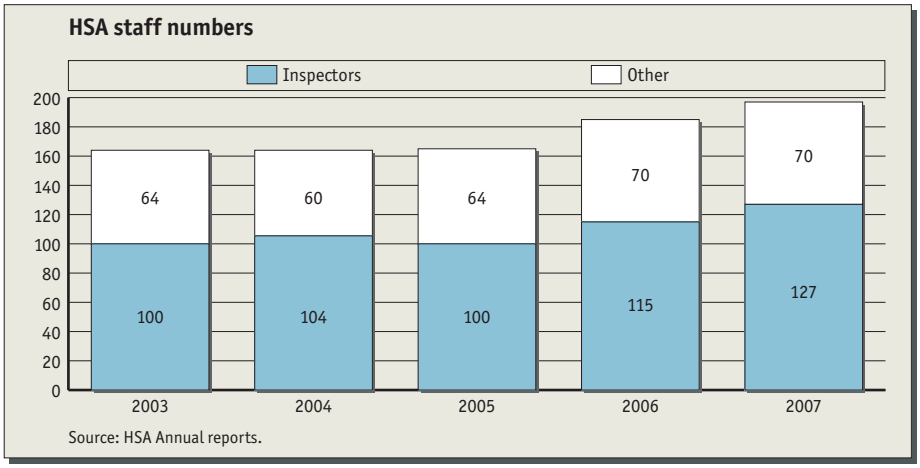
UK The UK Health and Safety Executive (HSE) is an independent, statutory, non-departmental public body. The HSE's mandate derives from the Health and Safety Act of 1974 and its sponsoring department in government is the Department for Work and Pensions. The minister has no direct power to change the HSE's remit, which has not altered in the last five years. On April 1st 2008 the previously separate bodies of the Health and Safety Commission and the HSE were merged into a unitary agency, but this change did not affect health and safety requirements or their enforcement. In the UK, the local authorities also have a role in enforcing health and safety regulations alongside the HSE. They are responsible for enforcement in offices, shops and other parts of the service sector, while the HSE takes the lead in energy, manufacturing, agriculture, schools and hospitals. Health and safety legislation covers all places of work, and thus over 26m employees.

Effectiveness and cost comparisons

It has been suggested that Irish health and safety regulation is of benefit to firms, overall. A majority of firms surveyed in industry and construction believed that the legislation had reduced the cost of accidents with a significant majority of construction firms believing that it had reduced insurance costs[2].

The HSA's operating costs in 2007 amounted to €27.2m, almost double the level in 2002. Salary costs accounted for 55% of total expenditure, at just under €15m.

[2] Indecon, (2006), *Report on the Economic Impact of the Safety, Health and Welfare at Work Legislation*.



Total staff numbers have increased over the past two years from 165 to 197. This figure comprises 127 inspectors, up from 100 in 2005, and 70 other staff, up from 65. The additional staff were recruited to fulfil a new regulatory function, called REACH.

Table 35: Details of HSA inspections.

Year	Total	Per inspector
2003	10,704	107
2004	11,382	114
2005	13,552	136
2006	15,365	134
2007	13,631	107

Source: HSA Annual Reports.

The total number of inspections increased by 44% between 2003 and 2006, but subsequently fell back to their 2005 level in 2007[3]. This occurred at the same time as an increase in the number of inspectors, so that the number of inspections per inspector grew from 107 in 2003 to a peak of 136 in 2005, but had fallen back to 107 by 2007. The HSA has explained that the additional staff recruited for REACH is mostly technical and scientific policy makers and administrators, rather than field inspectors. Including them in the 2007 figure therefore reduces the inspection rate artificially, as most joined the HSA late in 2007. The HSA has also explained that the reduction in inspections in 2007 was to the result of enforcement staff taking up new REACH positions and the effort needed to recruit and train their replacements as well as the new REACH inspectors.

Table 36: Details of prosecutions.

	2002	2003	204	2005	2006	2007
Summary	86	61	25	22	12	14
Indictment	5	15	16	18	27	17
% convictions						
Summary	81	89	83	77	86	93
Indictment	100	100	100	94	100	100

[3] The SLIC Report indicated that the HSA had a target of 16,000 inspections for 2007 (p 22).

The number of summary prosecutions has fallen steadily from 86 in 2002 to 14 in 2007. In part this drop is explained by an increase in the number of more serious prosecutions on indictment, which rose steadily from five in 2002 to 27 in 2006, but then fell back to 17 in 2007. The HSA had a high success rate in terms of securing criminal convictions.

The following data provide some comparison of activity levels.

- In Ireland, the HSA carried out 13,631 inspections in 2007. These resulted in 785 prohibition notices, 906 improvement notices, two improvement directions and 4,273 written advices. About 44% of HSA inspections resulted in formal actions.
- The Norwegian authority carries out around 13,000 inspections a year, similar to the Irish level. Approximately half of these result in some form of formal reaction, such as orders, fines, shutdowns or police reports. The authority is responsible for over 270,000 enterprises and 2.4m employees.
- In Denmark, over 51,000 inspections were carried out during 2007, with approximately 310,000 businesses and 2.7m employees under the scope of regulations. The number of improvement notices issued in 2007 was 20,465; the number of requirements to stop work was 4,444; the number of on-the-spot fines was 97; and the number of cases sent to the public prosecutor was 368, 93% of which led to a conviction.
- In the UK, the HSE brought over 1,100 prosecutions in 2006-07, with 848 convictions and an average penalty per conviction of £15,370. The HSE (excluding local authorities) issued just over 8,000 enforcement notices in 2006-07. The trends in enforcement notices, prosecutions and convictions are broadly downwards.
- In Germany, over 690,000 complaints were investigated by labour inspectors in 2006, on a downward trend from over 800,000 in 2004.
- In New Zealand, almost 20,000 workplace interventions were made and 119 legal proceedings resulted in convictions in 2004-05, the latest year for which figures were provided. In 2007 over 460,000 businesses came under the scope of health and safety supervision, employing 2.2m people.

Comparative costs

The HSA's operating costs per employee amounted to €138,000 in 2007, which was the lowest of any of the agencies reviewed with the exception of the Commission for Taxi Regulation (CTR). Payroll costs per employee were lower than in all of the Irish agencies reviewed apart from the CTR.

Table 37: HSA average payroll costs per employee compared with other regulators.

CAR	Electricity	Gas	Communications	Postal services	CTR	Fin. Reg.
-3.4	-17.5	-8.9	-15.3	-12.1	+50.9	-4.3

An external review of the HSA's activities by representatives of similar agencies from a number of other EU member states was generally favourable in its

assessment[4]. It found that legislation was being effectively implemented and enforced despite limited resources, although it stated that it "found some evidence of lower levels of formal enforcement action being taken than we would have anticipated, in view of the issues observed"[5].

With the exception of Germany, the comparator regulators have a similar remit to the HSA in that they also develop regulations, provide advice and guidance, carry out inspections and investigate accidents. In this respect, the resource comparisons are appropriate with Ireland. However, the BAuA does not cover the same range of functions. The BAuA is focused on the provision of information and advice to companies, government agencies, social partners and the general public to improve safety and health at work. In addition, the agency is involved in research and safety design of technology and humane design of working conditions. Since BAuA does not enforce regulation or carry out inspections, the overall resource requirements are considerably fewer than the comparator agencies. Germany also has other regional and sectoral inspection bodies that are not accounted for in this data. For these reasons the German health and safety authority is not a good comparison with Ireland in this context.

The comparative data on the income of health and safety regulators that we have gathered to date are summarised below.

Table 38: Income ratios, 2007

Country	Ireland	Denmark	*Germany	New Zealand	Norway	UK
Regulator income, €m [6]	27.1	60.0 (DKr447m)	45.7	20.0 (NZ$37.1m)	46.3 (Nkr370m)	415 (£282m)
Regulator income per head of population, €	6.6	10.9	0.6	4.9	10.1	6.8
Regulator income per employee, €'000	140	80	69	111	84	116
Regulator income to GDP	1:7,050[7]	1:3,795[8]	1:53,000[9]	1:4,717[10]	1:6,150[11]	1:4,968[12]

* The German health and safety authority does not enforce regulation or carry out inspections.

The Danish regulator has an income of €10.9 per head of population, making it the most resource-intensive on this measure. Disregarding the German authority because of its different regulatory remit, the New Zealand regulator is the least resource-intensive, at €4.90 per head. Ireland is between the two extremes at €6.6, which is comparable with the UK. Looking at regulator income per employee the results are similar, with Denmark the most costly,

[4] Senior Labour Inspectors Committee (SLIC) Evaluation of the Irish Labour Inspection System, June 18th-27th 2007, October 9th 2007. The team was comprised of experts from the UK, Cyprus, Denmark, Estonia, France, Slovakia and Sweden.

[5] P 28.

[6] Regulator income sourced from 2007 annual reports.

[7] CSO Ireland—2007 GDP €191bn.

[8] Danmarks Statistik—2007 GDP Dkr1,696bn.

[9] Statistisches Bundesamt—2007 GDP €2,423bn.

[10] Statistics Norway—2007 GDP Nkr2,276bn.

[11] Office for National Statistics—2007 GDP £1,401bn.

[12] Statistics New Zealand—2007 GDP NZ$175bn.

New Zealand the least costly (disregarding Germany) and Ireland and the UK approximately the median results. However, on the regulator income per regulator employee measure, Ireland is the most costly at €140,000, which is well above the results for the other regulators. The Norwegian and Danish regulators are the least costly on this measure, at €80,000 per employee.

Since health and safety regulations typically cover all types of employment, another cost-efficiency measure is regulator income to GDP. On this measure Denmark is again the most resource-intensive, requiring €1 in income for approximately every €3,800 of GDP. Ireland requires the fewest resources according to this measure, with €1 in income for approximately every €7,000 of GDP. The general higher cost of the Norwegian and Danish regulators is in line with the OECD comparative pricing index presented in Table 12.

Table 39: Employment ratios, 2007

Country	Ireland	Denmark	Germany	New Zealand	Norway	UK
Regulator staff numbers[13]	197	760	660	180	550	3,582
Regulator employment growth over 5 years (%)	22	18	n/a	n/a	n/a	-14
Regulator employment to total national employment[14]	1:10,660	1:3,763	1:60,000	1:11,761	1:4,400	1:8,820

Ireland and Denmark have witnessed a similar proportionate increase in staff numbers over the previous five years with growth of 22% and 18%, respectively. Over the same period the UK regulator staff numbers have decreased by 14%. In addition to the UK HSE, however, the local authorities also have a health and safety regulatory role for large sectors such as retail, wholesale, offices, financial services, hotels and catering, which requires additional staff not accounted for in the above table.

Another efficiency measure is to compare regulator staff numbers with total national employment, since health and safety regulations typically apply to all workers. On this measure Denmark scores lowest, with one regulator employee for approximately every 3,800 people employed in the overall economy. New Zealand is the least resource-intensive on this measure with only one regulator employee for approximately every 11,800 employees in the overall economy. Ireland also performs relatively well on this measure with one employee for approximately every 10,600 employees in the overall economy.

Overall, the HSA compares favourably with the other regulators in terms of income and staffing levels. In particular, the regulator is far less resource-intensive than Norway or Denmark, both countries of similar size to Ireland. With the exception of Germany the comparator regulators' functions and objectives are closely aligned with the Irish regulator, and as a consequence the

[13] Regulator staff numbers sourced from 2007 annual reports.

[14] Employment data sourced from Economist Intelligence Unit database: Ireland (2.1m); Denmark (2.9m); Germany (39.6m); Norway (2.4m); UK (31.6m); New Zealand (2.1m).

resource comparisons are appropriate. The HSA therefore appears to be relatively low cost.

Governance and accountability

Lines of accountability

In Ireland, the minister must approve the HSA's three-year statement of strategy, as well as a detailed annual work programme. The minister may also issue policy directions. The sponsoring government department has a representative on the HSA board and there are formal liaison meetings between the department and the HSA.

In Norway, the ministry sends the Authority a letter of award each year, which defines the framework for activities in the coming year. It gives the Authority instructions on objectives, general strategies, expected results and specific activities. The letter also states key performance indicators such as number of inspections, number of working hours spent on inspections in different business sectors and number of injunctions. This is supplemented by regular instructions throughout the year, although many of these are based on recommendations made by the Authority. The Authority reports to the ministry every half-year and makes specific reports on special topics such as pay below the minimum wage, excessive hours and insufficient holidays. Results are discussed in three formal meetings a year with the ministry.

In the UK, the HSE submits an annual report to parliament on its activities. It also expresses a strong commitment to ensuring public access to health and safety information, which it believes improves confidence in the health and safety regime. Details of its public and advisory committee meetings are published on the HSE's website.

A general feature of accountability in health and safety is the extent of reporting and consultation with other organisations—employer representatives, trade unions, research and technical institutes. In Denmark, the Working Environment Council comprises employer and union representatives, other government ministries and research bodies. It initiates discussion on emerging health and safety concerns and helps draft new legislation.

In both Denmark and Norway, employer representatives expressed concerns about aspects of health and safety regulation. These concerns broadly centred on the costs of compliance, a lack of commercial awareness and insufficient consultation or research prior to the implementation of new regulation.

Performance evaluation

The nature of health and safety regulation lends itself relatively well to quantitative measures of activity and performance. The metrics used are similar in most of the comparator countries, for example: numbers of inspections, trend reductions in accidents, injuries and days lost. Most of the regulators were able to provide detailed reports on activity levels and trends—it is an area where meticulous observation and recording are essential.

In Denmark, for example, targets were set in 2005 by government for achievement by 2010. These included a 20% reduction in industrial accidents; a 10% reduction in absenteeism resulting from adverse psychological effects of

the working environment; a 15% reduction in hearing damage and a 10% reduction in nuisance noise; and a target for musculoskeletal disorders.

In the UK, the principal performance targets for the HSE were established as far back as June 2000 with the publication of the Revitalising Health and Safety Strategy. This included three main national targets to be achieved by 2010:

- to reduce fatalities and major injuries at work by 10%;
- to reduce cases of work-related ill health by 20%;
- to reduce the number of working days lost per worker from work-related injury and ill health by 30%.

In addition, half of each of these targets was to be achieved by 2004. The HSE reports annually on its progress towards the targets and in its most recent report, for 2006-07, it stated that: the objective on fatalities and major injuries was on track to meet the 2010 target; that they were behind target on work-related ill health; and similarly behind target for working days lost. In addition to these targets, the HSE must also deliver against targets set in a Public Service Agreement between the Department of Work and Pensions and the Treasury.

Unusually, New Zealand does not collect national data on working days lost through occupational injury or ill health. Trends are monitored through compensation claims for work-related injuries handled by the Accident Compensation Corporation.

Appeals procedure

In Denmark there is a Council of Appeal on Health and Safety at Work for decisions made by the Authority. It consists of five representatives from the employers' organisations and five from trade unions under a chair appointed by the minister for employment. In New Zealand, all enforcement decisions can be appealed through the courts and some cases may be subject to judicial review.

10. Transport

Two sectors within transport have been considered: civil aviation and taxis. These are considered separately in this chapter. In the case of civil aviation, we have incorporated our coverage of the impact on the regulated industry within a broader section on regulatory structure and mandate.

Civil aviation

The Commission for Aviation Regulation (CAR) was established on February 27th 2001 under the Aviation Regulation Act, 2001, and is responsible for the regulation of certain aspects of the aviation and travel trade sectors in Ireland. The Commission is an independent public body under the auspices of the Department of Transport, and is accountable to the Houses of the Oireachtas (the Irish parliament). The CAR website states that its principal function is in the area of price regulation, ie, setting the maximum level of airport charges at Dublin Airport and aviation terminal services charges at Dublin, Cork and Shannon airports.

The CAR is also responsible for granting licences to both tour operators and travel agents. As part of this function, the CAR administers a bonding scheme to reimburse consumers in the event of the collapse of a travel agent. The CAR also licences airlines and approves ground-handling services providers under regulations implementing EU legislation. In addition, the CAR is responsible, under EU legislation, for discharging Ireland's responsibilities for schedule co-ordination/slot allocation at Irish airports and the appointment, where necessary, of a schedules facilitator/slot co-ordinator.

Policy context

In terms of regulatory best practice, a significant issue in the context of regulating airport charges involves decisions regarding what items should be included and excluded. There are two methods of regulating airport charges, referred to as the "single till" and the "dual till" approach. The CAR operates the single till model, but has the power to use either one if it chooses. The single till approach involves the regulator taking account not only of the revenue from airport charges, but also of the airport's other revenue—from retailing, car park charges, rental of outlets, etc. The dual till approach distinguishes between revenue for airport services and other revenue. The single till mechanism has been criticised for leading to lower airport charges at congested airports and giving rise to distortions[1]. Airport charges are effectively cross-subsidised by other non-aviation activities, including duty-free sales, which means that airport

[1] D Starkie, (2001), A New Deal for Airports in C Robinson ed., (2001), *Regulating Utilities: New Issues New Solutions*, London, Institute of Economic Affairs.

service charges do not reflect the cost of providing such services, thereby giving rise to excess demand, particularly at peak times[2].

The UK's Civil Aviation Authority (CAA) argued strongly in favour of a "dual till" rather than a "single till" approach in a consultation document issued as part of its 2002 price review. It reported that charges at seven of the ten busiest US airports were no longer regulated on a single till basis[3]. Ultimately, however, the CAA decided against the "dual till" approach, after it had been rejected by the Competition Commission. The Competition Commission concluded that a switch from single to dual till would have resulted in a large transfer of revenue from the airlines to the British Airports Authority (BAA), which it felt was undesirable[4]. The CAA had argued that, at congested airports, airlines were under no pressure to pass on cost reductions arising from lower charges resulting from a single till, and that any change would merely involve redistribution in the economic rents that resulted from congestion from the airlines to the airports. S G Littlechild criticised the Competition Commission's approach, observing that there were serious disadvantages with the single till approach[5]. The Australian Competition and Consumer Commission (ACCC) adopted a dual till approach for Sydney Airport in 2001[6].

In setting the existing price-cap for Dublin Airport the CAR adopted the single till approach. It has recently issued a consultation paper as part of the process of reviewing airport charges after the expiry of the existing price cap in 2010. The consultation paper raises the question of whether the CAR should continue with a CPI ± X approach, using a single till, when setting the price cap. The consultation paper does not appear to contain any analysis of the relative merits of the single versus dual till approach, suggesting that the CAR intends to retain the single till approach and that the question posed in the consultation is limited to whether or not it should retain a CPI ± X price-cap regime[7].

Regulatory structure and mandate

The case for economic regulation of airports stems from the fact that an individual airport operator may enjoy a monopoly or dominant position. There are currently four international airports located in Ireland at Dublin, Cork, Shannon and Knock. Of these Dublin, Cork and Shannon were traditionally owned and operated by a single state company, Aer Rianta. In addition, there

[2] C McCarthy and J McDonnell, (2004), *Late Arrival: A Competition Policy for Europe's Airports*, Dublin, DKM. The authors point out that, while airports appear to be the main beneficiaries of a single till regime, the benefits effectively accrue to airlines.

[3] CAA, (2000), *The "Single Till" and the "Dual Till" Approach to the Price Regulation of Airports*, London, CAA.

[4] Competition Commission (2002), *BAA plc: A Report on the Economic Regulation of the London Airports,* London, HMSO.

[5] S G Littlechild, (2002), *Competition Commission BAA London Airports Inquiry*, Institute of Economic Affairs Discussion Paper No.1, London, Institute of Economic Affairs.

[6] A Fels, (2001), *ACCC Airports and Aviation—Regulatory and Competition Issues*, Australian Competition and Consumer Commission.

[7] CAR, (2008), *Maximum Levels of Airport Charges at Dublin Airport Issues Paper*, Commission Paper 6/2008, Dublin, CAR.

are a number of smaller regional airports, the most important being located at Waterford, Kerry, Galway, Sligo and Donegal. To some extent regional airports such as Kerry and Galway may exercise some competitive constraint on Cork and Shannon, for example Ryanair relocated a service from Shannon to Frankfurt/Hahn to Kerry in order to benefit from lower airport charges.

Originally the CAR was responsible for regulating charges at all three Aer Rianta airports. Following the announcement by the government that Aer Rianta was to be restructured and that its airports would be split into three independently operated facilities, the CAR's role was reduced to regulating airport charges at Dublin Airport. In that scenario Cork and Shannon would appear to be sufficiently close to one another to exercise a competitive constraint on each other, while Kerry also provides some competition to both of these airports. The establishment of Cork and Shannon as independent stand-alone entities would mean that regulation of charges at those airports is not required, since there is sufficient competition between them. Dublin Airport, however, would not appear to face any significant competitive constraint. Thus, even if the former Aer Rianta were split into three separate independent airports, there would appear to be a need for the continued regulation of airport charges at Dublin Airport, as it is unlikely to face any significant competition for the foreseeable future. There is now some doubt as to whether the government is going to proceed with the split of the three airports. If Cork and Shannon are not established as separate, independent airports, but remain part of a single, virtual monopoly airport operator, the CAR's remit would need to be expanded to cover the setting of airport charges at both sites

The existing legislation governing regulation of airport charges by the CAR will have to be reviewed in the context of implementation of the airport charges directive which is expected to be formally adopted shortly. Under the provisions of the directive, an independent supervisory authority will be required to oversee airport charges at airports with more than 5 million passengers per annum and at the largest airport in each member state. While the directive gives some discretion in relation to how the supervisory authority is to exercise oversight over airport charges, the directive means that an independent authority will have to be given responsibility for overseeing charges at airports above the specified thresholds.

The CAR also regulates prices of aviation terminal services at Dublin, Cork and Shannon. Such services relate to air traffic control and other services provided by the Irish Aviation Authority (IAA). In addition to providing such services, the IAA also has regulatory responsibilities for air safety. The IAA is a monopoly provider of aviation terminal service charges such as air traffic control, and so the basic rationale for the regulation of these charges remains in place.

In contrast with the position in communications and, to a lesser extent, in energy, we see little prospect for a scaling back of price regulation in airport services and airport terminal services.

In addition to its price regulation functions, the CAR is responsible for a range of activities, including licensing of airport ground handling services, the regulation of travel agents, and the operation of bonding arrangements for tour

operators. The regulation of travel agents, for example, dates back to a time before the existence of the Internet when travel agents were major sellers of airline tickets[8]. An obvious issue to be addressed in considering the appropriateness of the current regulatory system is whether it is logical to assign such functions to an economic regulator.

On May 9th 2008 the minister of transport asked the CAR to conduct a study:

- to review the effectiveness of the travel trade licensing provisions as the optimum means to provide financial protection to the travelling public;
- to consider whether the regulatory requirements are being bypassed by online vendors of travel services and if there is any consequential loss of consumer protection or distortion of competition;
- to consider the overall internal coherence of the regulatory framework with regard to relative treatment of tour operators and travel agents; and
- to consider, in the light of the analysis, the need for reform by way of a new approach, amendments to the existing arrangements to improve efficiency and effectiveness, or indeed through some deregulation.

The extent to which this review leads to any changes or modifications of the existing travel trade licensing provisions may have implications for our findings.

The current travel trade bonding and licensing regime is primarily governed by two acts dating back to 1982 and 1995, respectively. The CAR has indicated that the existing legislation is not suited to more recent and likely future developments affecting the travel trade industry, such as the growth of the Internet and changes in payment systems. The European Commission has itself called for a review of the Council Directive on Package Travel Holidays, transposed in Ireland by the 1995 Act. The CAR also noted that providers and carriers were increasingly selling directly to consumers rather than through travel agents. As a result, determining who needs what licences or bonding under the current regime had become increasingly complex, and there was a real risk that the current scheme was failing to protect all of the travelling public, while at the same time imposing unnecessary costs on some sectors of the industry[9].

It is sometimes suggested that airport charges constitute only a small proportion of actual ticket prices. Lower airfares resulting from aviation liberalisation in Europe mean that airport charges increased as a proportion of the price[10]. Charges also constitute a higher proportion of fares for shorter trips. In the face of widespread criticism about hidden add-ons, some regulators such as the Office of Fair Trading (OFT) now oblige airlines to disclose the full cost of travel including all taxes and charges on their booking sites. This would be

[8] The CAR issued a consultation document setting out various options for the future regulation of ground handling, travel agents and tour operators.

[9] CAR (2008), *Review of Trade Legislation in Ireland*, Commission Paper 5/2008, Dublin, CAR.

[10] S Barrett, (2000), Airport Competition in a Deregulated European Aviation Market: *Journal of Air Transport Management,* 6:17-27.

unnecessary if airport and other charges did not constitute a significant proportion of the fare in many cases[11].

Comparator countries

The comparator countries used were Denmark, Norway, the UK, France and New Zealand.

Denmark The Danish Civil Aviation Administration (DCAA) is a government enterprise under the Ministry of Transport and Energy and was established in 1938. The DCAA is the aviation regulator in Denmark, the Faroe Islands and Greenland. Its functions cover:

- safety regulation;
- security regulation;
- airspace regulation; and
- economic and performance regulation.

UK The regulator for the UK is the CAA. It is an independent body, covering:

- safety regulation;
- airspace policy;
- economic regulation; and
- consumer protection.

The secretary of state for transport appoints members of the CAA's board. In response to a recommendation by the Transport Select Committee, the government conducted a strategic review of the functions, structure and policy-making role of the CAA. The findings of the review were published in June 2008 and included the recommendation that the safety and economic regulation functions remain with the CAA. Its economic regulation department sets airport charges for Heathrow, Gatwick and Stansted airports.

France Aviation is regulated by the Direction Générale de L'Aviation Civile (DGAC), a department within the Ministry of Ecology and Sustainable Development. The DGAC is responsible for:

- safety;
- security (checking of passengers, baggage, freight);

[11] It was suggested to us that booking fees for credit card bookings also constituted a significant add-on to the cost of airline tickets and that it seemed disproportionate to regulate airport charges and not credit card booking fees. The issue of fees for using credit cards when booking tickets is not confined to airline tickets, but applies to many other types of goods and services bought on the web or over the telephone. It would seem appropriate to consider the issue of such charges in a broader context rather than just in the context of airport regulation.

- economic regulation;
- air traffic control services; and
- guaranteeing the quality of personnel training.

The DGAC also has a remit to reduce pollution generated by air transport, particularly noise and atmospheric pollution. The DGAC also monitors the economic and financial activity of French airlines and issues public air transport operator licences in compliance with EU regulations.

Norway

The Civil Aviation Authority (CAA) is an independent administrative body under the Norwegian Ministry of Transport and Communications. It has four core tasks, all safety-related:

- certification; the CAA carries out various checks and inspections before an operator is approved;
- surveillance; this comprises planned inspections of regulated organisations, to enforce national and international aviation safety requirements;
- development of regulatory framework; the development of the regulatory framework takes place mainly within international networks in which the CAA plays an active role; and
- information; the CAA provides information on, for example, accident and incident statistics.

The state ownership of airports is administered by Avinor AS, a wholly state-owned limited liability company. Avinor is also responsible for air traffic control services in Norway. Both airport and air traffic control charges are fixed annually directly by the ministry.

New Zealand

The New Zealand CAA was established under the Civil Aviation Act of 1990 as a Crown entity. It is designated by the minister of transport as the:

- airspace authority;
- air traffic services authority;
- aviation security authority;
- dangerous goods authority;
- meteorological authority; and
- personnel licensing authority.

In summary, there is wide variation in the mix of functions performed by civil aviation authorities and we will return to this in more detail later in this chapter when making the cost comparisons.

Effectiveness and cost comparisons

In terms of costs, the CAR performed quite well in comparisons with other Irish regulatory bodies described in Chapter 4. Its overall budget means that it was the smallest of the regulatory agencies considered in the report with a total income in 2007 of just €4.2m. Similarly, its operating costs were among the lowest and when legal expenses were excluded, its operating costs in 2007 of €3.3m were similar to the costs incurred by the Commission for Energy Regulation (CER) in regulating the gas industry. Likewise, figures for operating costs per employee and payroll costs per employee were relatively low in comparison with most of the other agencies examined. For example, excluding legal fees, operating costs per employee in 2007 at €158,000 were slightly higher than those of the Financial Regulator and the Health and Safety Authority (HSA), but were well below the figures for electricity, gas, communications, postal services and taxis. Its operating costs per employee excluding legal fees fell by 2.6% between 2004 and 2007.

Payroll costs per employee of €78,400 in 2007 were lower than those of all the other bodies reviewed except the HSA and Commission for Taxi Regulation (CTR) as Table 40 below illustrates. They increased by just 0.5% between 2004 and 2007.

Table 40: difference in CAR average payroll costs per employee compared with other regulators, 2007

Electricity	Gas	Communications	Postal services	CTR	HSA	Fin.Reg.
-14.6	-5.7	-12.3	-9.0	+56.1	+3.5	-0.9

In terms of the international comparison, Ireland is the only country under review that has two separate aviation regulators, the IAA and CAR. The IAA is responsible for safety regulation and air traffic control. The CAR is responsible for economic regulation and sets the airport charges for Dublin Airport as well as the air traffic control charges that the IAA can levy on users at Dublin, Cork and Shannon airports. In this respect the IAA, as a service provider, is regulated by the CAR.

In the UK, the CAA is responsible for economic regulation, airspace policy, safety regulation and consumer protection. Its economic regulation department sets the airport charges for Heathrow, Gatwick and Stansted airports as well as en route air traffic control charges. Air traffic control services at most of the UK's major airports are supplied on the basis of a competitive tender process. They are therefore not regulated by the CAA.

Denmark's CAA is responsible for economic, safety, security and airspace regulation. The economic regulation function sets the airport charges. Air traffic control services are provided on the basis of a competitive tender and charges are therefore not regulated by the Danish CAA.

In Norway, the CAA is responsible for safety regulation and also has an information-provision duty. State ownership of airports is administered through Avinor, a wholly state-owned company reporting to the Ministry of Transport. Avinor is also responsible for air traffic control services. Both airport charges and air traffic control charges are fixed annually by the ministry.

In France, the DGAC has wide-ranging responsibility covering all regulatory aspects of the aviation sector: economic regulation; safety regulation; security regulation; air traffic control services; industry partnership; and environmental duty. The DGAC sets airport charges and, as the air traffic control service provider, it sets its own charges "under best possible conditions of safety and cost".

In New Zealand, the CAA is responsible for airspace regulation, security regulation and safety regulation. The airports are free to set charges subject to consultation arrangements with airlines and the threat of review and re-regulation by the government under a light-handed regulatory regime. The state-owned Airways New Zealand is certified by the New Zealand CAA as the air traffic control service provider throughout the country and its charges are subject to audit by the regulator.

In summary, the approach to aviation regulation clearly varies considerably across the comparator countries. Ireland is the only one to have a separate aviation regulator responsible for economic regulation. In the UK and Denmark the regulators oversee a mix of economic regulation and competitive tenders. In Norway the regulator is not responsible for economic regulation. In France the regulator, as the air traffic control service provider, is self-regulating. In New Zealand the regulator oversees a light touch, principles-based regime.

In Denmark, France and New Zealand the regulators have responsibility for security regulation, which includes checking baggage, passengers and freight. This function is resource-intensive and must be considered in cost comparisons with other countries. It is also more appropriate to combine the resources of the CAR and the non-air traffic control income of the IAA when making international comparisons, since the other countries have a single aviation regulator.

Table 41: Income ratios, 2007

Country	Ireland	Denmark	France	New Zealand	Norway	UK
Regulator income, €m [12]	*20.2	11.1 (Dkr82.5m)	**1,673	15.0 (NZ$27.8m)	17.3 (Nkr138m)	233.8 (£159m)
Regulator income per head of population, €	4.9	2.0	27.0	3.7	3.8	3.8
Regulator income per employee, €'000	215	74	138	79	108	239

* Includes CAA income and non-ATC income of the IAA (4.2m and 16m, respectively).

** Includes air traffic control income.

Aviation regulation in Ireland costs more than in Denmark, New Zealand and Norway. This is partly because of air traffic control services not being competitively tendered in Ireland as they are in the UK and Denmark, thereby requiring the CAR to regulate those charges. However, both Denmark and the Netherlands have an additional security function that would be expected to make regulation more expensive. On the basis of regulator income per head of

[12] Income data sourced from 2007 annual reports except: Norway 2006 report and French data provided by regulator.

population, only France is more expensive than Ireland, which reflects the fact that the DGAC also directly provides air traffic control services.

In terms of regulator income per employee the UK is the most resource-intensive at €239,000. Ireland is also relatively resource-intensive on this measure at €215,000 per employee. Denmark is least resource-intensive on this measure at €74,000.

Table 42: Employment ratios, 2007

Country	Ireland	Denmark	France	New Zealand	Norway	UK
Regulator staff numbers[13]	*94	150	***12,123	191	160	980
Regulator employment growth over 5 years (%)	**24	-37	0	14	10	-8

* Includes both CAA staff and safety-related IAA staff (21 and 73, respectively).

** CAA only.

*** Data include air traffic control staff.

CAR employees and IAA safety regulation staff account for 94 employees. There are additional finance, human resources and training personnel that should be added to the IAA staff numbers, but this breakdown has not been sourced. It seems likely, however, that even accounting for additional staff, Irish aviation compares favourably with the other countries in terms of employee numbers. Norway is the closest comparator with Ireland in terms of regulator functions and country size. Ireland would appear to be less resource-intensive in terms of staff than Norway. Employment growth is of limited value since the Irish data refers only to the CAR staff.

Overall, the Irish regulatory regime would seem to be relatively resource-intensive in terms of income. However, the CAR and IAA do not appear to be overstaffed relative to the other regulators.

Governance and accountability

Since its establishment in 2001 the CAR has operated with just a single commissioner, although the legislation provides for the appointment of up to three members. In Chapter 4 we concluded that in the case of economic regulators, such as the CAR, a three-person commission was superior to a single-member body or sole regulator. We note, however, that the small size of the CAR may raise some questions about whether it would make sense to appoint a three-member commission. A three-member commission in an agency of around 20 people might be regarded as somewhat top heavy. Again, given its small size, the appointment of two extra commissioners would have a non-trivial impact on its operating costs, although at the same time its operating costs would probably continue to compare favourably with those of other regulatory bodies in Ireland.

We also suggested in Chapter 4 that having a commission made up of one full-time member and a number of part-time members may not be especially effective, as the part-time members might find it difficult to exercise any meaningful check on the sole full-time commissioner. Similarly, we do not

[13] Data sourced from 2007 annual reports.

consider that appointing an advisory panel akin to that which operates in the case of the CTR would represent a useful model in the context of the CAR.

Lines of accountability

In Denmark, the DCAA reports direct to the minister of transport and any decisions made by the regulator can be appealed against to the minister.

In New Zealand, the minister is responsible for overseeing and managing the government's relationship with the CAA. The minister expects the CAA to achieve the government's desired results set out in the 1990 Act, to comply with other relevant government legislation, and to manage civil aviation safety and security risks on behalf of the Crown. The director of the CAA acts independently, however, and is not directly responsible to parliament.

Performance evaluation

In Denmark, performance targets are set in co-operation between the DCAA and the Ministry of Transport and generally cover aviation safety and economic efficiency.

In the UK, a range of performance indicators are reported on by the CAA in its annual report. These cover safety measures, for example fatal accident rates and near misses. They also cover service-level measures, such as departure delays and time taken to issue pilots' licences. The CAA also sets itself a number of corporate objectives, for example to maintain an effective working relationship with government and to support better regulation initiatives. The financial results of the group are assessed by reference to financial targets agreed with the Department for Transport. The group is required to set its unit charges at levels sufficient to achieve a return before interest on the average level of capital employed. The regulatory sector, comprising the activities of the Safety Regulation, Economic Regulation and Consumer Protection Groups, achieved a return of 6.9%, compared with a target of 6%.

In France, the breadth of the DGAC's responsibilities is reflected in its range of objectives and targets. These cover air traffic management standards, airline certification and security, and aeronautical training for engineers, technicians and pilots. For each objective, the DGAC publishes a series of indicators on a quarterly basis to illustrate its progress against targets.

Appeals procedures

The issue of accountability has already been addressed at some length in Chapter 4. There are, however, specific aspects of the appeal provisions in respect of the CAR that merit separate mention. Both the regulated airport and its customers, the airlines, may appeal against decisions by the CAR on airport charges[14]. In this regard the CAR is somewhat unique as there is no right of appeal against the pricing decisions of other economic regulators. The legislation requires the minister to appoint an appeals panel of at least three people to consider such an appeal. The powers of the appeals panel are limited to referring the decision back to the regulator, who may choose either to affirm or amend the original decision. The CAR's first price determination in 2001 was referred to an appeals panel. Following the panel's decision, the CAR revised its decision, and reduced its proposed airport charges. A second appeal i.e. an

[14] Aviation Regulation Act, 2001, s.40.

appeal of the September 2005 charges determination resulted in a decision in June 2006 to allow a limited increase in the charges cap. A decision on a further appeal of a subsequent CAR determination is due before the end of February 2009.

Impact on consumers

Airport charges are a relatively small, albeit significant, share of the total ticket price. Regulation of airport charges therefore has a lower impact on consumers than other forms of regulation such as energy or telecommunications. Furthermore, as previously outlined, the role of the CAR in regulating airport charges was withdrawn from Shannon and Cork airports. Nevertheless, the work of the CAR combined with the ability of the airlines to appeal against pricing decisions has proven effective in preventing excessive airport charges at Dublin airport. However, the CAR consultation paper should possibly have considered the merits of a single versus dual till approach to aviation regulation.

The CAR also regulates the price that consumers pay for air traffic control services at Dublin, Cork and Shannon airports. This role was not typical of the comparator aviation regulators where the charges are more usually determined on the basis of competitive tenders from prospective service providers.

The CAR has a significant consumer protection role. It is the national enforcement body tasked with the monitoring and regulation of EU legislation covering air passenger rights and the provision of assistance to passengers with reduced mobility.

Taxis

The Commission for Taxi Regulation (CTR) is an independent public body, the principal function of which is the development and maintenance of a regulatory framework for the control and operation of small public service vehicles (SPSVs). SPSVs comprise taxis, wheelchair-accessible taxis, hackneys and limousines. The CTR sets maximum fares for public-hire vehicles, ie, taxis, including wheelchair-accessible taxis. Fares charged for hackney and limousine hire are not regulated and must be agreed in advance by the customer and the operator. The CTR was established in September 2004 under the provisions of the Taxi Regulation Act, 2003. It also has a wide range of licensing, complaints, enforcement and prosecution functions that had previously been the responsibility of the Gardai (the national police force).

Policy context

The rationale for economic regulation of taxis differs somewhat from that in the utilities industries. In contrast with the situation in energy and, historically at least, in telecoms, the issue of natural monopoly does not arise. In the past in Ireland the number of taxis was limited, but quantitative restrictions were

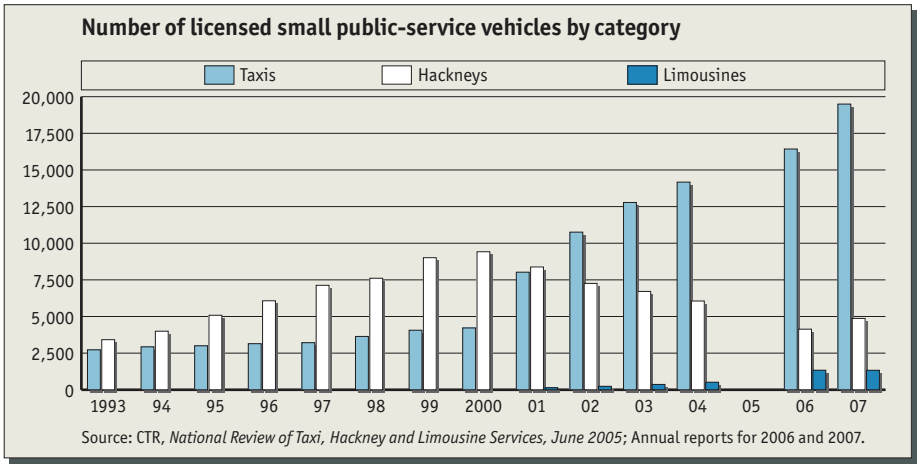
deemed illegal by the courts[15] and since their abolition, taxi numbers have increased dramatically, from just over 4,000 in 2000 to almost 20,000 in 2007. Arguably, with such large numbers of suppliers one might expect prices to be set competitively by market forces and some countries, for example Sweden and New Zealand, have deregulated fares. The rationale for regulating taxi fares arises because of the nature of the service provided. There is potential scope for unscrupulous operators to exploit customers in particular situations, eg, tourists taking a taxi at an airport and individuals hailing a taxi on the street late at night. Regulating taxi fares is therefore designed to prevent such behaviour.[16] Clearly, however, the functions of the CTR as outlined above extend beyond pure price regulation and into the area of qualitative regulation.

Even though there may be many suppliers and customers, an unregulated taxi market is prone to market failure. Consumer choice is likely to be limited (in the case of having to take the first taxi available at ranks) and it is difficult to compare prices (especially as these will vary according to the time of day and are difficult to gauge when in an unfamiliar area). At the very least, consumers need some reassurance that the vehicle that they are stepping into is roadworthy and the driver is *au fait* with the street names and landmarks. The general purpose of taxi regulation is, therefore, to limit the impact of these information asymmetries by providing consumers with protection, normally in the form of maximum (metered) prices and entry requirements relating to safety and competency. When regulation is working well, the supply and demand for taxis is balanced. This results in minimal waiting time for passengers and a minimal queue of empty taxis.

Taxi fares in Ireland were traditionally regulated, to some extent at least, by local authorities, while hackney fares were a matter to be negotiated between the passenger and hackney operator. Local authorities set fares for journeys within "taximeter areas". Local authorities also had the power to designate such taximeter areas. In practice, taximeter areas were limited to the main cities and larger towns, and prior to the establishment of the CTR there were approximately 20 designated taximeter areas. Fares for journeys outside those areas were determined on the basis of negotiations between the driver and passenger. It should also be noted that where a journey commenced within a taximeter area but finished outside it, the fare again was a matter for negotiation between driver and passenger.

[15] *Humphrey & Ors. v. Minister for Environment & Ors.*[2001] IR 306. Following the judgment the minister introduced new regulations entitled the Road Traffic (Public Service Vehicles) (Amendment) (No.3) Regulations, 2000, which repealed the previous regulations that had already been rendered void by virtue of the *Humphreys* court judgment, and provided for the issuing of new taxi licences without quantitative restrictions for relatively modest fees.

[16] Gwilliam argues that taxis are subject to more widespread information asymmetry problems. K M Gwilliam, (2005), *Regulation of Taxi Markets in Developing Countries: Issues and Options,* Washington, DC, World Bank. We regard fare regulation as coming within the narrow definition of economic regulation, although certain quality standards and other regulatory rules might also be regarded as meeting the definition of economic regulation.



In a sense, the fact that taxi fares had previously been regulated in urban areas implied that the need to protect consumers from overcharging had long been recognised. Existing regulatory arrangements were clearly inadequate as they only applied in certain parts of the country and even then only for journeys that commenced and finished within the designated taximeter area. Thus, the establishment of a national regulatory body to regulate taxi fares throughout the country was based on the rationale that all taxi users in the country should be protected against overcharging for all taxi journeys. If the argument that consumers should be protected against overcharging by taxi drivers is accepted, then it becomes difficult to argue that such protection should not apply in all cases. This leads to the conclusion that taxi fares should be regulated throughout the country, although arguably it is not necessary to have a national regulatory authority to do this. Theoretically, at least, each local authority in the country could be obliged to regulate fares within its jurisdiction. Given the overall size of the country and the large number of local authorities, it seems likely that a single regulatory authority is a more cost effective and efficient option[17].

As noted, the powers of the regulator extend beyond simply setting fares. The regulator also has powers to set quality standards. Price regulation arguably provides an incentive for regulated firms to make savings by reducing quality, so quality control is an essential element of price regulation.

Comparator countries/cities

No other country in our study has a single national regulator. Instead, most national governments empower their local authorities to promote competition and protect consumers (as was the case in Ireland before the reorganisation). Hence, it is not clear which countries make the best comparators in this regulatory market. It is also unclear whether such comparisons should be made by combining all local authorities in the comparator country (thereby replicating the Irish Commission's function as a national regulator) or by

[17] It is suggested that regulation of taxis at a local level means that regulation can respond to local market circumstances, although it is also desirable that areas should be large enough to ensure that there are enough patrons for the number of taxis and to prevent competitors crossing over from other areas. See K M Gwilliam, (2005), *Regulation of Taxi Markets in Developing Countries; Issues and Options,* Washington, DC, World Bank.

looking at individual local authorities (which mimic the singular nature of the Irish regulator, albeit over a much smaller geographical area).

London is a suitable comparator. Its taxi services (both private hire and black cabs) are governed by an independent regulator that is responsible for setting quality and price levels. Denmark is one of the comparator countries for the transport case study and, combined with the fact that it has a similar population size to Ireland, it seems worthy of study. From a practical point of view we also examine what might occur if Ireland were to relax regulation further by deregulating prices (as well as licence quotas) by reporting on Oslo (where fares are unregulated) and Sweden, which from around 1990 has completely removed all price and quantity controls.

The table below summarises the scope of taxi regulation on price, quantity and quality within each location.

Table 43: Taxi regulation

Country/city	Regulator	Price	Quantity	Quality
Ireland	Commission for Taxi Regulations	Maximum (set by cost formula, nationwide)	No restriction	Vehicle quality/ driver standards
London	Public Carriage Office (TfL)	Fixed (set by cost formula)	No restriction	
Denmark	Local authority	Maximum (set by cost formula)	Yes	
Oslo	County authority	None	Yes, but discretionary	
Sweden	n/a	None, but fares agreed in advance and displayed.	None	Stricter driver standards

In the UK, if quantity restrictions are imposed the local authority must demonstrate that there is "no significant demand for the services of [taxis within its licensing area] which is unmet". This is usually done through consumer surveys. In London, the Public Carriage Office (PCO) has no power to restrict market entry, so this procedure is unnecessary. However, the PCO service charter states that:

"*You can expect us to make every effort to make sure that our licence fees and other charges represent value for money. We'll make comparisons with other licensing authorities, and make sure fees received for one licensing activity are not used to pay for another licensing activity.*"

According to the Transport Committee (2005) such comparisons have, in the recent past, been favourable to the PCO. The other major objective is to make fares predictable, simple to understand, value for money and sufficiently rewarding to taxi drivers.

The objectives are similar in other jurisdictions. In Denmark, for example, the objective of licensing is to ensure that consumers and the entire municipality get a satisfactory service.

Governance and accountability

In most countries the regulation framework is set by legislation and implemented by the local authorities (as was the case in Ireland before September 2006).

London differs slightly from the rest of the UK. A separate public body, the PCO, is responsible for licensing taxis and drivers. The PCO is part of Transport for London (TfL), a statutory body formed by the Greater London Authority Act 1999. Before this the PCO was part of the Metropolitan Police. The reorganisation in 2000 provided the PCO with strategic responsibilities that were previously assigned to the Ministry of Transport, namely an annual review of taxi fares and licence fee determination. Proposed fees are now approved by the TfL Board, which is chaired by the Mayor of London. The Mayor may also call upon the PCO to implement policy initiatives, such as those relating to emissions. In March 2007 the PCO outsourced the inspection and licensing of private-hire vehicles to a private company (SGS).

The PCO issues PCO notices to the trade press in order to communicate with taxi drivers. However, this has been criticised as not all drivers read these publications (Transport Committee 2005). Other general forms of public communication appear to be limited; information on the performance of taxi regulation in the TfL annual report is sparse.

In Denmark, local authorities regulate taxi services within their boundaries. Recent reforms have decreased the number of municipalities from 277 to 98, allowing local government communities to manage taxi regulation in the participating municipalities. In the Greater Copenhagen Region the Public Taxi Council (which superseded the Greater Copenhagen Taxi Board) is made up of 11 politicians, who shape taxi regulation in the 20 municipalities of Copenhagen. The Danish Ministry of Transport and Energy is the authority supervising technical and educational specifications.

In Norway, ultimate responsibility for taxi regulation resides with the Ministry of Transport and Communications (MTC), which sets quality and safety requirements applying to licence holders. (The MTC also has authority to regulate on issues across county borders.) Maximum prices are set by the national competition regulator (NCA), although five major cities (including Oslo) have been exempt from fare regulation since 2000. Most other powers have been decentralised. Counties have the ability (not obligation) to restrict the number of licensed taxis. They also decide the area over which the licences are valid, although in Oslo (and a few other counties) this is always taken to be the whole county.

In Sweden, licences are issued by the county administrative board. They also have responsibility to promote efficient competition within counties. However, no one agency has responsibility for monitoring the entire market, which makes it hard to retrieve market data.

Similar considerations arise in the case of the CTR as in the case of the CAR. While in general we believe that multi-member rather than single-member

commissions are preferable in the case of economic regulators, the small size of the CTR raises questions about whether a multi-member commission would have been a practical option for the CTR. We noted in Chapter 4 that the CTR has an advisory council and that it is required to consult with it prior to taking any regulatory decisions. The feedback that we received during the course of our meetings with stakeholders indicated that the advisory panel had reduced the degree of personalisation that can sometimes arise in the case of single-member regulatory commissions. To some extent, however, the position has been overtaken by events. Legislation providing for the establishment of a new Dublin Transportation Authority (DTA) was enacted in July 2008. It has been decided that the CTR should be amalgamated within the proposed new DTA. Although the exact details of how the new agency will operate are not yet in the public domain, the issue of a multi-member commission may be addressed by the proposed merger.

Effectiveness and cost comparisons

Prior to the establishment of the CTR fares were regulated at a local level in a limited number of individual taximeter areas, with fares effectively unregulated outside those areas. There was a wide disparity in fares between different taximeter areas. The CTR introduced a national maximum taxi fare in 2006. This was reviewed and a new increased maximum fare came into force on November 1st 2008.

It is difficult to assess how the CTR compares with other agencies in terms of best practice, given the limited period of time that it has been in existence. The consultation document that it issued regarding its 2008 fare review was a brief document and said little about the principles that should apply to setting fares. That said, it should be noted that it had commissioned a detailed review of fares both domestically and internationally before establishing a national maximum fare in 2006, and may have concluded that there was no need for an in-depth review of fares so soon after that review.

As noted previously, the CTR has responsibility for setting quality and other regulatory standards in addition to maximum fares. While quality regulation is necessary, for reasons already outlined, the economic literature on regulation suggests that care is needed to ensure that quality standards are not set so high that they come to constitute a barrier to entry. This can be a particular concern in the context of regulatory capture, where quality standards are overly influenced by the views of the regulated industry. At present there is no indication of any such problem in the case of the CTR and as pointed out above, taxi numbers have increased considerably in recent years indicating that there are no significant barriers to entry, regulatory or otherwise.

The CTR is a relatively new agency, having only been established in the latter part of 2004. Its 2005 figures are distorted by the fact that staffing build-up occurred during the course of the year, so that they do not reflect the full-year cost of such staff. Therefore we only have figures for two years, 2006 and 2007, on which to make comparisons with the other regulatory bodies. In terms of costs per employee the CTR compares rather unfavourably with the other

bodies reviewed, with average costs per employee in 2007 of €178,000. This is significantly below costs per employee in electricity of €278,000 and is lower than in postal services and aviation, but higher than in financial services and health and safety. If legal costs are excluded, the costs per CTR employee fall to €168,000.

The largest item of expenditure recorded by the CTR was vehicle and driver licensing costs, which amounted to €2.1m, around 24% of its total operating costs. Data provided by the CTR split the licensing costs between vehicle and driver licensing at €1.5m and €600,000, respectively There were approximately 26,000 licensed SPSVs and 43,000 drivers operating in 2007, so licensing costs work out at around €58 per vehicle and €14 per driver.

Average payroll costs per employee at just over €50,000 in 2007 were substantially lower than in any of the other regulatory agencies considered.

Table 44: Difference in CTR average payroll costs per employee compared with other regulators, 2007

CAR	Electricity	Gas	Communications	Postal services	HSA	Fin.Reg.
-35.9	-45.3	-39.6	-43.9	-41.7	-36.5	-33.7

As already pointed out, it seems likely that a single national taxi regulator is more efficient than the previous regime whereby fares were determined separately in around 20 individual taximeter areas by individual local authorities. It would be difficult, however, to compile data on the actual costs of the previous regime. Similarly, the fact that there is a single national fare would seem to reduce the cost of price reviews.

Taxi regulators are largely self-funded. In London, the PCO is only permitted by law to earn enough from licence fees to cover the cost of provision.

Table 45: Taxi regulator operating costs

Country/region	Regulator	Income	Expenditure	Employees	Taxis	Drivers
Ireland	Commission for Taxi Regulation	€21.9m (2007)	€8.8m (2007)	20 (2007)	25,695 (end-Dec 2007, includes 19,496 taxis and 6,199 private hire vehicles)	43,262 (end-Dec 2007)
London	Public Carriage Office (TfL)	£19m (2008/09) £17.2m(2008/09)	£19m (2008/09)	182 (2008/09)	67,000 (includes 21,000 black cabs and 46,000 private vehicle hires	69,000
Greater Copenhagen	Local authority	€250,000 (approx)	€500,000 (approx)	5 (11 politicians)	2,250	7,900
Oslo	County authority	n/a	n/a	n/a	n/a	
Stockholm County	County admin board	€40,000 (est.)	€50,000 (est.)	3	5,500	10,000

Sources: CTR Annual Report 2007; Transport for London revised 2008/09 budget; Transport for London Annual Report, 2008; Storkobenhavens Taxinaevn; County Administrative Board of Stockholm.

Looking at total expenditure for the purpose of cross country comparability, in 2007 the cost per licensed vehicle in Ireland was €342. This is slightly higher

than the figure for London in the current financial year (2008/09), which is expected to be around £264 (€310) for each vehicle (based on TfL's forecast of 72,000 licensed vehicles). However, costs per issued driver licence are substantially lower in Ireland (around €200 compared with €322 in London). In Greater Copenhagen the equivalent figures for both licensed vehicles (€200) and drivers (€63-125) are lower still than in London and Ireland, possibly reflecting the fact that licences are issued biannually. In terms of income, only the CTR earns an income significantly in excess of costs.

Impact on regulated business

In the UK, local authorities have considerable discretion. They can choose whether or not to impose quantity restrictions through limits on the availability of licences and, where such constraints are imposed, fix the number of licences in circulation. In London, no limits are placed on the number of licences issued. Rather, additional restrictions are imposed in the form of testing the competence of new drivers in their knowledge of the streets and places of interest in the capital ("the knowledge"). TfL can (and does) prescribe conditions for the granting of taxi drivers' licences. Applicants must satisfy TfL that they are "of good character and fit to act as a cab driver".

Copenhagen also makes thorough checks on the skills and suitability, both economic and personal, of each licence applicant. Drivers must obtain a business driving licence from the police, have the ability to master Danish, have sound geographical knowledge of the area and pass a two-week training course. Licence awards are made every two years to applicants with the highest turnover and seniority. These are valid for a period of up to ten years and are not transferable. There are additional stipulations. Since the number of licences may be limited, drivers must run their business as a private firm (not as a corporation). They must also be affiliated to one of six approved dispatch centres, which co-ordinate and distribute telephone orders and have powers to fine drivers or recommend the removal of their licences if they fail to act in the general public interest. The average income from a taxi that is used efficiently by drivers in Copenhagen is around €154,000 per year.

In Oslo, where fares have been deregulated since 2000, there has been no relaxation in quantity limits or additional stipulations concerning the presentation of prices/fares. Prices immediately began to rise in Oslo (and other deregulated city states) as a result. It has been argued by the NCA that, since there have been few new entrants in Oslo (and other price-deregulated markets), the licensing system needs to be relaxed. Indeed, counties have the right, not the obligation, to restrict quantities, so this is possible under the current legislation.

In Oslo and Norway, generally taxi drivers have little freedom. Licences are not tradable and must be returned to the state if the owner decides to leave the market. Drivers must be assigned to a prescribed dispatch service and can only operate within the county. More accurately, the MTC does not allow journeys to start and end outside the county where the taxi is registered.

Taxi firms operating in Sweden enjoy considerable freedom. Once drivers have passed a rigorous suitability test, which encompasses trade skills, financial and personal suitability, they can operate in any part of the country[18]. Moreover, there is no requirement for them to belong to a dispatch service. This has greatly increased the number of taxis in operation.

Impact on consumers

In London, consumers can be confident that their driver will have a detailed knowledge of the street layout. They can also be assured that no matter which cab they select, the fee will be the same (as set by the meter). This mandatory fare is set by the PCO using a cost formula and approved by the TfL board, which is chaired by the Mayor of London.

In Denmark, consumers receive price protection in the form of a maximum fare. Since 2001 a Weighted Cost Index (WCI) has been used to set these maximum fares in the Copenhagen region (which covers about half of all taxies in Denmark). The index, which is made in co-operation with Statistics Denmark, may be overridden in exceptional circumstances, such as abnormal rises in petrol prices. As in London, different fares apply to different times of day. There are typically also additional charges for baggage handling and for more than four passengers.

In Norway (Oslo), the Competition Authority believes that fare deregulation has worked, but the Consumer Council has voiced some concerns. Prices have been more variable.

In Sweden, the increase in supply of taxis since deregulation has reduced waiting times. There is also greater consumer choice—some firms market themselves as being environmentally friendly while others specialise in business clients. Smaller and cheaper vehicles have entered the market to satisfy cost-conscious private consumers. Prices climbed after deregulation, although this coincided with the introduction of value-added tax on taxi fares at a rate of 25%. More recently, prices have been growing in line with inflation and have tended to be higher in rural areas where there is less competition or higher costs.

[18] Applicants must have €10,000 and pass a test conducted by the Swedish Road Administration. They must also have no convictions for serious crime.

11. Recommendations

In this closing chapter, we present our conclusions on what the review has revealed about the regulatory structure in Ireland and on how we recommend that it should evolve. We have developed these recommendations from the research evidence from Ireland and overseas, and from a series of discussions that we have had with the inter-departmental steering group and other stakeholders. In presenting them, we set out, where appropriate, some of the options considered before reaching a final position.

Our conclusions are presented under the headings used to structure the original brief for the review: the appropriateness of current structures; governance and accountability; adequacy of existing mandates and; effectiveness and cost comparisons. We begin, though, with an additional category to cover more generic points.

It should be noted that in relation to financial regulation, the continued turbulence in international markets, recent developments affecting the Irish banking system and continuing discussions on improvements to the international system of regulation make it difficult to draw definitive conclusions on the different national models. We should also note that most of our recommendations relate to core economic regulation issues and are therefore generally less applicable to the Health and Safety Authority (HSA).

General

The need for continued regulation

It would be wrong to miss the obvious question of whether or not there is a continued need for regulatory structures in the sectors used as case studies. Changes in markets, technology and competitive drivers are rapid and continuous. The legislative and organisational frameworks set up to deal with one set of market conditions are much harder to change or remove once in place, even when the original set of problems that they were set up to address have moved on.

We considered this issue in detail when looking at market conditions within Ireland in the selected sectors and also when looking at how regulatory policy internationally has been evolving. Clearly in many areas there has already been a rolling back in regulatory coverage—in telecoms, for example, and in parts of the energy sector. There have also been examples of regulation becoming lighter in touch in some sectors and countries—financial services being an obvious example. Most jurisdictions, including Ireland, have already demonstrated a willingness to reduce regulatory requirements when the need for change has become evident.

Our overall conclusion, however, is that *there remains a strong case for continued regulation in certain sectors*. Progress towards genuinely competitive markets remains slow in some sectors. Recent developments in the financial markets are

likely to result in a tighter approach to regulation rather than a further rolling back. In many areas, EU directives place a legal requirement on member states to implement regulation (while limiting its scope in some areas) with no national discretion to do otherwise.

In telecoms and energy, we believe that regulation is still required in some sectors of the market, but that the presumption should be towards continued roll-back of controls as competition continues to increase, although in the case of energy, regulation of the natural monopoly transmission and distribution parts of the business is likely to be required on an ongoing basis.[1] Objective tests need to be applied on a more systematic and regular basis to check at what point competition is sufficiently well established to roll back further in the potentially competitive segments of these industries—based, for example, on tests of market dominance, price trends and efficiency of investment.

In other sectors, especially where consumer protection remains an objective alongside economic regulation, continued market supervision will be required—in civil aviation and health and safety for example.

A restatement of the case and objectives for regulation

Regulation does not usually attract a good press. Businesses see it as intrusive, a cost burden and commercially unaware. Consumers see it as failing to protect them against price rises and inadequate quality of product and service. Politicians question the costs and bureaucracy involved. These views are by no means unique to Ireland, and were evident in most of the comparator countries where we were able to take soundings from business representatives. Within Ireland, though, some specific issues and opinion emerged from our research. The regulatory system was seen to have evolved in an *ad hoc* way, with inconsistencies and overlaps in responsibilities. There had been "mission creep", with regulators taking or being given additional tasks that had no obvious fit with their core purpose. The case for continued regulation, even where EU directives make it non-negotiable, was not being made clearly.

On the basis of our previous recommendation on the continued role of regulation, *we believe that a restatement of the overall strategy, principles and objectives of regulation would be helpful.* We do not see this as involving changes to legislation or structures. It is more of an overarching statement of principles that will help ensure:

- greater clarity of overall and sectoral regulatory mandates;
- a more consistent approach across the regulated sectors;
- more regular and systematic reviews and revisions of mandates and structures; and
- better business, consumer and political understanding of the need for regulation.

[1] As previously pointed out, the EU Framework for telecoms considerably limits the scope for regulation to markets where one or more firms enjoy a dominant market position.

Appropriateness of current structures

Continued case for independent regulation

In most cases, economic regulation in Ireland follows generally recognised best practice in being delivered through independent regulatory agencies. While such agencies receive their mandates through legislation, have their key appointments made by government, may be subject to ministerial directives and must demonstrate accountability to the executive and political arms of government, they are given sufficient independence of action and in many cases funding to satisfy the regulated market that they are empowered to make objective decisions. This is not the only model, however, and in Scandinavia in particular the regulators are generally branches within government ministries, rather than independent legal entities. There was no evidence from our research that the Scandinavian model produces poorer regulatory outcomes, and in fact the approach includes safeguards that enable the regulators to act with a degree of independence. This approach may not be sustainable, however, since the third legislative package on EU electricity and gas markets proposes that the regulatory authority be legally distinct and functionally independent of any other public or private entity.

In general, however, we found that the form of legal structure and relationship with government was not in itself a determinant of effective or independent regulation. Legally, independent regulators have formal obligations and accountabilities to government, while regulators that sit within government benefit from safeguards that protect their independence of action. It is the degree of effective independence rather than the precise form of legal structure that is important.

On that basis, *we recommend that the independent status of the relevant regulators should remain unchanged*. This will maintain the characteristics and advantages that have built up over time with the independent model, such as more flexibility in recruiting and retaining specialists. In addition, any attempt to absorb regulation into government would create a perception of reduced independence and of political control that may be damaging to market confidence. This would almost certainly undermine regulatory credibility, which we have noted is extremely important.

Merging of functions

There were a number of examples from the international research of regulatory functions being merged into larger "super-regulators". These included:

- New Zealand, where regulation of a number of sectors is combined with the competition agency;
- Denmark and the Netherlands, where the same combination of sectoral regulation and enforcement of competition has been created; and
- Germany, where a super-regulator covering a number of network-based sectors has been established.

The perceived advantages of the approach include greater consistency in policy, reduced overlap and duplication of functions, more efficient use of technical

expertise, reduced risk of regulatory capture and an opportunity to reduce administrative costs. All of these are appealing objectives and, if achieved, would mitigate many of the concerns previously noted about the *ad hoc* evolution of current structures. Additionally, there is some evidence from the research that integrated regulation, in Germany and the Netherlands for example, is less costly to administer.

We have considered a range of options for restructuring.

- The full integration of all regulatory and competition agencies into a single super-regulator. Although the international comparisons revealed various combinations of economic and competition authorities integrated into single bodies, none had gone to the full extent of integrating every component of the regulatory framework. We see more risks than benefits in this radical option—for example, loss of focus, lack of transparency and reduced accountability.
- The creation of a single economic regulator that would be separate to the Competition Authority. This would effectively involve merging the existing economic regulators, ie, the Commission for Aviation Regulation (CAR), the Commission for Energy Regulation (CER), ComReg and the proposed new Dublin Transportation Authority (DTA), which the Commission for Taxi Regulation (CTR) has already been merged with. Such an agency would have more commonality of interest than the overall super-regulator model described above.
- A more limited merger of the CER and ComReg into a combined energy/communications network regulator. There would again be some benefits in such a move. Economic regulation has to deal with similar issues in both cases, eg, cost of capital, appropriate rate of return, etc. The differences between the sectors would not appear to be any greater than the differences between communications and postal services, which are already combined within the remit of a single regulator. It is also the case that the need for regulation seems to be declining more rapidly in communications than in energy so such a merger would permit a transfer of resources from an area where they are no longer required. The European Commission's proposals on the third internal market will have implications for the function and structure of energy regulators and these will need to be considered when examining the case for a merger.
- Shared support and administrative services. The CER and ComReg have a combined staff level of around 170 people, which is not that large an entity. There may well be scope for savings through sharing an administration and support services. Indeed, it might be possible to go further and have shared legal and possibly economic resources, although this would arguably come close to a full-scale merger.

Of these options, we would not recommend the first—there is no evidence from the research to confirm the potential benefits and we see it as too high-risk an approach at this stage. For similar reasons, we also do not favour the second option.

We do, however, see more merit in the third option—bringing CER and ComReg together. They are of a combined scale that should make it possible for efficiencies to be gained. The principles of regulating network services are similar and there are examples internationally of this approach being adopted. Also, as indicated, the scale of regulation required in telecommunications continues to decline and integration may provide a more flexible approach to managing the two sectoral resources. The business case for a merger would need to be developed and assessed in detail before a final decision could be taken. *We therefore recommend the preparation of this case as the appropriate next step.* This need not await the first cycle of formal remit reviews that we recommend later in this chapter.

As a minimum, or as a first step, we recommend the fourth option as an interim stage. We have not considered the shared service option for other regulators, for a number of reasons—the CTR has been merged with the DTA; we have separately mentioned the possibility of the CAR and the IAA coming together; the Financial Regulator already shares resources with the Central Bank of Ireland, and the HSA's remit is markedly different from the other regulators.

We also believe that an important early step is to review and refresh the remits of the existing individual regulators and to deal with overlaps, inconsistencies and lack of fit within the current structures. Otherwise, any merged body would simply absorb existing weaknesses in the system and perhaps make them more difficult to isolate and remove.

An exception to the above is the position of the CAR. As previously noted, it is a relatively small agency. It has certain other functions in terms of licensing various activities and overseeing the travel trade, but these are areas where some reform and streamlining of services is possible. *One option would be to merge the CAR and IAA* thereby combining functions that are undertaken jointly by aviation authorities in most of the other countries examined. One obvious difficulty here is that the CAR currently regulates the IAA's charges for airport terminal services. It would seem undesirable to have the regulator in effect regulating itself (although the Direction Générale de L'Aviation Civile—DGAC—in France does in fact do that). That responsibility would probably need to be assigned elsewhere. The IAA was not included in the remit for the review and without having examined its position we cannot recommend such a change at this stage. However, *we do recommend that it is separately considered as an option.* As with our recommendation on the CER and ComReg, a full business case would need to be prepared, but this could begin at an early stage.

Another alternative for the CAR would be to merge it with the DTA into an overall national transport regulator. We do not have sufficient information about how the new DTA will operate to offer any conclusions as to whether that would make a logical fit.

The growing convergence between electronic communications and broadcasting suggests that there might be potential for merging of regulatory bodies in this area. Legislation to reform broadcasting legislation and to merge the existing Broadcasting Commission of Ireland (BCI) and the Broadcasting Complaints Commission (BCC) has been published. Neither body was included

in the remit for the review. Without having examined them we cannot therefore recommend such a change at this stage, although we do recognise the merit in considering the option.

Reallocation of existing roles and responsibilities

We have noted in the report the tendency for "mission creep" in regulatory agencies, with additional functions and tasks being added at the expense of a focus on core objectives. This is not a uniquely Irish problem, having been noted in many of the comparator countries. Few energy regulators, for example, have a simple focus on economic regulation, but instead they have been given a mix of wider responsibilities in, for example, renewables, fuel poverty or carbon dioxide (CO_2) reduction.

The two main areas where we found possible overlap or dilution of focus were in competition policy and consumer protection, both areas where there is an existing, national body—the Competition Authority and the National Consumer Agency[2]. There were also some instances of overlap regarding health and safety responsibilities (an issue also evident elsewhere, in Denmark and New Zealand for example).

In relation to competition policy, the roles of competition authorities and economic regulators should in theory be quite distinct. The former intervene on an *ex post* basis, where markets that should be competitive are not actually functioning that way, while the latter act on an *ex ante* basis, seeking to create a competitive market place. Nevertheless, both require similar types of industry and technical expertise in order to operate effectively. Moreover, there are examples from the international research of the two roles being conducted by the same organisation, in New Zealand and the Netherlands in particular. There are potential problems with the combined approach, such as added difficulties in scrutiny and transparency or insufficient focus being given to individual sectoral needs. In the two countries mentioned, sectoral regulation is carried out by distinct departments or "chapters" within the integrated body, often with separate governance and accountability procedures.

As indicated earlier, *we do not believe that the case for integration of sectoral regulation and competition policy is currently strong enough to make a recommendation that it should be pursued.* It could instead be one of the options considered as part of regular remit reviews, particularly in sectors where the scope of regulatory control is being rolled back in any case. We noted that ComReg has concurrent powers with the Competition Authority to apply competition law in the communications sector. In general we suggested that it was unclear that such powers enhanced the regulatory powers already available to ComReg to address problems of dominance. It must be asked whether such a duplication of functions is beneficial. *We do not believe that similar powers to enforce competition law should be extended to other regulatory bodies.*

Regarding consumer protection, there was consistent feedback from our research in Ireland that regulators were not adept at encouraging and

[2] As previously noted, the merger of the Competition Authority and the National Consumer Agency was announced in the 2009 Irish government budget.

responding to consumer interests. Regulators have been assigned a number of consumer advisory and protection functions, but these are not generally at the core of their mandate. In most cases the regulators were established before the National Consumer Agency (NCA). There is a serious risk that consumer interest will lose out to the producer viewpoint within regulatory agencies. Producers are generally far better organised and resourced than consumers. The tendency is exacerbated in the regulated industries because of the sheer complexity of the issues involved. This means that there is a real need for stronger representation of consumer interests within the regulators and the NCA would seem to be the logical agency to contribute to this.

The problem is especially acute with regard to issues such as pricing reviews, which have largely become a forum for insiders and are not seen by outsiders as transparent. This undermines the legitimacy of the price review process in the eyes of customers. Again, the NCA would seem to be the logical agency to play a role here. The merger of the NCA with the Competition Authority will hopefully enhance its ability to do so. In order to eliminate any perception that the consumer voice is not being heard and to enhance the overall transparency of the process, it might be useful if the price review process were to incorporate some form of public hearing.

In addition, it may be appropriate in some cases for some of the regulators' other consumer protection functions to be transferred to the NCA. We would, however, suggest that the Financial Regulator retain its existing role in the area of consumer protection as it has been seen to fulfil this role effectively.

Finally, on health and safety issues, we identified areas where economic regulators had responsibilities that did not obviously fit with their core purpose. The clearest example that we found was the CER's responsibility for setting safety standards for individual electrical contractors and gas fitters. We recognise that such responsibilities must unequivocally belong to some organisation, as should the resources required. However, it is difficult to see that such a role sits logically with the CER's functions of economic regulation. It has required the CER to develop new skills and incur additional costs, and it is not clear that this is a role suited to an economic regulator. We recognise that the HSA's role is primarily in the more traditional occupational health and safety sphere. So it is not self-evident that it should take over this responsibility from the CER, but it would represent a more logical "home" than an economic regulator. In the UK, for example, the Health and Safety Executive (HSE) has responsibility for setting electricity safety standards whereas in New Zealand such responsibility rests with the Ministry of Economic Development.

We note that there are considerable overlaps between the HSA and a variety of other agencies, all of which have health and safety responsibilities. We note also that up to now there has been no cataloguing of the roles and functions of the various agencies with responsibilities in this area. We welcome the fact that the HSA is currently engaged in such an exercise. Once it has been completed consideration needs to be given to the scope for rationalising the roles of different bodies.

Structured co-operation across regulators

Concerns about inconsistency of approach between regulators were commonly expressed internationally and within Ireland. One option for addressing these that does not need to involve policy or structural changes is to *improve the level of communication and co-operation across the regulators.* In the UK, for example, the Joint Regulators Group brings together the leaders of the regulatory bodies on an approximately quarterly basis. The minutes of their meetings are published to provide transparency. As an example, the June 2008 minutes cover work being done to test for consistency in the imposition of financial penalties by regulators, future joint work on the case for compliance incentives rather than penalties and work on regulators' financial frameworks. We should stress that we have not investigated the impact and effectiveness of the Group's work. However, *we recommend that a similar approach in Ireland would be a relatively cost-effective means of demonstrating a more structured and transparent commitment to consistency and exchange of good practice.*

Governance and accountability

Regulatory performance and effectiveness

Performance monitoring and evaluation emerged as a substantial weakness during our research. It was unclear from our discussions with sponsoring government departments how they would measure the performance of the regulators that they are responsible for, or indeed define what good performance should look like. Regulators themselves tended to report on activity measures rather than on impact or effectiveness. Again, this was by no means a unique problem in Ireland and in some countries we found even less clarity on what good performance was and how it could be measured. In conducting the review, we have looked at evidence on certain variables that might indicate economic regulatory performance, such as price trends, market dominance, switching trends and costs, etc. Some is relatively easy to source, often from international organisations and associations (the main base on which the telecommunications regulator in Denmark reported that it tracks its performance). However, this is not universally the case, and there is no consistently accepted set of metrics on which to base a performance evaluation. As a result, the "default" position is generally to rely on statements of activity—reports published, actions taken, etc, which clearly do not equate to effectiveness. Also, regulators are left able to defend their performance by adopting, or rejecting, measures on a selective basis.

Nevertheless, there were some interesting and innovative approaches. For example, the UK Financial Services Authority has recently adopted a detailed, systematic approach to performance appraisal that combines both quantitative and qualitative analysis.

We recognise that regulatory effectiveness is difficult to measure, in particular in terms of isolating the effects of regulation from other factors such as external economic or technology trends—we have experienced that difficulty ourselves in the course of this review. However, without a clear, accepted performance evaluation framework it is impossible to address a number of fundamental questions, such as tracking progress towards competitive markets and assessing when it would be appropriate to change or roll back regulatory policy. It also makes it difficult for regulators to demonstrate their continued value and legitimacy.

We do not have a specific recommendation to make on performance measurement methods, which in any case will need to be tailored to the circumstances of each sector and each regulator's remit. We note, for example, that ComReg and the HSA have commissioned external reviews to measure the impact and benefits of particular regulatory interventions. However, *we do recommend that departments and regulators recognise their common interest in developing such methods and that this should be a priority for early action.* A similar point was made in the recent OECD report on the public service.[3] , and indeed participation in any future OECD or EU review projects could be useful in helping to develop appropriate methods. *We also recommend that the operating costs of regulators should be a part of the performance evaluation process,* for reasons that we shall return to later.

Industry and consumer panels

The business and consumer advisory panels incorporated in the Financial Regulator model are seen to have performed a useful role. There may be merit in having similar panels with similar powers in the case of some of the economic regulators, notably the CER and ComReg. We note that ComReg currently has a consumer panel; it is relatively small with only six members, who are chosen by the regulator. While in no way expressing any criticism of the individual members, it needs to be recognised that having the regulator appoint its own consumer panel may not be the most appropriate model.

We recommend that a consumer panel with similar powers to those enjoyed by the Financial Regulator consumer panel, including the power to review the regulator's proposed budget for the following year and with some independent resources to fund necessary research, should be established in the case of the CER and ComReg. The panel could be appointed by the minister, and should include representation from the NCA. We also think that such panels would need to be larger than the existing ComReg panel, as they need to represent business consumers as well as domestic customers in energy and communications. We therefore further propose that the minister responsible consults with business representative groups to ensure adequate representation for small and medium-sized enterprises (SMEs) on the consumer panel. We do not see any need for a panel to represent the regulated firms, as these already appear to have adequate access to the regulatory agencies.

Parliamentary scrutiny

Effective parliamentary scrutiny of regulatory policy and implementation is recognised as essential. We found no examples in our research of there being no line of accountability to parliament. The direction that the line takes does of course vary—via ministers or directly to members. And the form that it takes also varies, from the simple submission of an annual report that may or may not lead to questions, to a more intense level of direct scrutiny by parliamentary committee. The most challenging form of scrutiny that we were able to identify was in the UK parliament, where sector-specific, cross-party committees with research support regularly call in regulators to review policies and performance.

[3] OECD, (2008).

The Oireachtas (the Irish parliament) now has a specific committee for regulatory affairs. Members themselves felt, however, that they did not have the detailed knowledge necessary to perform an effective scrutiny function. They also felt that there were insufficient research resources available to them both to inform their questions and to assess the answers given. In these circumstances, regulators may be able to divert scrutiny by focusing on technical matters or matters that would be more appropriately handled elsewhere.

We believe that soundly based parliamentary scrutiny is an essential part of maintaining the legitimacy of continued regulatory intervention and its longer-term effectiveness. We have not investigated the extent of resources available to the Oireachtas committee and therefore cannot make a judgement on it. However, *we do recommend that it should be kept under regular review and adjusted if necessary to ensure the most effective scrutiny possible.*

Multi-member commissions

We examined the available research on the appropriate structure of regulatory commissions, as well as reviewing the range of models evident from the international fieldwork. Generally the international pattern of regulatory governance is one of collective decision taking by an Authority or board of directors with a lead executive responsibility held by a chief executive officer (CEO) or director general. The Scandinavian countries bear the closest resemblance to a single regulator approach, albeit within the confines of a non-independent ministerial entity.

We believe that a multi-member commission is preferable to single commissioners and the case for this is set out earlier in the report—a three-member structure is the most common variation. We recognise that, particularly for small regulatory agencies, a multi-member commission may appear top-heavy and expensive. However, in the interests of effective regulation, we do recommend that it should be the norm in all cases.

Appeals mechanisms

Experience of the framework and process for appeals is patchy with a general view that it is currently not satisfactory, but without a clear consensus on what would be preferable. Again, this is not a uniquely Irish issue and the international research revealed a diverse approach to appeals mechanisms, including sector-specific panels, cross-sector panels and direct reliance on the courts. We believe that improvements in the process are required and *recommend that a single, cross-sector panel is the most appropriate option for the economic regulators* (in this case therefore excluding the HSA). In making this recommendation, we recognise that a number of complex issues need to be considered in designing the remit and structure of the panel:

- decision-changing powers versus referrals back to the regulator;
- which decisions could be appealed against and by whom;
- the setting of time limits for both making and resolving appeals; and
- the appropriate judicial level for hearing appeals against panel decisions.

In our view there is a need for a specialist appeals panel. Incorrect regulatory decisions impose significant costs and an effective appeal mechanism including a right to appeal against pricing decisions would itself provide a strong incentive for regulators. We recognise that it is not possible under the Irish legal system to exclude an ultimate right of appeal to the courts, although it may be possible to limit appeals against decisions of the appeal panel to points of law. We recognise that this may lengthen the decision-making process, but the costs of this, assuming the regulator's decision is found to be correct, are temporary whereas the adverse cost of bad regulatory decisions are long-lasting. In addition, we believe that allowing appeals against pricing decisions would restore confidence in the regulatory process, which is currently lacking. An option here would be to give the NCA power to appeal pricing decisions on behalf of consumers rather than giving a right to every individual.

Adequacy of existing mandates

Regular formal review

We identified a number of threats and challenges to the adequacy and appropriateness of existing mandates: mission creep, regulatory capture, market changes and technological advances. Failure to deal with these challenges represents a fundamental threat to the effectiveness and legitimacy of regulation. Anticipating them and being flexible enough to respond to them are essential. Generally this has not happened to date, resulting in the concerns over inconsistencies and overlaps that we have identified. We should add here that once again this is not a unique problem to Ireland and the same issues were apparent internationally. However, there are examples of other countries being more responsive and flexible in adapting to changing requirements, for example in New Zealand and the Netherlands.

We therefore recommend that each regulator should be the subject of a formal mandate review by government on a regular basis, say every five years.[4] The review would identify changes, actual and anticipated, in market conditions, reset regulatory objectives where necessary and propose any legislative and operational changes required. It should also be sufficiently fundamental to identify if there is a case for changing the regulatory structure, for example through integration with other agencies. There are some risks attached to such a process, such as creating market uncertainty in the period preceding each review and creating a febrile lobbying environment. Nevertheless, we believe that these are outweighed by the advantages of a regular and fundamental review procedure.

Advice to ministers

Currently the relevant legislation in Ireland provides for economic regulators to give advice to ministers. This is by no means unusual internationally. Whether by statute or practice, most regulators we researched had a role in providing advice to ministers. It does, though, raise the question of whether it is appropriate for regulators to have a position of influence over ministerial decisions, prejudicing their perceived independence. On balance we believe it is

[4] OECD (2008) p 260 makes a similar recommendation in respect of all state agencies. *"Agency status should be reviewed every five years to determine whether or not the services are still needed and if it is the most appropriate organisational structure for delivering the services."*

just that—a question of balance. Regulators have specialist knowledge and expertise that will be valuable to ministers in framing policy and it appears legitimate and sensible for them to be called upon to provide it. If this were to develop into playing a dominant role in policy formulation, that would be inappropriate. However, there would be a role here for government departments in evaluating the advice provided and ensuring input from other relevant sources. Departments of course need to retain sufficient in-house expertise to enable them properly to discharge their functions. Otherwise, *we do not recommend any change in the current framework.*

Stress-testing of regulatory structures and mandates

The current instability in global financial markets is proving to be a major shock and challenge for regulatory structures worldwide. Approaches that until recently were regarded as good practice, in the UK for example, have now been shown to have been inadequate in their core task of prudential supervision. It is conceivable that similar shocks could affect not just the financial markets in future, but other regulated sectors as well—geopolitical threats to energy security for example, or fundamental breakdowns in telecommunications networks. These may not be for regulators to solve. Still, it would be prudent for them to have procedures in place for risk assessment, scenario planning and stress-testing of their current mandates and operations. What could conceivably go wrong, and how would it affect regulatory functions, if at all? *We have not examined the regulators' current approach to such stress-testing, but we do recommend that it should form part of their risk assessment procedures.*

Effectiveness and cost comparisons

Cost structures

The evidence from our international comparisons of the costs of operating regulatory structures is that in many sectors such costs are higher in Ireland than elsewhere. We have sought as far as possible to ensure like-for-like comparisons and to take into account any exceptional circumstances in Ireland. We also recognise that as a small country the relative costs of regulatory structures would be expected to be higher. However, there are other small countries in the comparative analysis. There may be a number of reasons for higher costs, such as high reliance on external consultants or a higher propensity for litigation. There may be insufficient scrutiny of costs, for example where the bulk of regulator income is generated from industry levies.

As we have said earlier, low-cost regulation is not the same as good regulation. Nevertheless, we do believe that there is sufficient evidence to conclude that it is generally more costly to operate regulatory structures in Ireland than in the comparator countries. *We recommend that the reasons for this are explored further.*

It is also important in relation to costs that the process of setting industry levies is as transparent as possible. The Financial Regulator's industry panel provides a valuable mechanism for this.

Targets for achieving competitive markets

Progress towards achieving genuinely competitive markets through economic regulation has been varied in Ireland, as it has in other countries. It is happening, though, as shown by the roll-back of regulation in sectors of the

energy and telecoms markets for example. There is still a way to go, however. This is particularly true in the energy sector where liberalisation is far more complicated than in telecoms,. Again we have pointed out that this is partly the result of factors that are beyond the regulator's control. In particular, the regulator has secured some divestment of the Electricity Supply Board (ESB) generating plant and authorised some new entrants. In addition, the single electricity market (SEM) will expand the market. The concern is that regulation alone is not capable of delivering the lowest possible energy prices. This is not because of any shortcomings on the part of the regulator. It is attributable to limitations that are inherent in the regulatory process. Various independent reports have all indicated that even within the context of an SEM and an inter-connector link with Great Britain, further restructuring is required to prevent the electricity market from being dominated by a duopoly. This is ultimately a matter for government rather than the regulator. We simply note that regulation by itself will not suffice to provide Irish consumers with the lowest possible prices and that this has wider implications for industry competitiveness.

We have raised already the lack of a systematic framework for measuring progress towards achieving the desired economic regulatory outcomes. *If such a framework is developed as recommended, it should then be possible to set some targets for the timescale over which outcomes should be achieved and to track progress towards them.* There is a risk of such targets being artificial and perhaps distorting market behaviour. However, if properly based on objective tests of market performance, they would provide regulators and stakeholders with specific and focused priorities.

