

# TIT FOR TAT: THE ART OF RESPONSIVE REGULATION – HOW AGENCIES CAN MOTIVATE REGULATED FIRMS TO BECOME VIRTUOUS

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## INTRODUCTION

The power of a regulatory agency to conduct inspections is a fundamental feature of every regulatory scheme. This power gives a designated agency official the authority to enter and inspect private property without the occupier's consent and without a court warrant or order. These powers provide the authority for officials to take certain actions as part of the inspection including requiring the production of certain documents or information or seizing things that afford evidence of an offence.<sup>1</sup> Without such powers, a regulatory agency would be unable to carry out its mandate of protecting the public interest by ensuring regulated actors comply with the requirements of a regulatory scheme.

Inspections are often the primary point of contact between a regulated actor and the agency. They also serve as the backbone of every agency's compliance and enforcement program, which at its core seeks to answer two very basic questions that ultimately inform how to allocate scarce agency resources: "who to inspect?" and "how to respond when a violation is detected?" The effectiveness of an agency's compliance and enforcement program that answer these two core regulatory functions can be measured on three levels: (a) *from the perspective of the regulated firm* – does the program motivate the regulated firm to become "virtuous", by voluntarily adopting self-audit functions that seek to identify and correct violations without the need for agency intervention? (b) *from the perspective of the regulated sector* – do other regulated firms in that sector believe that investing in self auditing functions is in their self-interest? *from the perspective of the public*: does the program instil greater public confidence that the agency is an effective regulator, is acting to protect the public interest and is not subject to regulatory capture?

This paper seeks to examine these questions with a focus on the Ontario Ministry of Environment and Climate Change's (MOECC) compliance and enforcement program. The first section of this paper discusses how courts have considered inspection provisions in light of section 8 of the Charter and ends with a description of the way inspection powers in provincial environmental protection statutes are circumscribed to be consistent with section 8 and designed to satisfy other policy objectives. The second section briefly introduces the theory of responsive regulation and the regulatory pyramid and discusses some of the insights that literature suggests for what makes an effective compliance and enforcement policy – namely to what extent the policy motivates regulated firms in a particular sector to become and remain "virtuous" by adopting self-auditing functions. The final section describes MOECC's compliance and enforcement program including how it determines which regulated actors to inspect, how a response to a contravention is

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<sup>1</sup> See s 156 of the *Environmental Protection Act*, RSO 1990, c 19 [EPA] as an example of a general inspection power commonly found in environmental protection statutes in Ontario. Section 156 includes the power to require the production of documents – see cl 156(2)(g). See s 160 of the EPA as an example of a provision that authorizes seizures during an inspection.

formulated and ends with observations that responsive regulation theory would suggest for the MOECC program.

## REGULATORY INSPECTIONS AND SECTION 8 OF THE CHARTER

Soon after the introduction of the *Charter of Rights and Freedoms*, courts were confronted with challenges to regulatory inspection provisions and asked to consider whether they were consistent with section 8 of the Charter. When the decision of *Hunter v Southam*<sup>2</sup> was rendered, there was some doubt that such regulatory inspection powers would survive Charter scrutiny. In *Hunter* the Court was asked to consider provisions under the federal *Combines Investigation Act* which authorized inspectors, after obtaining prior authorization from a designated official, to enter private premises and seize documents. The powers were held to be inconsistent with section 8 of the Charter for the reason that they did not provide a prior authorization procedure before a search of the premises could be undertaken. According to the Supreme Court of Canada, there were two defects with the provisions that authorized the exercise of the search powers under the Act. First, the official that provided prior authorization was not sufficiently independent of the responsible regulatory agency. Second, the search powers were not appropriately circumscribed by only authorizing searches where there were reasonable and probable grounds that an offence had been committed.

For some time after the decision in *Hunter* there was a question as to how the Supreme Court would treat regulatory inspection provisions that authorized entry without prior authorization from an independent official and without reasonable and probable grounds that an offence had been committed. However in decisions that followed *Hunter* – the Supreme Court began to signal that a more flexible standard must be applied when determining whether a regulatory inspection provision authorized unreasonable searches, contrary to section 8 of the Charter. They agreed that a regulatory inspection was a search for the purposes of section 8 of the Charter – but they held that an inspection was not an unreasonable search if the statute clearly authorized the entry and the provisions authorizing the entry were appropriately circumscribed given the regulatory context. In other words, the court recognized that applying the *Hunter* standard to regulatory inspection would be impractical because of the central role they play in regulatory schemes: As La Forest observed in *Thomson Newspapers*<sup>3</sup> at page 507:

In many cases, this regulation must necessarily involve the inspection of private premises or documents by agents of the state. The restaurateur's compliance with public health regulations, the employer's compliance with employment standards and safety legislation, and the developer's or homeowner's compliance with building codes or zoning regulations, can only be tested by inspection, and perhaps unannounced inspection, of their premises. Similarly, compliance with

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<sup>2</sup> [1984] 2 SCR 145.

<sup>3</sup> [1990] 1 SCR 425.

minimum wage, employment equity and human rights legislation can often only be assessed by inspection of the employer's files and records.

Even if inspections may ultimately lead to enforcement actions including prosecutions, this does not take away from their predominant purpose of being one of compliance. As the court noted in *Comité paritaire de l'industrie de la chemise v Potash; Comité paritaire de l'industrie de la chemise v Sélection Milton* at page 421:

The underlying purpose of inspection is to ensure that a regulatory statute is being complied with. It is often accompanied by an information aspect designed to promote the interests of those on whose behalf the statute was enacted. The exercise of powers of inspection does not carry with it the stigmas normally associated with criminal investigations and their consequences are less draconian. While regulatory statutes incidentally provide for offences, they are enacted primarily to encourage compliance. It may be that in the course of inspections those responsible for enforcing a statute will uncover facts that point to a violation, but this possibility does not alter the underlying purpose behind the exercise of the powers of inspection. The same is true when the enforcement is prompted by a complaint. Such a situation is obviously at variance with the routine nature of an inspection. However, a complaint system is often provided for by the legislature itself as it is a practical means not only of checking whether contraventions of the legislation have occurred but also of deterring them.<sup>4</sup> (emphasis added)

The underlined portion of the above extract from the *Potash* decision seems to presage the jurisprudence that would develop in later years under section 8 of the Charter, where the courts sought to place limitations on the use of regulatory inspection powers to gather evidence for a regulatory prosecution. Specifically, the passage hints at the “predominant purpose” test that was later adopted by the leading case on this issue – *R v Jarvis*.<sup>5</sup> This paper will not delve into that issue or the jurisprudence, as it is canvassed in the paper by my colleague Paul McCulloch (see “Environmental Investigations – A Government Perspective”).

There are several factors a court will consider when determining if an inspection provision is constitutionally valid and authorizes reasonable search and seizures in the circumstances, namely:

- (a) the context of the power (whether it is criminal, quasi-criminal or regulatory);
- (b) the intrusiveness of the search power;
- (c) the reasonable expectation of privacy in the property searched; and
- (d) the purposes of the power.

The focus of the inquiry then is whether the legislation in question strikes the appropriate balance between a person's reasonable expectation of privacy and the state's interest to ensure it can effectively administer and enforce the regulatory scheme in question to protect the public interest. The Courts have repeatedly recognized that persons engaged in

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<sup>4</sup> [1994] 2 SCR 406.

<sup>5</sup> *R v Jarvis*, [2002] SCJ No 76.

regulated activity have a reduced expectation of privacy and for that reason will not apply the *Hunter* standard to regulatory inspection provisions.<sup>6</sup>

However even if the courts were not prepared to apply the prior authorization requirement set out in *Hunter* to regulatory inspections, they continued to scrutinize those provisions under section 8 of the Charter to determine whether the powers were appropriately circumscribed given the public purpose of the regulatory regime and the expectation of privacy by those being regulated. For example, in *Johnston v Minister of Ontario (Minister of Revenue)*<sup>7</sup> the Court of Appeal for Ontario struck down the inspection provisions in the Ontario's *Tobacco Tax Act* because they authorized a warrantless search of any commercial motor vehicle regardless of whether the vehicle was connected with the trade of tobacco or any reasonable grounds that the commercial vehicle contained evidence of a contravention of the Act. Arbour J.A. observed:

For a random search to be reasonable under s. 8, even in a case where the privacy interest affected is minimal, it has to be established that such a random search is the least intrusive method available to provide for adequate enforcement of the regulatory scheme.

Section 156 of the *Environmental Protection Act*<sup>8</sup> sets out the inspection authority of provincial officers under that Act and is typical of inspection provisions found in many MOECC administered statutes. The power provides provincial officers, who are designated by the Minister, to enter property without consent and without a warrant or court order, but the power is circumscribed in several important respects so that it is consistent with section 8 of the Charter. The following are the constraints that are typically imposed on the exercise of an inspection authority and other policy issues that typically arise in the drafting of inspection provisions:

- The power to inspect can only be exercised at “reasonable times”.
- A provincial officer can only enter a place, if he or she has a “reasonable belief” that a thing or activity that is subject to the Act can be found in that place. For instance, the provincial officer can enter into a place if he or she has reasonable belief that the place is required to be subject to an approval under the Act.
- Officers are required to identify themselves and explain the purpose of their entry.
- In 1998, the inspection provisions in the *Environmental Protection Act* and the *Ontario Water Resources Act* were re-introduced and structured to separate in one subsection the places a provincial officer could enter and in a separate subsection what things a provincial officer could do after entering a place. Because the provision was structured in this fashion, the Court of Appeal for Ontario held that the MOECC could not rely on its inspection powers to make telephone inquiries – inquiries could only be made as part of an inspection of a place. Those statutes have

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<sup>6</sup> *BC Securities Commission v Branch*, [1995] 2 SCR 3.

<sup>7</sup> 75 OR (2d) 558.

<sup>8</sup> RSO 1990, c 19.

- since been amended to include an express authority for provincial officers to make telephone inquiries.<sup>9</sup>
- Force cannot be used to execute an inspection. If an occupant refuses to allow a provincial officer to enter to a place, even though the provincial officer has lawful authority to exercise the entry, the only recourse is to obtain a court inspection order under section 158 of the EPA or to refer the matter to the Investigations and Enforcement Branch on the grounds that the person obstructed the provincial officer in carrying out his or her duties under the Act.<sup>10</sup>
  - The inspection powers cannot be used to enter any room that is used as a dwelling. A dwelling can only be inspected pursuant to a court inspection order under section 158. When drafting legislative provisions concerning inspection orders or warrants issued by the court, it is appropriate to expressly provide that if the application for the inspection order or warrant concerns the inspection of a dwelling the application should expressly advise the court of this.<sup>11</sup>
  - More current provisions concerning regulatory inspections provide that where an entry is exercised and property is damaged as a result of the inspection, the officer must restore the property to the condition it was in prior to the entry.<sup>12</sup>
  - Inspection provisions often expressly permit the officer to be accompanied by another person who has expert or special knowledge that is related to the purpose of the entry.<sup>13</sup>
  - Most inspection provisions under provincial environmental protection statutes permit inspections without giving the occupant prior notice of the inspection (otherwise known as unannounced inspections). However, recently in response to stakeholder concerns, some MOECC Acts that are to be administered locally require that prior reasonable notice of the entry be given to the occupant. An exception is provided where the officer reasonably believes that a contravention has occurred and that entry without reasonable notice is necessary to prevent or reduce environmental harm. There should be careful consideration before imposing a notice requirement on the power of entry, particularly if it is determined that unannounced inspections are necessary to effectively regulate the regulated actors that will be subject to the regulatory scheme.<sup>14</sup>

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<sup>9</sup> *R v Crompton* (2005), 78 OR 3rd 135. In 2009, to respond to that court decision, s 157.0.1 was added to the EPA and s 15.0.1 was added to the OWRA to expressly provide authority for provincial officers to make telephone inquiries.

<sup>10</sup> See s 184 of the EPA, s 184(1) provides that “No person shall hinder or obstruct any provincial officer or employee in or agent of the Ministry in the performance of his or her duties under this Act.”

<sup>11</sup> As an example of this, see s 26 of the *Lake Simcoe Protection Act, 2008*, SO 2008, c 23, specifically s 26(19).

<sup>12</sup> *Lake Simcoe Protection Act, 2008*, SO 2008, c 23, s 26(25).

<sup>13</sup> See s 26(9) of the *Lake Simcoe Protection Act, 2008*.

<sup>14</sup> See ss 26(11)-(12) of the *Lake Simcoe Protection Act, 2008*. The inspection power in the *Clean Water Act, 2006*, SO 2006, c 22 also contained a notice requirement – see s 62 of that Act. Other provincial statutes that deal with environmental protection matters also contain notice provisions that pre-date their introduction in MOECC statutes, such as the *Conservation Authorities Act*, RSO 1990, c C.27 – see ss 28(20)-(22), and the

- Some recent statutes have required that officers must complete a training course – the requirements of which are prescribed by the regulations – before exercising an entry power. This was included in recent MOECC statutes that were to be administered locally, largely at the request of the agricultural sector in response to their concerns that local officers entering agricultural operations understand how to deal with risks related to biohazards at an agricultural operation.<sup>15</sup>

## RESPONSIVE REGULATION AND THE REGULATORY PYRAMID

The theory of “responsive regulation” and the “regulatory pyramid” was first introduced by Ayres and Braithwaite in their seminal book *Responsive Regulation*.<sup>16</sup> The theory was advanced to bridge the divide between the two competing regulatory theories that emerged during the 1980s – the first believed that a strict enforcement approach was necessary to deter regulated actors from violating the law. The second competing theory took the opposite view calling for the use of persuasion as the primary compliance tool however critics charged that this was just another call for deregulation. Advocates of this theory asserted that strict enforcement was counterproductive because it undermined the potential for a cooperative relationship between regulated actors and the regulator and diminished a regulated firm’s motivation to adopt self-auditing functions. Ayres and Braithwaite attempted to bridge these two disparate theories through the conception of the regulatory pyramid – suggesting that an agency’s compliance and enforcement program must incorporate aspects from both theories and be calibrated so that it directs the appropriate response given the circumstances of a particular case:

The crucial question for Ayres and Braithwaite was “When to punish; when to persuade?” Their prescription was a ‘tit for tat’ or responsive approach in which regulators enforce in the first instance by compliance strategies, but apply more punitive deterrent responses when the regulated firm fails to behave as desired. Compliance, they suggested, was more likely when a regulatory agency displays an explicit enforcement pyramid – a range of enforcement sanctions extending from

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*Niagara Escarpment Planning and Development Act*, RSO 1990, c N.2, see s 28. Often these notice constraints are placed in statutes that are to be administered by local bodies as opposed to provincial bodies. In his report following the Walkerton Inquiry, Mr. Justice O’Connor spoke about the importance of ensuring that unannounced inspections be authorized in the legislation that was to regulate drinking water systems. He made a number of important recommendations concerning compliance and enforcement under his proposal for a *Safe Drinking Water Act*. See Part Two, Report of the Walkerton Inquiry, Chapter 13 in particular pp 452-455 at 454: “The Ministry of Environment’s inspection program for municipal drinking water systems should consist of a combination of announced and unannounced inspections. The inspector may conduct unannounced inspections when he or she deems it appropriate and least once every three years, taking into account such factors as work priority and planning, time constraints, and the record of the operating authority.

<sup>15</sup> See s 26(7) of the *Lake Simcoe Protection Act, 2008* – a similar training requirement appears in the *Clean Water Act, 2006*. Note that the inspection authority in the *Clean Water Act* is very similar to the *Lake Simcoe Protection Act* and the very recently passed *Great Lakes Protection Act, 2015* largely adopts by reference the inspection provision in the LSPA, as both statutes contain a regulation making authority governing activities in shoreline areas and adjacent to wetlands.

<sup>16</sup> I Ayres & J Braithwaite, *Responsive Regulation* (Oxford: University Press, 1992).



persuasion, at its base, through warning and civil penalties up to criminal penalties, license suspensions and then license revocations. Regulatory approaches would begin at the bottom of the pyramid and escalate in response to compliance failures. There would be a presumption that regulation should always start at the base of the pyramid.<sup>17</sup>



**Figure 1: Example of a Regulatory Pyramid**

Source: Update of I. Ayres and J. Braithwaite. 1992. *Responsive Regulation: Transcending the Deregulation Debate*, p. 35.

Three types of regulated actors are suggested by the theory: (a) the *virtuous firm* -those firms that genuinely desire to identify and self-correct violations without any agency intervention, (b) the *rational firm* – those firms that generally only comply if they believe there will be a financial consequence to non-compliance and therefore may require some form of agency response where a violation is detected in order to deter those firms from future non-compliance, (c) and finally the *incapacitated firm* – no matter what amount of financial penalty a regulatory agency may impose for non-compliance, the firm simply does not have the capacity to or simply refuses to comply – accordingly the agency must consider elevating its response to the top of the pyramid and withdrawing the firm’s license to engage in the regulated activity.

The goal of responsive regulation is to try to cultivate a regulatory environment where regulated firms are motivated to become and remain virtuous: where the firm’s front line staff and management assume the mentality that it is their duty to establish and maintain appropriate self-auditing functions such as environmental management systems to ensue compliance, rather than waiting for these violations to be discovered through an inspection. The goal then is to design policies that allow inspectors to calibrate their response to

<sup>17</sup> Robert Baldwin & Julia Black, *Really Responsive Regulation*, LSE Law Society and Economy Working Papers 15 (London, UK: London School of Economics & Political Science Law Dept, 2007). See also John Braithwaite, “The Essence of Responsive Regulation, Fasken Lecture” (2011) 44 UBC L Rev 475.

violations knowing when to escalate their response so that it sends the appropriate signal to the violator and to the other regulated firms in that sector. The foundation of the approach is dialogue with the regulated firm and to escalate the response only reluctantly when the tools at the base of the pyramid fail and once compliance has been achieved to de-escalate the agency response back to the base of the pyramid. As Braithwaite notes: “The pyramid is firm yet forgiving in its demands for compliance. Reform must be rewarded just as recalcitrant refusal to reform is ultimately punished.”

The regulatory pyramid approach to regulation only works effectively if the agency demonstrates that it is willing and able to escalate its enforcement response to the very top of the pyramid and to revoke a firm’s license to engage in a regulated activity – the ultimate penal consequence. If the regulated community begins to suspect that this threat of escalation is a hollow one and the agency would never exercise this power of last resort, the regulatory pyramid approach is undermined and there will be little motivation on the regulated community to comply.

The logic of regulatory pyramid relies on the peak of the pyramid to activate these compliance principals. The peak of the pyramid represents the ultimate constraint on pursuing a course of action that is in breach of the rules. Providing it is a credible sanction, that is, those being regulated believe that the regulator can and will use this power, it serves a number of functions. In a societal sense, it signals the seriousness of a breach of rules. It reminds those being regulated of their obligations and of course of action they should pursue, as agreed in the social compact at the base of the pyramid. Should social pressure fail, economic pressures come into play. It is costs to escalate to the top. It is rational for the regulatee not to carry the costs of non-compliance, and return to a cooperative stance at the base of the pyramid that respects the law sooner rather than later.<sup>18</sup>

Agencies in many jurisdictions have sought to integrate a version of the regulatory pyramid into their compliance and enforcement policies. For instance, many regulatory agencies in Australia have adopted a version of the enforcement pyramid and the effectiveness of those policies has been discussed at length.<sup>19</sup> One challenge, however, in adapting the regulatory pyramid approach for environmental protection regimes is that a broad range of activities subject to an environmental protection law may not require a license from the agency. Rather the law may simply impose operational requirements on the activity or the activity may only be subject to some form of a general pollution prohibition. Further, many regulators are moving toward reducing the range of activities that are subject to a licensing scheme, requiring instead that such activities simply register on a government registry and setting out operational rules that must be followed for regulated firms in that sector (often called a “permit by rule approach”).<sup>20</sup> Without the authority to suspend or revoke a license,

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<sup>18</sup> Applications of Responsive Regulatory Theory in Australia and Overseas: Update, cited in note 10 at 7.

<sup>19</sup> See Mary Ivec & Valerie Braithwaite, *Applications of Responsive Regulatory Theory in Australia and Overseas: Update*, RegNet (Regulatory Institutions Network) Research Papers Working Paper No 72 (2015).

<sup>20</sup> See for examples changes made to the *Environmental Protection Act* and the *Ontario Water Resources Act* that introduced the “modernization of approvals program” where activities that were subject to the requirement of a MOECC approval would now be exempt from such requirements and instead required to

and left essentially with the power to impose monetary penalties such as fines to respond to violations, such agencies may face unique challenges in adopting an effective regulatory pyramid approach. In other words, can the regulatory pyramid approach work effectively if the regime does not provide the regulator with a mechanism to suspend or permanently shut down a regulated firm's operations, something that is inherent in a licensing scheme?

One can easily question the assumptions underpinning the regulatory pyramid approach – for instance what levels of non-compliance will the approach condone before violators are penalized? Will this approach ultimately undermine the public perception that the agency is being a firm and effective regulator? Does the approach downplay the risks posed by a contravention? What about the charges that this approach may give rise to too much potential to an appearance of regulatory capture? For instance instruments made or issued under provincial environmental protection statutes, such as regulations or approvals, which impose pollution discharge standards, generally require a regulated actor to report to the Ministry any instances where those discharge standards are exceeded. This is also true of pollution incidents that breach the general pollution prohibition. This form of self-reporting is a cornerstone of environmental protection legislation. Indeed environmental protection legislation could not operate without such self-reporting obligations. The Supreme Court has held that imposing an obligation on a regulated actor to self-report a contravention as part of a larger regulatory scheme does not offend the Charter's guarantee in section 7 against self-incrimination.<sup>21</sup> One may think that where a regulated firm violates something as significant as a pollution discharge standard or a general pollution prohibition – shouldn't that generally be followed up with a swift enforcement response that involves some form or penalty both from a specific and general deterrence perspective? Wouldn't the public interest and the protection of the environment demand such a firm response?

However there is some evidence to suggest that an overly aggressive enforcement policy may be counter-productive and undermine a regulatory environment that motivates regulated actors to become and remain more "virtuous". In one study that analyzed data over a 10-year period from US industrial facilities subject to the *Clean Air Act*, it observed that an enforcement response that relied on penal threats often did not produce the desired outcome – that being that a regulated firm would carry through on promises to institute a self auditing function. Instead the authors postulate that in many instances the threat of a penalty created an adversarial relationship between the regulated actor and the agency, undermining past cooperative dealings and negatively affecting the morale of front line staff and management and their motivation to voluntarily identify and correct violations. The study found that the critical motivator for regulated actors to become or to remain virtuous was for the agency to ensure close surveillance – meaning a robust inspection regime. Close surveillance tells the regulated firm that its efforts at self-auditing are being closely watched and signals to other firms that investing in self-auditing functions is a

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register on the Environmental Activity and Sector Registry (EASR) – see in particular Part II.2 of the EPA. A description of the program can be found online: <<https://www.ontario.ca/page/environmental-approvals>>.

<sup>21</sup> *R v Fitzpatrick*, [1995] 4 SCR 154.

sound investment because their competitors are also being closely monitored. As the authors of the study, Short and Toffel, note:

[We] demonstrate that there are important distinctions between the effects of sanctions and surveillance on organizational behaviour that are not fully captured by either deterrence theory or the organizational literature on social control and cooperation. Although coercive regulatory threats appeared to have dampened intrinsic motivations to self-regulate, surveillance had the opposite effect. Disclosing facilities in heavily monitored industries were more likely than those in less monitored industries to follow through on their commitment to self-regulate. Furthermore even direct surveillance of individual facilities promoted effective implementation of self-regulation.<sup>22</sup>

Since its introduction, there have been many scholars who have expanded on the foundation of responsive regulation including Professor Malcolm Sparrow's *Regulatory Craft*.<sup>23</sup> Sparrow calls for a pragmatic approach to compliance and enforcement policy and suggest three core elements to reform: (1) *A clear focus on results*: The focus of an agency's compliance regime should be on defined outcomes and not merely on process outputs – meaning counting how many types of inspections or enforcement actions have been taken and whether there is an increase or decrease in those numbers from one year to the next; rather the focus should be on developing meaningful performance measures to determine if the chosen outcomes are being met; (2) *The adoption of a problem-solving approach*: The identification of important risks or patterns of non-compliance to help explain how an agency's scarce resources will best be allocated to achieve the desired outcomes. Sparrow emphasizes that there should be tailor-made solutions for each problem – and the need to retain the appropriate balance in enforcement policy – one that “enhances the agency's enforcement sting while using enforcement actions economically and within the context of coherent enforcement strategies.” (3) *An investment in collaborative partnerships*: Engaging in an open dialogue with all stakeholders to identify a shared purpose through collaborative agenda setting and prioritization – meaning the process of problem identification should be done by the agency in an open and transparent manner.<sup>24</sup>

It is beyond the scope of this paper to delve deeply into Sparrow's approach – as he is the first to acknowledge that his problem-solving approach to regulation is extremely difficult to implement. The next section will return to the two core questions that animate every agency's compliance and enforcement regime – with a focus on MOECC's program – namely how does MOECC decide who to inspect and when a provincial officer detects a violation during an inspection how does the provincial officer formulate his or her response. The section will conclude with some observations about MOECC's program

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<sup>22</sup> Jodi Short & Michael Toffel, “Making Self-Regulation More Than Merely Symbolic: The Critical Role of the Legal Environment”, Georgetown Public Law and Legal Theory Research Paper No 11-14 (2010) 44 Admin Sci Q 361-396 at 388.

<sup>23</sup> Malcolm K Sparrow, *The Regulatory Craft: Controlling Risks, Solving Problems and Managing Compliance* (Washington, DC: Brookings Institution Press, 2000).

<sup>24</sup> See discussion of the three core elements in particular Chapter 7 “Elements of Reform”.

based on the insights that responsive regulation and the regulatory pyramid have suggested makes for an effective regulator.

## **WHAT LESSONS MOECC'S COMPLIANCE PROGRAM CAN LEARN FROM RESPONSIVE REGULATION**

The Ministry of Environment and Climate Change (MOECC) regulates a wide range of sectors – from drinking water systems to waste disposal sites and waste management systems, industrial, commercial and municipal sewage works, pesticide applications and point source air discharges. Some of the more significant statutes that engage MOECC in compliance and enforcement activities include the following:

- *Environmental Protection Act*
- *Ontario Water Resources Act*
- *Pesticides Act*
- *Safe Drinking Water Act, 2002*
- *Toxics Reduction Act, 2009*
- *Nutrient Management Act, 2002* (MOECC has responsibility for the compliance and enforcement provisions of this Act)

In a typical year, the Ministry conducts between 3,000-4,000 proactive (or planned) inspections across a range of program areas that fall within its mandate and approximately 350 reactive inspections (in response to an incident). In the fiscal year 2014/15, a total of 4,033 inspections were completed. The Ministry's Operations Division (OD), the division that is responsible for compliance and enforcement within the Ministry, assigns each program area to an OD Region or branch. See the table below:

<b>OD REGION</b>	<b>REGULATORY PROGRAM</b>
Central	<ul style="list-style-type: none"> <li>• Hazardous Waste</li> <li>• Non-Hazardous Waste</li> <li>• Brownfields</li> <li>• Properties of Environmental Concern</li> </ul>
West Central	<ul style="list-style-type: none"> <li>• Air</li> </ul>
Southwest	<ul style="list-style-type: none"> <li>• Agriculture</li> <li>• Permits of Take Water</li> <li>• Surface and Groundwater</li> </ul>
Eastern	<ul style="list-style-type: none"> <li>• Pesticides</li> <li>• Water Wells</li> <li>• Aggregates</li> </ul>
Northern	<ul style="list-style-type: none"> <li>• Communal Sewage</li> <li>• Industrial Sewage</li> <li>• Mining</li> </ul>

Sector Compliance Branch	<ul style="list-style-type: none"> <li>• Vehicle Emissions</li> <li>• Renewable Energy</li> <li>• EASR and Toxics Audits</li> </ul>
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Using a risk-based approach, each year the program leads determine which regulated firms should be subject to planned inspections. Firms are ranked and selected based on an analysis of potential impacts to human health and the environment in addition to the firm’s compliance history. The source protection planning process that was introduced by the *Clean Water Act* provides a good example of how risk is incorporated into the planning process for proactive inspections. Source protection plans are required to identify the areas where a specific type of activity, such as the operation of a waste disposal site, is considered to be a significant risk to a municipal drinking water source. OD will use this information to give priority to those firms whose operations are located within significant threat areas. There is a delicate balance for program leads when planning proactive inspections for a given year, between identified local priorities and the program priorities being set centrally within Ministry.

The Ministry’s Compliance Policy<sup>25</sup> governs how the Ministry responds when it finds a violation, including during both a proactive or reactive inspection. My colleague Fred Maef’s paper, *Anatomy of a Compliance Regime: Initiation of Action* describes the elements of that policy. The focus of discussion here will be on the Informed Judgement Matrix (IJM) and the case specific considerations set out in Compliance Policy – because they direct how a provincial officer is required to formulate his or her response to an incident<sup>26</sup> and determining whether a “voluntary” or “mandatory” abatement approach is appropriate in the circumstances. “Voluntary abatement” means using the tools at the base of the regulatory pyramid including “persuasion” or a “warning letter” – in other words, allowing for a dialogue with the regulated actor before an incident is elevated to a “mandatory abatement” response. “Mandatory abatement” means using statutory enforcement powers to compel compliance and those tools include orders, a ticket issued under Part I of the *Provincial Offences Act*,<sup>27</sup> amending an approval for the site if one exists or referring the matter to the Investigations and Enforcement Branch for a possible laying of charges to commence a prosecution under Part III of the *Provincial Offences Act*. It also includes the issuance of an environmental penalty order (EP), which is a type of administrative penalty, but is only available to be used against facilities in one of the nine industrial sectors listed in the environmental penalty regulations and only in relation to

<sup>25</sup> *Compliance Policy: Applying Abatement and Enforcement Tools* (May 2007).

<sup>26</sup> “Incident” is defined in the Compliance Policy not only to be a contravention, but incidents not involving a contravention where an activity has the potential to result in an adverse impact. The reason for this is that the Ministry’s abatement powers are not only available when a contravention is found, but the Ministry is also given preventive measure order powers so that the Ministry does not have to wait for a breach of the general pollution prohibition to intervene – see for instance ss 18 and 157.1 of the EPA as an example of these powers.

<sup>27</sup> RSO 1990, c P.33.

contraventions specified in those regulations (largely contraventions related to unlawful discharges from those facilities to land or water).<sup>28</sup>

Informed Judgment Matrix (IJM)		Health/Environmental Consequences							
		1. Administrative	2. Minor Environmental	3. Minor Health	4. Medium Environmental	5. Major Environmental	6. Medium/Major Health		
Compliance History	A. No history / Good Compliance History	Compliance Category I		Compliance Category III					
	B. Previous Violation (unrelated)	Compliance Category II							
	C. Previous Violation (related)								
	D. Ongoing Violation Not Resolved Despite Ministry Directions								
	E. Previous Significant Convictions or Environmental Penalty Orders	Compliance Category III							
	F. Obstruction/ False Information**								

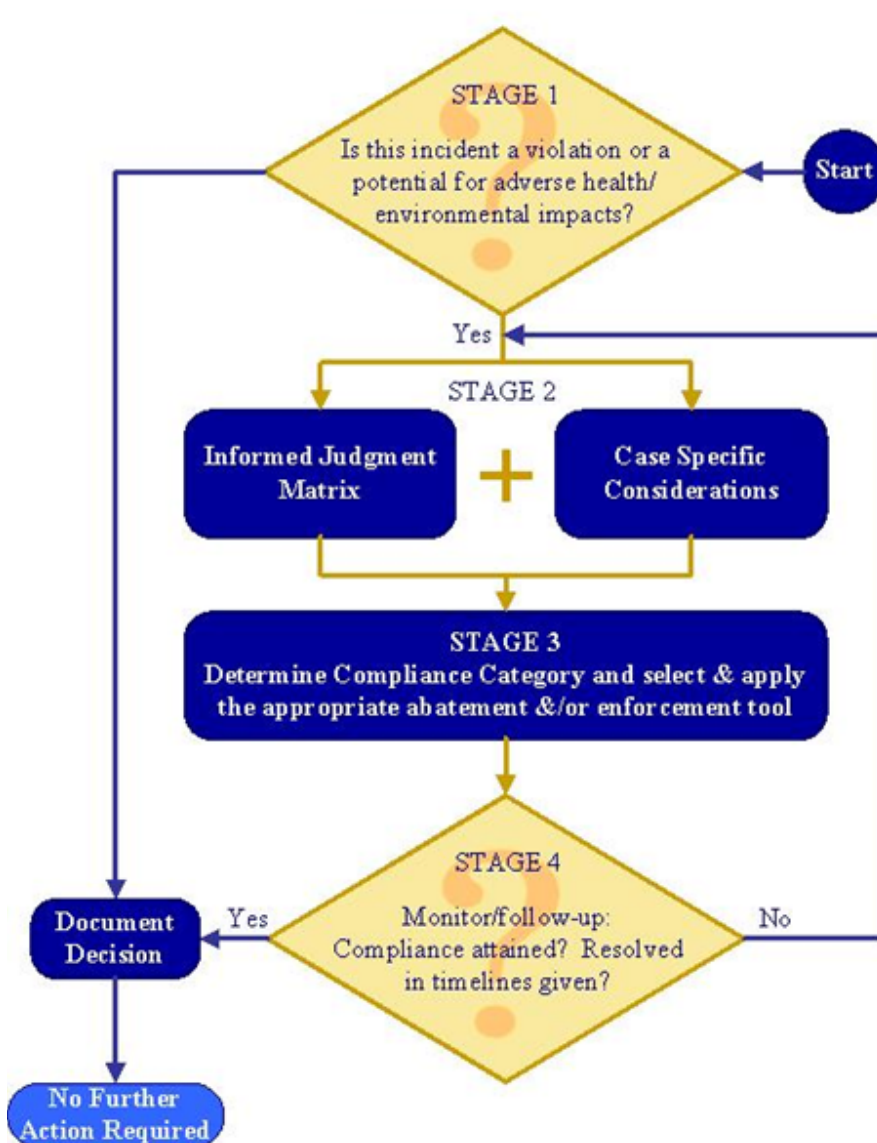
### Case Specific Considerations (Examples)

- Is there public concern about the incident?
- Is the regulatee someone with whom we can work to achieve a positive outcome?
- Did the regulatee disclose the incident voluntarily? Did the responsible person co-operate?
- How swiftly did the regulatee respond?
- Did their actions effectively resolve the incident and prevent its recurrence?
- Given the sophistication of the regulatee, would education and outreach be more effective to assist the person in understanding, managing and complying with ministry legislation?
- Was the incident the result of gross negligence and/or deliberate actions by a responsible person?

<sup>28</sup> See s 182.1 of the EPA and s 106.1 of the OWRA and the regulations made under those sections (O Reg 222/07 and O Reg 223.07).

Where a provincial officer detects an incident, the provincial officer is required to determine using the IJM whether the incident falls within Category I, II, or III. This is based on assessing (on the y axis of the IJM) the compliance history of the regulated actor and (on the x axis of the IJM) the environmental/health impacts of the incident. Case specific considerations can then be applied to determine whether the category of the incident should be escalated or de-escalated. Once an incident is classified into a category – the policy sets out the following responses for each category:

- *Category 1:* Voluntary compliance – including education and outreach, though mandatory abatement actions such as orders or referrals to IEB may be considered.
- *Category 2:* Stronger mandatory application of tools such as orders are recommended and an IEB referral should be considered.
- *Category 3:* Mandatory tools strongly recommended, and incident must be referred to IEB.





The diagram above sets out the decision tree a provincial officer is directed to follow when detecting an incident during an inspection. After the appropriate response is chosen (whether voluntary or mandatory abatement), the provincial officer is required to follow up to determine if the incident has been resolved. At all stages of the response the provincial officer is directed to document his or her decisions. Where a voluntary abatement approach is taken, and the regulated firm enters into a voluntary abatement plan to resolve the incident, the policy provides that unsatisfactory progress shall not be tolerated beyond six months (180 days). Where voluntary abatement efforts are not working to resolve an incident, the response must be escalated to a mandatory abatement response.

It is worth mentioning the compliance and enforcement scheme under the *Safe Drinking Water Act*, because unlike other MOEC statutes, a regulation<sup>29</sup> under that Act prescribes the minimum frequency of inspections for municipal drinking water systems and for labs and when a mandatory abatement response must be taken to deal with certain types of contraventions under that Act. The Act also establishes a Chief Drinking Water Inspector and requires the Chief to publish an annual report which describes the results of inspections of municipal drinking water systems and labs and the level of compliance found at those facilities. All of these features were incorporated into the SDWA to satisfy the recommendations of the Walkerton Inquiry Report<sup>30</sup> – in that Report, Mr. Justice O’Connor set out many detailed recommendations for a *Safe Drinking Water Act* including recommendations about compliance and enforcement under that Act and what matters should be prescribed by the law – matters that are, under other MOECC statutes, left entirely to the discretion of the MOECC.

Drawing on the responsive regulation literature canvassed in the second section, here are some observations concerning MOECC’s compliance and enforcement program:

1. *Establish clear outcomes for each program area to guide inspection planning and compliance and enforcement actions:* Through an annual integrated planning process, the program leads currently establish a set of goals for each program area, identify the priorities that will be the focus for the coming year and the results to be achieved. After these strategic directions are established, the program leads then work with each region to determine which regulated actors should be the target of proactive inspections. The development of the strategic direction guides the integrated planning process for a program area, such as setting goals and identifying priorities for a given period, would benefit in several ways if it was done in a more open and transparent manner involving the participation of regulated actors and other stakeholders. First, providing this opportunity for a dialogue would assist in obtaining buy-in from regulated actors to the Ministry’s priorities and will help leverage such partnerships. Further, engaging in the integrated planning exercise in a more open fashion would enable regulated actors across the sector

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<sup>29</sup> See O Reg 242/05 (Compliance and Enforcement).

<sup>30</sup> The Honourable Dennis R O’Connor, *A Strategy for Safety Drinking Water, Report of the Walkerton Inquiry, Part Two* (Toronto: Queen’s Printer for Ontario, 2002).

to understand where their self-auditing efforts should be focused and the Ministry rationale behind the two fundamental decisions of “who to inspect” and “how to respond.” Finally, conducting this planning exercise, in a more open and transparent manner will help build public confidence in the MOECC as an effective regulator.

*2. Regular reporting for each program area on compliance and enforcement outcomes:* Responsive regulation cautions against too much of a focus on tracking agency outputs as a performance measure – for instance tracking whether the number of prosecutions has increased or decreased from one year to the next. At a minimum each program area should report to the public at regular intervals on the number of proactive and reactive inspections conducted during the reporting period, the instances that voluntary versus mandatory abatement was used to resolve an incident, the number of incidents that were resolved successfully without the need for escalation and the type of abatement responses used (warnings, voluntary abatement plans, orders, prosecutions). The Ministry currently releases annual “environmental compliance reports” that describe incidents where air or water discharge standards are exceeded and what follow up action was taken to respond to the incident.<sup>31</sup> Going beyond the mere exercise of “bean counting” however, effective reporting would measure agency performance against a set of performance measures, and assess whether established outcomes are being achieved. Public reporting is also important, as it allows an agency to highlight the tools it employed in the program area during the reporting period to achieve outcomes including any targeted inspection programs, compliance assistance programs, programs designed to incent regulated firms in that sector to adopt self-auditing functions. Even more importantly, regular public reporting for each program area would allow the Ministry to demonstrate that it is capable of escalating enforcement responses up the regulatory pyramid when necessary, including highlighting cases where approvals have been suspended or revoked.

*3. Motivate regulated actors to adopt self-auditing functions:* In most types of MOECC approvals, such as approvals for waste disposal sites, the approval holder is required to prepare an annual report that includes a requirement to report any incidents of non-compliance and how the incident was resolved. Similarly, under the *Safe Drinking Water Act*, municipal drinking water system operators are required to prepare annual reports documenting any violations, the duration of the violation and what actions were taken to correct the violation.<sup>32</sup> Recently, a regulation under the EPA has required that a third party be retained to certify the accuracy of a compliance report.<sup>33</sup> Another regulation under the EPA which requires specific industrial facilities to prepare spill prevention and contingency plans requires an officer or director of the regulated firm to make a written statement as part of an annual report that the plans comply with the regulation. Are regulated firms that are compelled by law to document violations and how they are resolved

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<sup>31</sup> See “Environmental Compliance Report”, online: <<https://www.ontario.ca/data/environmental-compliance-reports>>.

<sup>32</sup> See Schedule 22 (Summary Reports for Municipalities) to O Reg 170/03 made under the SDWA.

<sup>33</sup> See O Reg 298/12 (Collection of Pharmaceuticals and Sharps – Responsibilities of Producers), s 9.

more inclined to adopt and maintain effective self-auditing functions? Do facilities that are compelled by law to monitor their own compliance have higher rates of compliance as a result of these legal obligations? Finally, to what extent is compliance reporting obligations audited by the regulator? These questions deserve examination because the trend has been to legally compel these self-auditing functions and it would be valuable to know to what extent these requirements result in higher compliance rates.

Beyond compelling self-audits by law, the Ministry has developed softer approaches to motivate the adoption of self-auditing functions. Under the Environmental Penalty program, a violator is given an automatic reduction to a penalty if the violator can demonstrate that, at the time of the contravention, it had an environmental management system in place that meets the requirements of the regulation. In July 2004 the Ministry adopted the *Environmental Leaders Program*<sup>34</sup> – a program that promised a regulated firm certain benefits such as assured turnaround times on approval decisions if the regulated firm agreed to certain conditions to join the program including having an environmental management system in place. Finally, as part of the integrated planning process, a program area may develop a compliance promotion project to encourage regulated firms to adopt self-auditing functions. How these compliance promotion projects are communicated to regulated firms can have significant bearing on their success.<sup>35</sup> Programs that recognize the importance of self-auditing functions and motivate regulated firms to adopt self-auditing functions are critical from the perspective of responsive regulation. Since the regulator cannot be at all places at all times to detect violations, the agency’s compliance and enforcement approach must send the appropriate signals that the virtuous firms in a sector will be recognized and rewarded.

*A call for greater use of administrative penalties to supplement MOECC’s regulatory pyramid:* Administrative penalties are simply the authority of an agency to impose a monetary penalty on a violator without having to use a court process such as a prosecution or a civil action. Administrative penalties have a long tradition in a broad range of regulatory contexts (including environmental protection) in the United States and in other jurisdictions, but they have not been adopted widely in Canada until quite recently with the exception of specific regulatory contexts such as taxation and aeronautics. This means the only way the MOECC can impose a monetary penalty for a violation is by commencing a prosecution. There are many downsides to an over reliance on prosecutions. First, investigations and prosecutions are very resource intensive. Consequently, prosecutions are not suitable for penalizing violations of a minor nature. Second, the monetary penal

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<sup>34</sup> Ministry of the Environment, Environmental Innovations Branch, *A Framework for Ontario’s Environmental Program* (July 2004).

<sup>35</sup> Agencies have found that the very manner in which an agency seeks to communicate to a regulated firm to induce the firm to identify and correct violations can have a significant impact on whether the firm will follow through – the area is sometimes called “Communications for Compliance” – see for example, Scott Killingsworth, “Modeling the Message: Communicating Compliance Through Organizational Values and Culture” (2012) 25 *Geo J Leg Ethics* 960-987.

consequence resulting from a prosecution is imposed long after the contravention has been detected, sometimes up to two years following the detection. Indeed, for the Ministry, often the only mandatory abatement response available to deal with violations that aren't suitable for prosecution is by issuing a provincial officer contravention-based order<sup>36</sup> – which often is simply an order requiring the regulated firm to comply with a legal requirement the firm was supposed to comply with in the first place. In other words, an order power without a concomitant administrative penalty power greatly hampers the leverage of the agency in compliance negotiations with a regulated firm.

Take for example a routine proactive inspection of a regulated firm that uncovers a long list of violations. Most of those violations may be classified as minor or administrative in nature such as failures to report, document or monitor – violations which from an agency resource perspective are not appropriate to be pursued through prosecution. When the inspection report is given to the regulated firm with the list of violations, beyond a referral to IEB, the only other mandatory abatement tool that a provincial officer has to compel compliance is a contravention-based order. With a properly tailored administrative penalty scheme, the monetary consequences of non-compliance for the regulated firm would be far more manifest and urgent. Unlike fines which are set by courts on the facts based on the particular case, administrative penalties are set in a far more predictable and transparent manner. They also can be tailored to reward certain behaviour, such as providing reductions for firms that have environmental management systems in place, or provide for significant reductions or even cancelled penalties if violations are corrected within a specified time. Moreover, unlike prosecutions, most administrative penalty schemes are based on absolute liability – the steps a violator took to prevent a violation are considered in determining the penalty amount and not as a defence. Reliance wholly on strict liability offences to monetarily penalize violators may motivate regulated firms not to be as forthcoming to investigators about what steps they took to prevent a violation on the grounds that this may unduly prejudice their due diligence defence in any potential prosecution.

After introducing enabling legislation in 1998 for administrative penalties, in 2002 the Ministry consulted on draft administrative penalty regulations for a very broad range of contraventions, but not for serious matters such as unlawful spills.<sup>37</sup> However the government of the day never pursued the proposal after encountering intense pressure from the regulated community which opposed giving the Ministry the authority to penalize violators and felt that the proposal would create an adversarial relationship between MOECC's abatement staff and regulated firms – a relationship they felt that had always been a cooperative one. In 2005 however in response to a series of spills to the St. Clair River from industrial facilities in the Sarnia area, the government passed legislation to

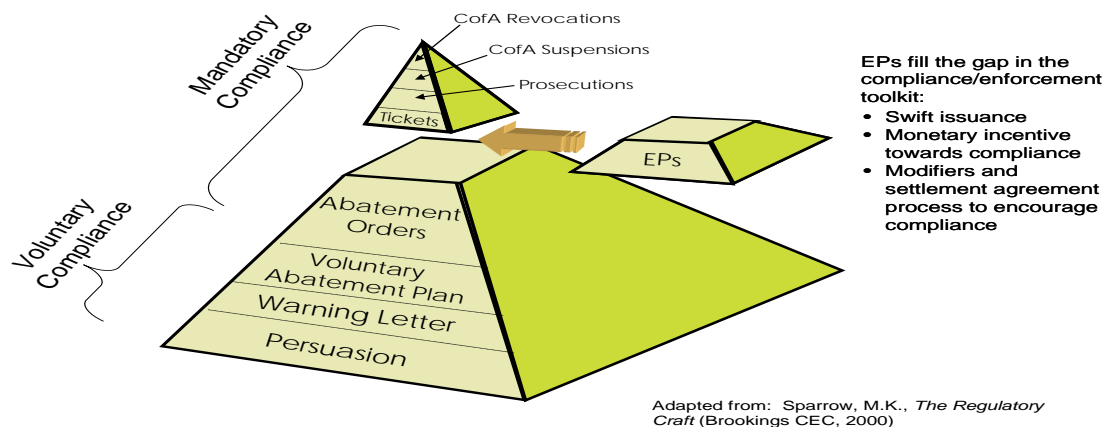
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<sup>36</sup> See as an example of a provincial officer contravention-based order, s 157 of the EPA.

<sup>37</sup> The draft regulations were proposed under the *Environmental Protection Act*, the *Ontario Water Resources Act* and the *Pesticides Act*. The posting can still be viewed on the Registry under the Environmental Bill of Rights, online: <<https://www.ebr.gov.on.ca/ERS-WEB-External/displaynoticecontent.do?noticeId=MTMxNzQ=&statusId=MTMxNzQ=&language=en>>.

replace the 1998 administrative penalty provisions with a new type of administrative penalties called “environmental penalties” (EPs). Unlike the older provisions that were designed to deal with violations of a minor nature, these new administrative penalties were designed specifically to deal with contraventions of a serious nature such as unlawful spills. For example, the new provisions allow a person to be prosecuted for a contravention even in cases where an administrative penalty was imposed and paid. Further, the maximum penalty amount for EPs was increased ten-fold. However environmental penalties are only available for specific types of industrial facilities and only in relation to contraventions that relate to unlawful discharges to land and water. MOECC needs a broad-based administrative penalty tool to respond to violations – one that will allow it to reserve prosecutions for the most serious types of violations. The diagram below was used by the Ministry when environmental penalties were introduced to explain the gap in the regulatory pyramid EPs were designed to fill. That gap continues to exist in the many program areas where EPs are not available.

How Environmental Penalties (EPs) Fill the Gap in the ministry's Compliance Toolkit



Mastering the art of being an effective regulator is an exceedingly difficult balancing act. The simple decision of determining what regulated firms to inspect and how to respond to a violation is fraught with difficult choices about how to best expend scarce agency resources. An agency often has to navigate between competing and sometimes contradictory pressures, balancing the need to be responsive to local concerns while dealing effectively with priorities being set by its leadership. The foremost message from responsive regulation is simple – pragmatism – the need to identify problems and figure out solutions by methodically setting goals and developing performance measures to achieve results. It means a commitment and an investment in gathering and analyzing data on an agency’s decisions and actions to figure out in a systemic way what works and what doesn’t. And it also means planning and reporting on compliance and enforcement activities in as much an open and transparent manner as possible in order to command confidence from the individual regulated firm, from the other firms in that sector and from the public at large.