

Business Standard

When the regulated become the regulator

Effectively involving the regulated entities in the rule-making process and crowd-sourcing ideas help create a better-governed market economy

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On October 4, 2023, market regulator Securities and Exchange Board of India (Sebi) invited suggestions from the public for a comprehensive review of a large chunk of its regulations, with a one-month timeframe for responses. Several other regulators have also initiated similar exercises, in line with the government's proposal in the Union Budget for 2023-24.

The Budget stated: "To meet the needs of *Amrit Kaal* and to facilitate optimum regulation in the financial sector, public consultation, as necessary and feasible, will be brought to the process of regulation-making and issuing subsidiary directions". It also proposed: "To simplify, ease and reduce cost of compliance, financial sector regulators will be requested to carry out a comprehensive review of existing regulations. For this, they will consider suggestions from public and regulated entities."

A related intervention is the Competition (Amendment) Act, 2023, enacted in April, which mandated the regulator to consult the public in making regulations and

prescribed the manner of such consultation. It also mandated periodic review of existing regulations. These two interventions, though made in the context of the Competition Commission of India and financial sector regulators, carry a broader message for every regulator.

It is important to appreciate the context. To deal with the challenges of a market economy, business reforms mandated regulators to govern markets through regulations. It is, however, not an easy task to craft regulations. Various tools and procedures have been developed to ensure the right quality and quantity of regulations. Yet, these regulations have fallen short in some aspects, prompting the need for the above two interventions.

A regulator is often accused of lacking democratic legitimacy. Public consultation is generally used to bridge the democratic deficit. Sebi started public consultation in 2002. Several regulators emulated the practice. This found a place in some regulatory statutes. In 2016, the Supreme Court exhorted Parliament to mandate consultation with stakeholders for making laws and regulations.

Regulations, once made, remain in the statute book even if they have lost relevance over time, or the costs of such regulations outweigh the benefits. It is necessary to weed out regulations that have run out of time, context, and relevance and make them contemporary and in tune with the requirements of business in a dynamic setting. Ease of doing business is a declared policy intent and regulations and regulatory changes must address that as well, without compromising on minimising the risk of market failure arising from unbridled market forces. An example of this initiative is the Reserve Bank of India's (RBI's) establishment of the Regulations Review Authority 1.0 in 1999, followed by Authority 2.0 in 2021, which aimed to reduce the compliance burden on regulated entities. On the recommendations of the Authority 2.0, RBI withdrew 714 circulars, in addition to other actions.

In the interest of promoting ease of doing business, every regulator should engage with the public to both formulate new regulations and review existing ones. For this purpose, it must release drafts of proposed regulations, not just the regulatory proposal. It must periodically review existing regulations to ease the compliance burden. These principles should also apply to subsidiary directions (such as orders, circulars, guidelines, etc), ensuring that they do not bypass the due process.

Though the practice of public consultation is not new and is a necessity, its sufficiency depends on the manner and intensity of consultation, which varies from regulator to regulator. Modern regulators use various methods — online, offline, and face-to-face — to reach out to stakeholders. They engage with them in

different formats — advisory committees, working groups, roundtables, seminars, workshops, and discussion papers. They often use technology to capture the provision-wise views of stakeholders.

Public consultation is effective for making regulations when the regulator presents a draft of the proposed regulations, along with the regulatory impact assessment of such regulations. This enables the regulated to appreciate the rationale and implications. It is meaningful for reviewing regulations if it is done periodically and when the regulator presents how each regulation, sub-regulation, and clause of regulation aligns with its intended objective. It is comprehensive if it covers both regulations and subsidiary directions. It is efficient if it uses technology. Hopefully, regulators will soon upgrade the process of public consultation without further prodding from the government.

Public consultation, however, often is passive participation, as stakeholders limit their comments to the proposals on the table, and have a short window to formulate their views. It will be much more rewarding if they can have active participation in making/ reviewing regulations.

A regulator, though closer to the market as compared to its principal, is still one step removed from the market compared to the regulated entity. It substantially depends on the regulated for understanding the market developments and designing solutions to emerging concerns. The regulated have first-hand experience of the market and its concerns, and, given their numbers, the universe of practical solutions they have is much larger. They must be given an opportunity to ask for/suggest new regulations and changes in existing regulations at their convenience to address market concerns and promote ease of doing business.

The regulator should periodically examine proposals coming from stakeholders and publicly comment on those proposals, similar to how public comments on draft regulations are sought by the regulator. It should take forward the proposals it considers useful for making regulations, following due process. In addition to making the regulators' consultation process more meaningful and effective, a *regulatory bridge* enabling the regulated entities to propose regulations will herald a major change in the process and mode of making regulations for a well-regulated market economy.

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First Published: Oct 25 2023 | 9:59 PM IST

Page URL :https://www.business-standard.com/opinion/columns/when-the-regulated-become-the-regulator-123102501246_1.html