



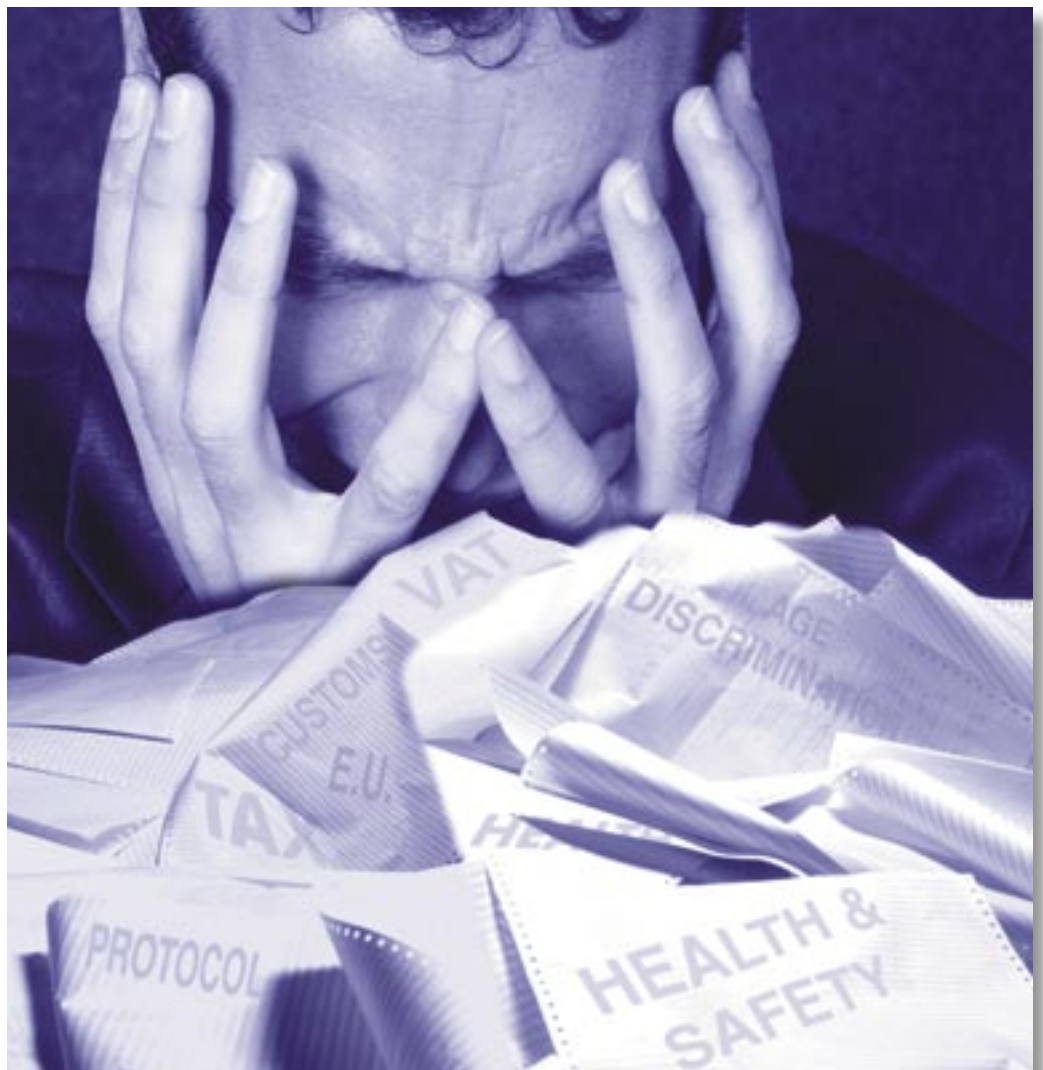
# Regulatory Impact Assessment

Professor David Parker, Research Professor in Privatisation & Regulation

The cost of regulation is spiralling. Manufacturing, financial services and even small businesses are struggling to keep pace with the time consuming and financially burdensome cost of new legislation and regulation required by both national government and international bodies such as the European Union. David Parker urges business to get fully involved in the consultation process to ensure such regulations are both necessary and reflective of economic and social needs.

**E**stimating the full economic costs of regulation - which would include both the administrative costs of managing regulations by Government and the (usually much larger) costs to business of complying with the regulations - is not easy. But undoubtedly the compliance costs are huge and often hidden. In 2005 the British Chambers of Commerce quantified the total cost of regulation on business since 1998 at £39 bn. Sir Digby Jones, the former Director General of the CBI, reported that 95% of business leaders felt that the time they spent dealing with regulation had increased over the past five years and a survey of offshoring work in 2004 by CBI/MORI concluded that regulation in the UK was playing an important part in companies' decisions to relocate abroad.

Whatever the correct figure for the regulatory burden, it is incontrovertible that regulation is extensive and seemingly growing bigger by the day. Volkswagen Group Chairman, Bernd Pischetsreider has described EU legislation affecting the motor industry as "not creeping, but explosive".



## The importance of regulatory impact assessment

Regulatory Impact Assessment (RIA), or what is sometimes referred to as Regulatory Impact Analysis, has been described by the Organisation for Economic Co-operation and

Development (OECD) as:

"an information-based analytical approach to assess probable costs, consequences, and side effects of planned policy instruments (laws, regulations etc). It can also be used to evaluate the real costs and consequences

## The OECD RIA Checklist

1. Is the problem correctly defined?
2. Is Government action justified?
3. Is regulation the best form of Government action?
4. Is there a legal basis for regulation?
5. What is the appropriate level (or levels) of Government for this action?
6. Do the benefits of regulation justify the costs?
7. Is the distribution of effects across society transparent?
8. Is the regulation clear, consistent, comprehensible, and accessible to users?
9. Have all interested parties had the opportunity to present their views?
10. How will compliance be achieved?

of policy instruments after they have been implemented.”

At the core of RIA is an assessment of the benefits and costs expected to result from a state regulation. A new regulation should be introduced only when it has net benefits. However, arguably RIA’s main contribution to better governance lies in improving the process by which the risks attached to a regulation are assessed and in promoting proper consultation with affected interests before a regulation is introduced.

A properly instituted system of RIA within Government has the potential to raise the quality of regulation and hence reduce the regulatory costs on business and society in general.

### Where did RIA come from?

RIA first surfaced as a process within Government in the USA in the 1970s. But it achieved wider popularity after the OECD began to champion the idea and

published, in March 1995, guidance on RIAs. The use of RIAs when proposing new regulations has been mandatory in UK central Government since 1998 and RIA guidelines were introduced for UK government departments in 2000. By 2001, 20 out of the then 28 OECD member states claimed to be using RIA in some form. In addition, international donor agencies such as the World Bank and the Asian Development Bank have undertaken recent initiatives to spread the use of RIA more widely to developing countries. The European Commission introduced a new Impact Assessment system in 2003.

Today, all government departments in the UK are expected to complete an RIA setting out the risks, costs and benefits of any new regulatory measure that has an impact on businesses, charities and voluntary bodies. RIAs are required for all new regulations except for:

- proposals that impose no costs or no

savings, or negligible costs or savings on the public, private or charities and voluntary sector

- increases in statutory fees by a predetermined formula such as the rate of inflation
- road closure orders.

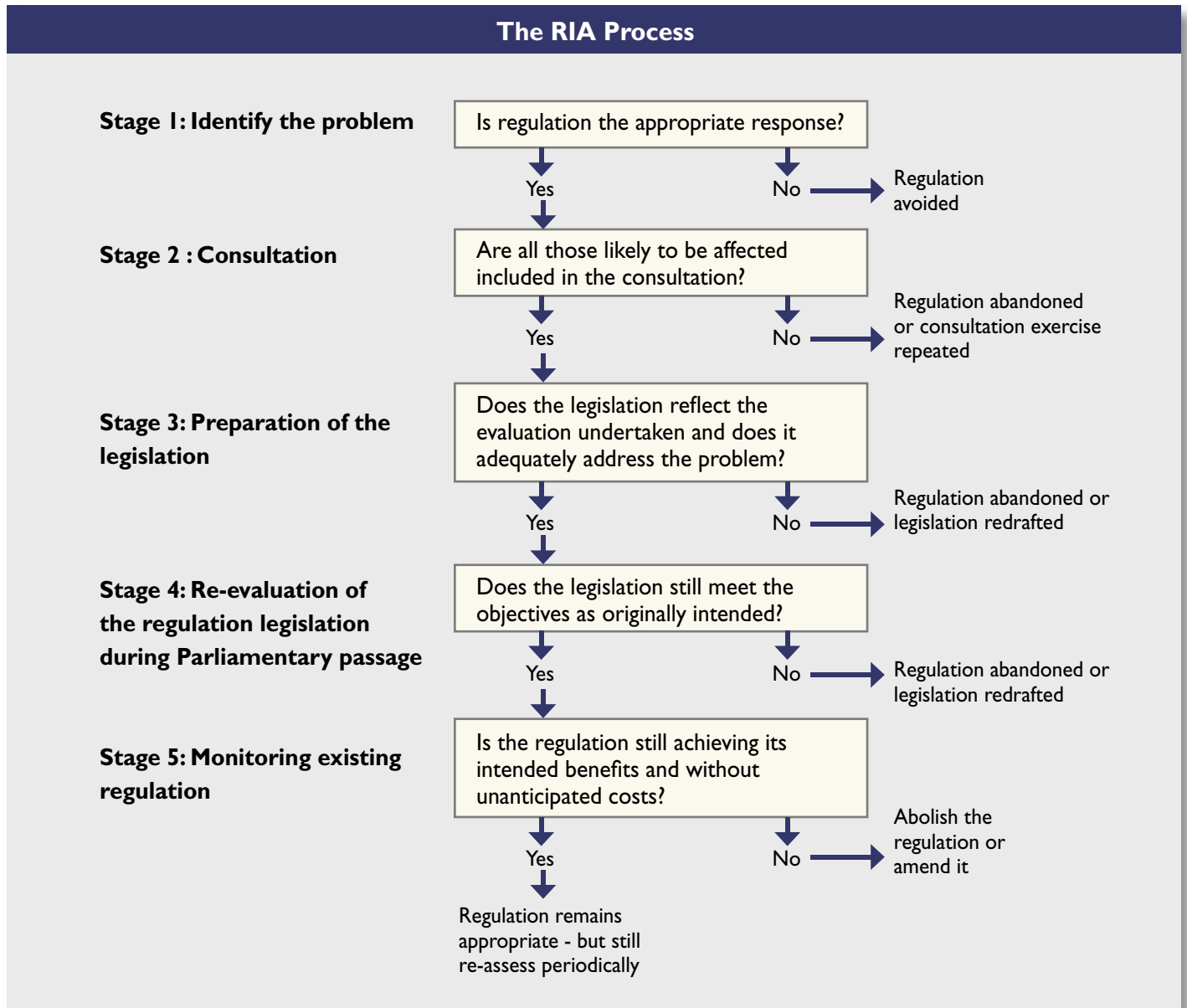
Also, all RIAs since 2002 must consider the implications for competition of a regulatory proposal. Where an initial test indicates that there may be an impact, departments should discuss the competition assessment with the Office of Fair Trading. Departments are also expected to pay particular attention to the regulatory impacts on small business. More recently, updated guidance to departments has increased the emphasis on investigating the wider impacts of regulation; in particular the new guidance has highlighted consideration of the impact on different racial groups, rural communities, sustainable development and the public sector.

### RIA policy in UK

RIA has been championed within Government in the UK by the Better Regulation Task Force (BRTF) and the Regulatory Impact Unit in the Cabinet Office. The BRTF was replaced on 1 January 2006 by the Better Regulation Commission (BRC). This now provides independent advice to government about new regulatory proposals and reviews the Government’s overall regulatory performance.

In the Budget in 2005 the Chancellor of the Exchequer, Gordon Brown, announced reforms to the regulatory process and the BRC is responsible for monitoring the reforms, including vetting departmental plans for administrative burden reduction.

Alongside the BRC operates the Better Regulation Executive (BRE) within the Cabinet Office, which was established



in May 2005. This is tasked with promoting the Government's better regulation agenda. The BRE has overall responsibility for the Government's commitments to:

- regulate only when necessary
- set exacting targets for reducing the cost of administering regulations
- rationalising the inspection and enforcement arrangements for both business and the public sector.

The BRE is expected to implement the recommendations of two major independent reports published on Budget Day in March 2005, namely the BRTF report Regulation 'Less is More:

reducing burdens, improving outcomes' and Philip Hampton's report, 'Reducing Administrative Burdens: effective inspection and enforcement'.

The BRE will also take forward the work previously carried out by the Regulatory Impact Unit including:

- scrutinising new policy proposals from Departments and Regulators
- speeding up the legislative process to make it easier for departments to take through deregulatory measures
- working with Departments and Regulators to reduce existing regulatory burdens affecting business and frontline staff in the public sector

- driving forward the better regulation agenda in Europe.

In the UK the BRE publishes guidelines and checklists for Government departments to use when undertaking RIAs that draw on and build upon the earlier OECD guidance. Recently a Standard Cost Model has been introduced to encourage the simplification and consolidation of existing regulations.

### Scope for improvement

RIA has taken off internationally and compliance in UK central government is now officially 100%. However, studies of

the operation of RIA (some undertaken in the Centre for Competition and Regulation Research at Cranfield) point to a number of areas for improvement. Firstly, to date, RIA has been mainly applied to new regulations (known as ex ante RIAs) but not to existing ones (ex post assessments), although the introduction of the Standard Cost Model could represent a step change in the Government's attempts to reduce the administrative burden of existing regulation. Arguably, big benefits would come from assessing the actual impact of existing regulations in terms of the original intentions, perhaps including the original RIAs - did they get it right? Most of the regulatory burden derives from existing laws.

Secondly, RIA is concerned with both the outcome and process dimensions of government regulatory policy. A good RIA attempts to assess all of the regulatory effects both quantitative and qualitative - RIA should not be limited simply to quantitatively measurable impacts because this may lead to the omission of important costs and benefits. However, a number of RIAs undertaken in the UK still fail to evaluate the impacts and opportunity costs in a meaningful way.

Thirdly, risk assessment is a central part of any serious RIA because costs and benefits are often unclear. However, to date there has been insufficient attention paid to the generation and analysis of alternative options (including alternatives to regulation where appropriate). Also worrying is the tendency for departments to report single point estimates when quantifying costs and benefits with no accompanying sensitivity analysis. A range of outcomes alongside probabilities would often be far more informative - and realistic.

Fourthly, there is much evidence that the use and quality of RIAs varies across

government departments reflecting differing levels of enthusiasm about the process. A series of studies by the National Audit Office has found major deficiencies in the way RIAs are implemented. Its latest report argues that RIAs are often not used in the right way, the purpose of RIAs is not always understood by policy-makers and there is a lack of clarity in the presentation of the analysis and persistent weaknesses in the assessments.

Finally, and tellingly, few RIAs have recommended the "do nothing" (don't regulate) option. The fear must be that civil servants are too reluctant to confront their ministers by pointing out that their pet regulatory project makes no sense whatsoever. In many cases RIAs do not offer a robust challenge to proposals to regulate.

### Why should business care?

Business moans about the regulatory burden but fails to engage with government to shape the regulatory agenda. RIA requires government departments to consult with affected interests before new regulations are introduced. But too frequently departments receive very few responses from business.

Business should not complain about the regulatory burden when it fails to take the opportunity to shape the regulatory agenda. RIA provides the opportunity for business to input into the regulatory process and thereby ensure that regulation is restricted to where it is really needed and produces net economic, social and environmental

benefits.

RIA has the potential to improve Government and reduce the mounting regulatory burden on society. It has much room to do good - not least because state regulation has expanded and continues to expand, at a pace and on a scale that must be of concern to all of us. Regulation must be restricted to where there is clear "market failure" and its benefits can be demonstrated clearly to outweigh its costs. However, to ensure this, business must do its part by engaging meaningfully with the consultation process, which is such a critical component of a RIA.

This in turn requires that managers should understand and become knowledgeable about RIA so as to learn how best to influence the process. The need to address the burdens imposed by the regulatory state is too great to allow the opportunity offered by RIA to pass us by.

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