Australian Government
Productivity Commission

Identifying and Evaluating Regulation Reforms

Productivity Commission Discussion Draft

September 2011

This discussion draft has been prepared for further public consultation and input.

The Commission will finalise its report after these processes have taken place.

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The Productivity Commission

The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians. Its role, expressed most simply, is to help governments make better policies, in the long term interest of the Australian community.

The Commission's independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.

Further information on the Productivity Commission can be obtained from the Commission's website (www.pc.gov.au) or by contacting Media and Publications on (03) 9653 2244 or email: maps@pc.gov.au

Opportunity for further comment

You are invited to examine this draft and provide written comments to the Productivity Commission.

Written comments should reach the Commission by 21 October 2011. If possible, please provide your comments by email. The final report will be prepared after comments have been received and discussions with interested parties have been held.

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Terms of reference

Identifying and Evaluating Regulation Reforms

I, Bill Shorten, pursuant to Parts 2 and 4 of the *Productivity Commission Act 1998* hereby request the Productivity Commission to undertake a research study on frameworks and approaches to identify areas of regulation reform and methods for evaluating reform outcomes.

Ongoing regulatory reform to improve the quality of regulation needs to be supported by frameworks and approaches to identify appropriate areas of reform and the priority of such reform. Equally important is the ability to effectively evaluate reform outcomes, in particular to provide an indication of how reform can reduce administrative and compliance costs for business. The Productivity Commission is asked to conduct a review to propose frameworks and approaches that will be effective in identifying poorly performing areas of regulation and regulatory reform priorities, and methods for evaluating reform outcomes.

This review is to replace the fifth year of the cycle of annual reviews of regulatory burdens on business, which was to have been a review of economy-wide generic regulation.

Background

In 2007, as part of the Government's response to the Report of the Taskforce on Reducing Regulatory Burdens on Business, the Productivity Commission was asked to conduct ongoing annual reviews of the burdens on business arising from the stock of government regulation. Four reviews have been conducted to date. At the direction of the Council of Australian Governments (under a separate review process) the Commission also undertakes reviews to benchmark compliance costs of regulations in targeted areas, such as food safety and occupational health and safety.

Scope of the annual review

In undertaking the review, the Commission should:

1. examine lessons gathered in Australia and overseas in reviewing regulation, identifying regulatory reform opportunities and priorities, and evaluating regulation reform outcomes.

2. build on such lessons to analyse possible frameworks and approaches for identifying poorly performing areas of regulation and regulatory reform

priorities, and both qualitative and quantitative methods for evaluating regulation reform outcomes

3. In proposing enhanced frameworks and approaches to identify poorly performing areas of regulation and regulatory reform priorities, and methods for evaluating reform outcomes, the Commission is to:
   - seek public submissions and consult with interested parties as necessary
   - have regard to any other relevant current or recent reviews commissioned by Australian governments' and
   - have regard to the assessment of the OECD in its 2009 Review of Regulatory Reform in Australia — Towards a Seamless National Economy that there is likely to be limited scope for gains to regulatory quality through a further tightening of existing processes

The Commission's report will be published within six months of receipt of the terms of reference and the Government's response will be announced as soon as possible.

Bill Shorten
Assistant Treasurer

[received 24 May 2011]

Contents

The following additional appendixes form an integral part of this Discussion Draft and are available on the study website (www.pc.gov.au/projects/study/regulation-reforms)

Preface

While regulations have been growing apace, governments have also been making significant efforts to improve regulatory processes and to reform costly or ineffective regulations. In this study, the Productivity Commission was asked to examine any lessons from past reviews, and to consider methods for evaluating reforms, in the context of identifying priority areas for the future.

In this Discussion Draft, the Commission has sought to distil some preliminary findings from the more detailed examination of 'approaches and frameworks' contained in appendixes. These are available from the Commission's website (www.pc.gov.au).

In the time available and given the range of experience to be covered, both in Australia and overseas, this draft should be regarded as a work in progress. It is being released now to elicit feedback that will help the Commission refine its findings and proposals in a final report that is due in late November.

Abbreviations

BCA	Business Council of Australia
COAG	Council of Australian Governments
GDP	Gross domestic product
IC	Industry Commission
NCP	National Competition Policy
OBPR	Office for Best Practice Regulation
OECD	Organisation for Economic Cooperation and Development
ORIC	Office of the Registrar of Indigenous Corporations
PC	Productivity Commission
PIR	post implementation review
RIA	Regulation impact assessment
RIS	Regulation impact statement
SNE	Seamless National Economy
VCEC	Victorian Competition and Efficiency Commission

OVERVIEW

Key points

- Even if all regulations were rigorously vetted at the outset, it would still be important to ensure that the stock of regulation remains appropriate and cost-effective over time.
- There is a range of approaches to reviewing existing regulation and identifying necessary reforms. Some are 'routine'; some involve programming, and some are more ad hoc in nature.
  - Each has strengths and weakness. But their effectiveness can be improved in various ways, drawing on past experience.
  - Good governance and effective consultation have generally been key success factors.
- Evaluation methods to assess regulations and reform outcomes vary in technical complexity and in the impacts they address.
  - While qualitative as well as quantitative methods can be used, they need to be attuned to the review task.
- An effective regulatory system will require a combination of review approaches and tools. These need to be used in complementary, timely and proportionate ways, such that the overall returns from the resources available can be maximised.
  - Prioritisation of reviews and of reform efforts is crucial.
- Australia's regulatory system has evolved over time, with the necessary institutions and processes now broadly in place.
  - However there would appear to be scope for further improvement in a number of areas, including the identification of review needs and the sequencing of reform efforts.

Overview

Regulation has grown at an unprecedented pace in Australia over recent decades. As in other advanced countries, this has been a response to the new needs and demands of an increasingly affluent society and an increasingly complex (global) economy. This regulatory accretion has brought economic, social and environmental benefits. But it has also brought substantial costs. Some costs have been the unavoidable by-product of pursuing legitimate policy objectives. But a significant proportion has not. And in some cases the costs have exceeded the benefits. Moreover, regulations have not always been very effective in addressing the problems for which they were designed.

Growing recognition of these costs and other deficiencies of regulation has led governments to undertake major reforms over the years. An early focus of such efforts was the removal of regulation that unduly impeded competition. This exposed firms to heightened market disciplines and caused them to give more attention to impediments to their competitiveness, including the effect of other regulations. Further waves of reform followed, being focussed on the regulation of key input markets and regulatory compliance burdens generally.

The Commission and its predecessor organisations, through their public inquiry programs, have contributed to these various reform efforts. A recent strand of this work has involved annual 'stocktakes' of regulation in key sectors to identify unnecessary burdens on business. These followed on from the economy-wide review by the 'Regulation Taskforce' in 2006. With the completion of the sectoral stocktakes early this year, the Australian Government asked the Commission to provide it with an assessment of these and other approaches to identifying priority reforms — and methods for evaluating their effects — together with advice on enhancing the 'frameworks' for reform efforts.

Why target the 'stock'?

The requested focus for this report relates to the existing stock of existing regulation rather than the flow of new regulation. The magnitude of the stock is many multiples that of the flow, and it has commensurately larger impacts within the economy. Ultimately, however, the stock of regulation is the outcome of the

accumulated flows. In many cases, deficiencies of regulation can be traced to the inadequate vetting of it in the first place.

Processes to improve the scrutiny of new regulatory proposals — notably through impact assessment requirements — have accordingly been introduced or upgraded by all governments in Australia over recent years (box 1). How well these are working in practice, and the scope to make further improvements, remains unclear at this stage. (The Commission will undertake a comparative study for the Council of Australian Governments (COAG) next year.)

However, even if all new regulations were subjected to rigorous assessment, uncertainties about their effects would remain in many cases. And even if a regulation were initially appropriate and cost effective, it may no longer be so some years hence. Changes can occur in markets and technologies, or in peoples' preferences and attitudes. Moreover, the accumulation of regulations leads to interactions among them that in themselves can give rise to increased costs and other unintended consequences.

Box 1 **Managing the flow of regulation**

The Australian Government established a system of regulation impact statements (RIS) in 1985 for all new Commonwealth regulation that imposes a significant burden on business. The guidelines and arrangements have been revised periodically, most recently in 2010.

All state and territory governments have also implemented RIS-type systems, now entrenched in COAG under the National Partnership Agreement to Deliver a Seamless National Economy.

A RIS is mandatory for all decisions made by the Australian Government and its agencies that are likely to have a significant impact on business or the not-for-profit sector. This requirement includes amendments to existing regulation and the rolling over of sunsetting regulation.

The RIS process is overseen by the Office of Best Practice Regulation (OBPR) in the Department of Finance and Deregulation. OBPR vets and comments on compliance with the Government's RIS requirements and on the adequacy of the RIS in its coordination comments.

The Cabinet Secretariat provides a gate-keeping role to ensure that regulatory proposals coming to the Cabinet and sub-committees of the Cabinet meet the RIS requirements. Any regulatory proposal that has not complied, cannot proceed unless the Prime Minister has deemed that exceptional circumstances apply, necessitating a 'post implementation review' within 2 years.

It is therefore very important that the stock of regulation be kept under review to verify that it remains 'fit for purpose', with any costly or otherwise poorly performing regulations being removed or amended.

The costs of regulation are multi-dimensional and have multiple origins (box 2). This means that an effective policy framework for regulatory reform must embody a suite of approaches that can address and remedy these different forms of cost or burden. However such reviews are themselves not costless. They require skilled people and other resources, all of which have competing uses. They therefore need to be allocated so as to address the priorities, in a proportionate and coordinated way.

Assessing the 'approaches'

A variety of approaches to identifying and implementing reforms to existing regulation have been used in Australia and overseas. They can be loosely divided into three broad categories: approaches that involve relatively routine or ongoing 'management' of the stock; those that are 'programmed' to occur at certain intervals or in particular circumstances; and those of a more ad hoc character, which may be triggered by various influences or emerging issues.

Stock management approaches

Regulator strategies

Regulators should be well placed to detect costs and problems in the regulations they administer and to advise policy department about these. Equally, participants in this review have emphasised that the manner in which regulations are applied and enforced can be a bigger driver of costs for businesses than the regulations themselves.

The 'Regulation Taskforce' report of 2006 argued that regulators needed to be more systematic in consulting and seeking feedback from regulated entities, and that any undue risk aversion of regulators needed to be addressed by government. A number of initiatives have been implemented since then, including more risk-based enforcement and other more light-handed and proportionate approaches. And more regulators have established consultative forums and processes. However, experience appears variable, with some doing better than others.

- *It would be desirable to conduct a comparative evaluation of regulators' consultation strategies and the arrangements put in place to encourage lower cost approaches to oversight and enforcement.*

Box 2 Sources of 'unnecessary' regulatory burdens

The Regulation Taskforce (2006) identified five features of regulations that contribute to compliance burdens on business not justified by the intent of the regulation.

- *Excessive coverage, including 'regulatory creep'* — Regulations that appear to influence more activity than originally intended or warranted, or where the reach of regulation impacting on business, including smaller businesses, has become more extensive over time.
- *Regulation that is redundant* — Some regulations could have become ineffective or unnecessary as circumstances have changed over time..
- *Excessive reporting or recording requirements* — Companies face multiple demands from different arms of government for similar information, as well as information demands that are excessive or unnecessary. These are rarely coordinated and often duplicative.
- *Variation in definitions and reporting requirements* — Regulatory variation of this nature can generate confusion and extra work for businesses than would otherwise be the case.
- *Inconsistent and overlapping regulatory requirements* — Regulatory requirements that are inconsistently applied, or overlap with other requirements, either within governments, or across jurisdictions. These sources of burden particularly affect businesses that operate on a national basis.

There may also be economic costs arising from 'distortions' — the effects of regulation on competition and on incentives for investment and innovation. Such distortions (often unintended), can be due to:

- substitution effects resulting from changes in relative prices, including distorting investment decisions which have long term consequences
- overly prescriptive regulation which prevents innovative or lower cost approaches to meeting the intended outcomes of the regulation
- interactions of regulations that can compound costs, create inconsistencies, and otherwise pose dilemmas for business compliance.

In addition, there may be other non-economic costs arising from adverse environmental and social impacts. Finally, if regulation is not effective, there may be 'opportunity costs' in terms of the foregone benefits that regulation intended to deliver.

Stock-flow linkage rules

A second type of management strategy constrains the flow of new regulation through rules and procedures linking it to the existing stock. The most commonly advocated approaches are 'one-in one-out' rules and 'regulatory budgets', though the Commission found few instances of these having been implemented. They have the apparent attractions of simplicity and rigour in 'holding the line'. But they raise significant measurement issues and can create perverse incentives within government agencies that could worsen regulatory performance.

- *There would be more disadvantages than advantages in introducing 'one-in one-out' rules or 'regulatory budgeting'. If there were nevertheless a wish to adopt such approaches, they should at least need to be conducted initially as trials or pilot schemes on a small scale.*

A weaker variant, with less downside risk, is the requirement under some existing RIS processes (including at the Commonwealth level) for agencies to document why existing regulation is not adequate to address a perceived problem and whether a new regulatory proposal provides scope to reduce it.

- *Such provisions have a potentially useful role to play, but it is not clear to what extent they have been utilised or enforced.*

Red tape reduction targets

Related to these approaches, an increasing number of governments overseas and in Australia (box 3) have implemented 'red tape reduction targets' — following the lead of the Netherlands in the early 2000s. These involve requirements on departments and agencies to reduce designated compliance costs (typically 'paperwork') by a certain percentage or value over a specified period of time. In most cases, targets are reported to have been met, with estimates of red tape reductions ranging up to several billion dollars in some cases (United Kingdom, Netherlands).

Percentage reduction target schemes requiring baseline estimates of costs have been expensive to conduct, although some less costly alternatives have been developed. Schemes have also varied in the uniformity of targets across agencies. However, scope remains for 'gaming' and it is not clear that declared reductions in burdens on business have actually been realised to the extent reported. Surveys indicate that many businesses have not perceived much improvement.

An alternative approach, adopted in British Colombia (Canada) is based on reducing the number of 'must comply' requirements. It appears to have had more impact, but is yet to be properly evaluated.

- *Red tape targets appear to have yielded reductions in regulatory burdens in the jurisdictions concerned, but the extent is unclear. They face measurement issues and other pitfalls. The approach appears most suited to situations where there has been little previous effort to reduce undue compliance costs.*

Box 3 Red tape reduction targets in Australia

Several Australian states have used red tape reduction targets to reduce regulatory burdens on business.

Victoria — The Victorian Government has set a target of a $500 million reduction in compliance costs to business by July 2012. The costs covered include administrative costs, substantive compliance costs, and delay costs. As at July 2010, Victoria had estimated a reduction in the compliance burden of $401 million.

In order to help meet the target, Victoria used incentive payments — including a $42 million tender fund. A model based on the Dutch standard cost model was used to estimate the regulatory savings of the reforms.

South Australia — In 2006, South Australia set a target of a $150 million reduction in net administrative and compliance burdens to business by 2008. Agencies were requested to develop plans outlining potential reforms, and a series of reviews were undertaken. The Office of Best Practice Regulation's (OBPR) business cost calculator was used to estimate the burden reductions associated with the reforms.

An independent audit by Deloitte (South Australian Government 2008) suggested that the reduction target was exceeded. Following this, the South Australian Government announced another $150 million reduction target by 2012.

New South Wales — New South Wales has a target of a $500 million reduction in red tape (including both administrative and substantive compliance costs). As at June 2010, an estimated $400 million of reductions had been achieved.

Queensland — The Queensland government set a target of a $150 million reduction in the administrative and compliance burden to business between 2009 and 2013. Departments have submitted simplification plans, which outline a range of potential reforms.

Programmed review mechanisms

Sunsetting

Some reviews occur at pre-determined times or intervals. 'Sunsetting' is the most comprehensive of these and the most widely utilised. (This approach could also be categorised as 'routine stock management' in many cases.) It essentially requires a regulation to be re-made after a certain period (typically 5 to 10 years) if it is not to lapse. This can apply to specific regulations or, as in a number of Australian jurisdictions, to all regulations that are not specifically exempted.

The logic supporting sunsetting is that much regulation inevitably has a 'use-by date', when it is no longer needed or will require significant modification. But without a trigger to reassess its utility, at least some of it will inevitably remain in place. Sunsetting has an important role to play in improving the regulatory stock — provided firstly, that exemptions and deferrals can be contained and, secondly, that any regulations being re-made are appropriately assessed first.

The first wave of sunsetted regulation under the Commonwealth's Legislative Instruments Act commences in 2013. This draws on the accumulated stock of regulations at the time of the Act, plus regulations made since then that are 10 years old. The number of regulations concerned is large (14000 instruments falling due over a seven year period, with most due in the first three years) yet, despite warnings from a 2008 review, it appears that little real preparation has been made by most agencies.

- *In order for the Commonwealth's new sunsetting reforms to be effectively implemented, departments and agencies would need to progressively screen and review regulations for which they are responsible well in advance of the deadlines (and communicate their intentions publicly).*
- *Sunsetting should be used proactively as an opportunity to re-assess groups of related regulation, and to consider any changes to improve enabling or primary legislation. Where regulations being remade have significant impacts on business, they should be subject to the same RIS requirements as new regulation.*

Five yearly 'default reviews'

The Australian Government, following a recommendation of the Regulation Taskforce (2006), introduced a further requirement that all regulation not subject to sunsetting or other evaluation be reviewed every five years. It seems likely that, in practice, very few regulations would now fall into this category.

- *Provided the Commonwealth's sunsetting regime is effectively implemented, the five yearly default review requirements are unlikely to yield sufficient benefits to warrant incurring their administration costs.*
- *The five year default rule could more usefully be confined to any regulation having a significant impact on business that was initially required to have a RIS.*

'Process failure' post-implementation reviews

The Government's 'best practice requirements' for making regulation provide for exemptions by the Prime Minister in 'exceptional circumstances', as long as such regulation undergoes a 'post-implementation review' (PIR) within 1-2 years. This is a fail-safe mechanism to ensure that regulations made in haste or without sufficient assessment — and therefore having greater potential for adverse effects or unintended consequences — can be re-assessed before they have been in place too long. Consistent with that rationale, the post-implementation reviews need to assess the costs and benefits of such regulations in the light of actual experience, and be able to propose significant amendments where needed to achieve better outcomes.

It had been anticipated that there would be few 'exceptions'. However, the numbers have been rising and include important areas of regulation with significant potential impacts (box 4). The Commission understands that, contrary to the original conception, some departments are anticipating that PIRs would only address relatively limited implementation matters. If this mechanism were to be used as a means of evading the RIS process, it would pose a considerable risk to the integrity of the Government's best practice requirements.

- *Post implementation reviews for regulations exempted from the Government's RIS processes need to be able to assess the costs and benefits of those regulations and recommend any necessary modifications.*
- *In the case of regulations with pervasive economic impacts, there is a case for reviews being conducted at arms length from the responsible policy department.*

Box 4 **Some regulations requiring 'post implementation reviews'**

The OBPR has advised that exemptions from the Government's RIS requirements, triggering a need for post-implement reviews, have been granted for some 40 regulatory initiatives across a range of areas. These include:

- changes to the arrangements for executive termination payments (2009)
- carbon pollution reduction scheme legislation (2009)
- industrial relations legislation (including the *Workplace Relations Amendment (Transition to Forward with Fairness) Act 2008* and the *Fair Work Act 2009*) (2010)
- pharmacy location rules (2010)
- live cattle exports to Indonesia (2011)
- certain responses to the Australia's Future Tax System Review, including the minerals resource rent tax and the targeting of not-for-profit tax concessions (2011).

'Embedded' statutory reviews

In some cases, reviews are specified in legislation. This approach is particularly beneficial where there are significant uncertainties about the likely impacts. It may also help reassure community groups where regulatory changes are controversial.

Embedded reviews have the advantage of being framed at the outset by those who are best placed to understand the regulation and its potential strengths and weaknesses. The legislation ideally should specify the governance arrangements for the review (including the degree of independence) and the key aspects to be evaluated (without unduly narrowing the review's scope), as well as make provision for the generation of necessary data where feasible.

- *Embedded statutory reviews have a number of attractions and could be more widely used, particularly in circumstances where there are significant uncertainties about outcomes.*

'Ad hoc' and special purpose reviews

Some of the most significant reforms to regulation over the past few decades have resulted from ad hoc initiatives in response to emerging problems or concerns. Some of these have focussed on a specific area of regulation, while others have been much broader in scope.

'Stocktakes' of burdens on business

One large-scale approach is the public 'stocktakes' of regulatory burdens on business. In the Commonwealth jurisdiction, the Small Business Deregulation Taskforce (1996) and Regulation Taskforce (2006) were economy-wide in coverage. Reviews by the Commission over the past few years have looked at particular sectors. Similar exercises have taken place within a number of states.

Stocktakes have been mainly limited to reducing compliance costs and have generally taken the policy itself as a given. For this purpose, their approach of seeking suggestions (or receiving complaints) from businesses — then 'filtering' and testing these with responsible agencies — has proven cost-effective. Moreover, stocktakes have also been a useful means of identifying areas of regulation with wider costs and problems necessitating deeper evaluation, and have subsequently led to some targetted reviews and valuable reforms.

However, to be successful, such broadly-based reviews need visible political support, expert taskforces and effective consultation strategies. They should not be conducted too frequently and preferably only after the recommendations of previous stocktakes are seen to have been addressed.

- *Public 'stocktakes' of regulatory burdens are a cost-effective mechanism for identifying reform needs, provided they have good governance and occur at appropriate intervals (for example, every 8-10 years).*

'Principles-based' review strategies

Another broadly-based approach to reviewing the regulatory stock focuses on key features of regulation that can give rise to undue costs. The largest exercise of this type in Australia was the Legislative Review Program under the National Competition Policy (NCP), which targeted regulations impeding competition across all jurisdictions (box 5). A further current example is COAG's 'Seamless National Economy' reform stream, which has addressed state-based regulations that lack desirable national 'coherence'.

In such approaches, following initial identification of candidates for reform, there need to be follow-up assessments to verify that there would be net benefits from specific reform actions. (In the case of the NCP, the onus of demonstrating net benefit was formally placed on those advocating retention of regulation.) Approaches of this kind are accordingly more demanding and resource-intensive than general stocktakes. But if the principle is robust and reviews are well conducted, they have the potential to identify a large number of reforms yielding substantial gains.

Box 5 **National Competition Policy and the Legislative Review Program**

In April 1995, the Australian Government and state and territory governments committed to the implementation of a wide-ranging NCP — which included a legislative review program (LRP) for all jurisdictions to review their regulation in regard to the impact it had on competition.

Australia's NCP initiative stemmed from a recognition that aspects of Australia's wider competition policy framework were impeding performance across the economy and constraining the scope to create national markets for infrastructure and other services.

Overall, the NCP LRP resulted in the identification of around 1800 laws regulating areas of economic activity for review under the NCP. In aggregate, governments reviewed and, where appropriate, reformed around 85 per cent of their nominated legislation. For priority legislation, the rate of compliance was around 78 per cent (NCC 2010).

A Productivity Commission review in 2005 found that the LRP had played an important role in winding back barriers to competition and efficiency across a wide range of economic activities. It also found that most of the NCP reforms were in place and that overall NCP had yielded substantial benefits to the Australian community. The success of Australia's NCP reforms saw them hailed internationally as a successful example of nationally coordinated reform.

NCP was completed in 2005. It was succeeded by Australia's National Reform Agenda, which included a stream of work on achieving a Seamless National Economy (SNE). The competition principle remains an important part of Australian regulatory policy, and is applied as part of the assessment of new regulation in all Australian jurisdictions.

Key considerations in this respect are the arrangements for screening regulation according to the agreed 'principle' and for prioritising or sequencing reforms. Although broadly successful overall, both of the above exercises experienced difficulties in these respects. Attempting to do too much at once can dilute available review resources, reduce scope for effective stakeholders' participation, and ultimately compromise the potential for beneficial reforms.

- *Principles-based reviews can yield substantial reform dividends if well conducted, and properly targeted and sequenced.*
- *As applies to stocktake reviews, it is important that reform processes in train are completed and implemented satisfactorily before embarking on new reforms.*
- *It was envisaged that legislative reviews conducted around the country under the NCP's competition principle would be repeated after 10 years. A cost-effective way of discharging this requirement would be to confine reviews to those anti-competitive regulations that were retained in the last round.*

Benchmarking

With different jurisdictions following different approaches to common regulatory objectives, benchmarking can potentially provide useful information on comparative performance, leading practices and models for reform. The World Bank's *Doing Business* reports contain data that enable international comparisons to be made annually across a range of regulatory areas. In contrast, the benchmarking studies for COAG by the Commission have looked at the performance of regulations in specific areas across jurisdictions within Australia (box 6).

Benchmarking nationally (including New Zealand in the case of food regulation) has been more detailed than the World Bank exercise. It has also seemingly been more instructive about relative performance and leading practices, given the similar institutional settings that apply nationally. These exercises have faced difficulties in devising and obtaining the data for quantitative indicators. However, they have shown that qualitative comparisons can be just as revealing.

Governance arrangements for these studies include an advisory panel of officials from all governments, which has proven effective in guiding the development of the approach, testing methodologies and obtaining data from jurisdictions. Benchmarking results have been found useful by governments and appear to have added reform momentum in the areas covered thus far.

The resource demands, however, have been significant (akin to a public inquiry), so it is crucial that areas for benchmarking are carefully selected. Timing is also important if the results are to be influential in supporting reform.

- *COAG's regulatory benchmarking program is proving an effective exercise in promoting reform nationally and within individual jurisdictions.*
- *Benchmarking is most useful where it:*
  - *encompasses the administration and enforcement of regulation, as well as differences in regulation itself*
  - *can compare the outcomes as well as the costs of regulation.*

Prioritisation and timing are important to maximise the benefits. The key requirements for inclusion in a regulation area are significant impacts and common policy objectives, together with some variation in approach and performance.

Box 6 COAG's Regulatory Benchmarking Program

The Commission's 'feasibility' study

To help implement COAG's 2006 agreement on benchmarking and measuring regulatory burdens, the Commission was asked to examine the feasibility of developing quantitative and qualitative performance indicators and reporting framework options. This feasibility study concluded that benchmarking was technically feasible and could yield significant benefits (PC 2007a).

The 'quantity and quality of regulation' & 'cost of business registrations' reports

In December 2008, the Commission released two benchmarking reports. The 'quantity and quality' report (PC 2008a) provides indicators of the stock and flow of regulation and regulatory activities. It included a number of quality indicators for a range of regulatory processes, across all levels of government. The 'cost of business registrations' report (PC 2008b) provided estimates of administrative and substantive compliance costs for business in obtaining a range of registrations required by the Australian, state, territory and selected local governments. The study tested three methods for benchmarking — regulatory surveys, 'synthetic' or representative business estimates and business focus groups. The aim was to triangulate the estimate of compliance costs. Much was learned in the exercise, including the difficulty of estimating compliance costs in a consistent way across jurisdictions, even for relatively simple regulation.

The 'food safety regulation' & 'occupational health and safety' reports

The 'food safety' report (PC 2009b) compared the food regulatory systems across Australia and New Zealand. The Commission found considerable differences in regulatory approaches, interpretation and enforcement between jurisdictions, particularly in those areas (such as standards implementation and primary production requirements) not covered by the model food legislation.

The 'occupational health and safety' (OHS) report (PC 2010a) compared the occupational health and safety regulatory systems of the Commonwealth and state and territory governments. The report found a number of differences in regulation (such as record keeping and risk management, worker consultation, participation and representation and for workplace hazards such as psychosocial hazards and asbestos) and in the enforcement approach adopted by regulators.

Planning, zoning and development assessments

The Commission examined and reported on the operations of the states and territories' planning and zoning systems, particularly as they impact on business compliance costs, competition and the overall efficiency and effectiveness of the functioning of cities (PC 2011d).

'In-depth' reviews

When it comes to major areas of regulation with wide-ranging effects, for which significant reforms may be required, there is generally no substitute for in-depth reviews. Such reviews need to be able to adequately assess the appropriateness, effectiveness and efficiency of regulation — and to do so within a wider policy context, in which other forms of intervention may also be in the mix.

Most of Australia's important regulatory reforms have emerged from such reviews (box 7). Those that have worked best in helping to achieve beneficial and enduring reforms have generally been characterised by independent leadership and skilled support teams, with adequate time to complete their task. Extensive consultation has been a crucial part of this, including through public submissions and, importantly, the release of a draft report for public scrutiny.

Box 7 **Examples of 'in-depth' reviews**

In-depth reviews have been conducted in Australia by a range of taskforces, panels, government departments and agencies. In considering regulations or issues with a strong regulatory dimension, these have generally (though to varying degrees) shared a common approach involving: consultation; research and the search for evidence in assessing the impact of current regulations; and identification of alternatives.

Some examples of in-depth reviews conducted by taskforces include the current Victorian Taxi Industry Inquiry; the 2011 transparency review of the Therapeutic Goods Administration; the 2008-10 Australia's Future Tax System (Henry) Review; the 2009-10 (Cooper) Review of Australia's Superannuation System; the 1998 (West) and the 2008 (Bradley) reviews of higher education; the 2009 National Health and Hospitals Reform Commission; and the 2008-09 (Hawke) Review of the *Environment Protection and Biodiversity Conservation Act 1999*. Other examples of past reviews using aspects of this approach include the 2004 (Hogan) Aged Care Review; and the Wallis (1996-97) and Campbell (1979) inquiries into the Australian financial system.

Regulatory reviews and inquiries undertaken by the Productivity Commission and the Victorian Competition and Efficiency Commission also use an in-depth approach. These reviews have tended to involve long time frames and extensive opportunities for public comment, including through draft reports. They have been able to explore and assess alternatives to regulation and they consider costs and benefits from a community-wide perspective.

Parliamentary Committee inquiries into current or prospective regulations also share some (if not all) of the characteristics of in-depth reviews. These inquiries tend to share a strong focus on public consultation via submissions and hearings. However, Committee reviews tend to be more lightly resourced than those conducted by standing bodies, panels and taskforces.

When done well, such reviews have not only identified beneficial regulatory changes, but have also built community support for them and thereby facilitated their implementation by government.

In-depth reviews can consume significant resources and therefore need to be directed at areas where the potential gains from reform are likely to be high. This means that while there will always be unanticipated circumstances that demand such reviews — including to avoid reflexive regulatory responses to emerging 'issues' — forward planning and prioritisation have important roles to play.

- *In-depth reviews have a central role in regulatory reform. They need to be well targeted to be cost-effective. The hallmarks of successful reviews are independent governance and the release of draft reports for public scrutiny.*

Evaluation methods

The Commission was asked to examine, and provide advice about, methods for evaluating *reform outcomes*. It is not only important in its own right to verify that reforms have 'delivered', but also to be able to demonstrate this to the community — thereby helping to achieve support for further reform. Evaluations can also pick up unintended consequences that require regulatory adjustments.

Explicit ex post evaluations of regulatory reforms in Australia have been relatively few in number (and rare internationally). There have been some 'embedded' reviews of specific reform initiatives (like the regulatory regime for third party access to essential infrastructure). There have also been broader reviews, such as to assess the net gains from the NCP reforms and, currently, the Commission's review of the impacts of the 'Seamless National Economy' reforms.

The methods that are potentially relevant to evaluating *reforms* are essentially the same methods that can be used to evaluate regulations generally, or indeed to evaluate regulatory *proposals*. Most of the review approaches just discussed could make use of such methods. In practice, there appears to have been more reliance on qualitative than quantitative techniques. Data permitting, the latter can bring additional rigour and give better insights about relative impacts.

The individual methods vary greatly in technical complexity and in the nature and extent of the impacts encompassed by the analysis (box 8). Different methods are accordingly suited to different evaluation tasks. For example, the 'business cost calculator' has been designed to estimate various regulatory compliance costs at the firm level, whereas general equilibrium modelling can project the magnitudes of

these and other costs (and benefits) across industries and for the economy as a whole.

Evaluation methods also vary greatly in their resource and skill requirements. Their allocation to review tasks, whether ex post or ex ante, is therefore a matter of 'horses for courses'.

- *Evaluations of regulations and reforms generally need to draw on both qualitative and quantitative methods. The selection of these should be determined by their 'fitness for purpose', relating to the nature of the task and access to data.*
- *Quantitative methods are desirable where practicable and could be more widely used. Partial quantification can often be better than none.*

Box 8 Some quantitative evaluation methods

Compliance cost 'calculators'

The Standard Cost Model (developed by the Netherlands Government) seeks to estimate the reduction in administrative compliance costs. These costs include paperwork costs, and the cost of time involved in completing the paperwork. More sophisticated versions of the cost accounting approach (such as the Commonwealth's Business Cost Calculator) broaden the scope to include substantive costs such as investment in training and equipment required for compliance, and the costs of delay.

Econometric analysis

Econometrics is a set of statistical tools that can be used to determine whether there is a mathematical relationship between two (or more) variables, what effect the variables have on each other, and the robustness of the relationship. Econometrics provides a way to test whether relationships set out in economic theory hold in practice, by applying real world data to theoretical models. In the context of evaluating regulations and reforms, econometrics can be used to determine whether regulations and reforms affect individual variables of interest.

Economic modelling

Partial equilibrium models describe the relationships between the variables that change directly in response to the reform and the target variables. Economic partial equilibrium models might look at a specific industry to estimate the effect on investment and/or innovation that result from reforms. The models may then be used to estimate the effect of these changes on industry inputs, output and profitability over time.

General equilibrium (GE) models capture the main relationships between inputs and outputs in the economy, and are used to estimate the flow-on effects to other sectors in the economy from changes at an industry level or to the availability and quality of the resources (labour, capital and land). Partial equilibrium models are generally used to estimate the 'shocks' that are fed into a GE model.

Strengthening the 'framework'

It emerges that several approaches to reviewing and evaluating regulations have made — and should continue to make — a useful contribution to identifying areas for reform and thus to enhancing the regulatory stock. However no approach can be relied on to 'do it all'. Each has its own 'niche', either in relation to the type of reforms targeted or the point in the regulatory cycle at which the approach comes into play. Such approaches are most effective, therefore, when they complement each other such that there are no 'gaps' in coverage (and, equally, no doubling up), with all regulations reviewed in the most timely and appropriate way.

Given the limited resources available for such activities — particularly skilled analysts — it is also important that these resources are allocated such that the overall 'returns' from the various approaches can be maximised. This depends in turn on the effectiveness of the wider system or 'framework' in which the individual approaches are designed and managed.

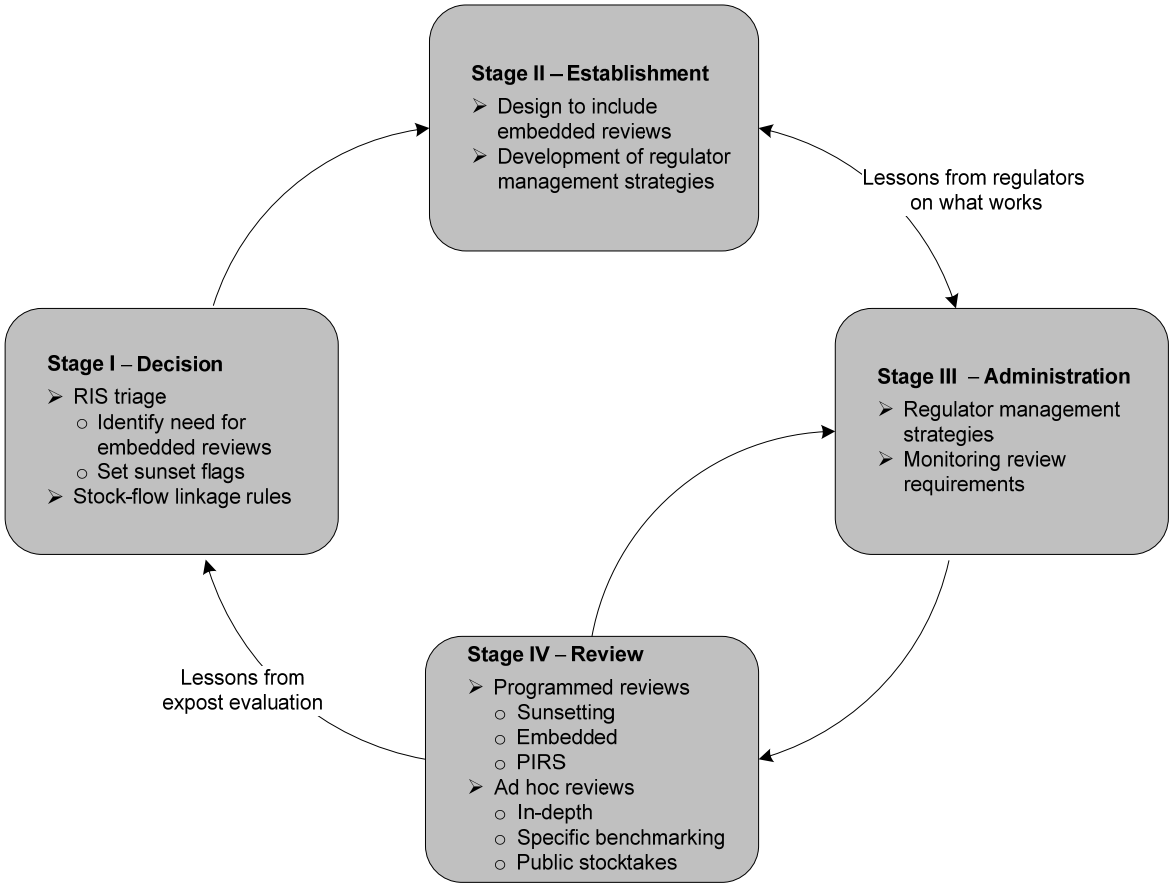
The Organisation for Economic Cooperation and Development (OECD) has emphasised the importance of regulatory governance to regulatory performance. It stresses the need for 'joined up' systems, comprising appropriate institutions, processes and 'tools' across the whole regulatory cycle.

The 'regulatory cycle' can be segmented into four stages or phases, from initial decision-making, to implementation, administration and finally review (figure 1). How well each of these is managed has an important bearing on the overall performance of the existing body of regulation.

A number of changes have been made to Australia's regulatory system over time, with the aim of strengthening its capacities at each stage of the cycle, as well as enabling better coordination. Among the more important of these at the Commonwealth level are:

- assignment of responsibility for good regulatory practice to a Cabinet-level Minister (the Minister for Finance and Deregulation)
- the strengthening of procedures and analytical requirements for making regulation, and the upgrading of the OBPR to provide advice to agencies as well as to vet and report on compliance
- the institution of automatic review mechanisms for subordinate regulation (notably though sunsetting)
- the initiation of a range of in-depth reviews in key areas of regulation.

Figure 1 **Review approaches through the regulatory cycle**



Within COAG, the establishment of the 'Business Regulation and Competition Working Group' has for the first time provided an ongoing national forum for the consideration of regulation reforms encompassing all jurisdictions — including to improve processes (for example, regulatory assessment) and to improve particular areas of regulation (for example the 27 'seamless national economy' items).

The OECD, in its recent review of regulation in Australia, endorsed these arrangements, a number of which had responded to earlier recommendations of the Regulation Taskforce. The various elements required for a good regulatory system can now be said to be largely in place. However, in considering from the perspective of this latest study how effectively the framework is operating in practice, there would appear to be scope for improvement in a number of areas:

- *More systematic ex ante identification of reviews?* Although provided for under existing RIS requirements, there could be a more systematic appraisal of review needs when regulations are being made. Clarifying that all regulations subject to RIS requirements must be reviewed within five years would help. The scope and broad governance of reviews could usefully be specified in advance (particularly

for embedded statutory reviews). This would be best overseen by the OBPR, which would also need to monitor implementation.

- *More attention to prioritisation and sequencing?* Prioritisation is important for a number of the above approaches, to ensure adequate resourcing and that related regulations are considered in a complementary way. This will be particularly important for the looming mass of sunsetting regulations. Past review programs, such as in the NCP and Seamless National Economy streams, have suffered from overload. While the 'selection criteria' adopted by these exercise have been appropriate in the broad (box 9) there appears to have been insufficient consideration given to the sequencing of reviews, or to the number and combination of reforms attempted at any one time. A clear understanding of the resources and timeframes needed to advance priority reviews and reforms is essential. There would also be benefits in seeking feedback on proposed reform programs from relevant stakeholders outside government.
- *Greater monitoring of reviews and reforms?* Although there have been various requirements to conduct reviews, it can be hard to determine what has actually been reviewed and what the outcomes were. For example, keeping track of actions in response to the Regulation Taskforce's 178 recommendations has been challenging even for the Commission. Lack of transparency can breed cynicism in the community about whether real progress has occurred, and a sense that contributing to such reviews is wasted effort. It is important to monitor reviews and their outcomes, and for this information to be made publicly available.
- *Better communications and consultation?* Communication and consultation are two of the OECD's 'four C's' for an effective regulatory system (together with coordination and cooperation). In addition to providing information about the outcomes of reviews, giving advance notice to business and the community of forthcoming reviews is very important. Regulatory plans intended to achieve this could be improved in many cases. 'Whole-of-government' principles for consultation have been developed, but arguably could also be better utilised. In particular, any review of a significant area of regulation should make provision for public feedback on its preliminary findings and recommendations, with further consultation at the more detailed implementation stage.

Box 9 Selecting candidates for COAG's 'Seamless National Economy' reform agenda

The Business Regulation and Competition Working Group (BRCWG) was tasked with identifying the first tranche of regulatory reform initiatives for the COAG regulatory reform agenda and the Seamless National Economy.

The BRCWG considered the potential benefits to growth, productivity and workforce mobility from over 35 possible reform areas. These were drawn from a number of sources. They included issues with multi-jurisdictional implications that were suitable for reform, but had nonetheless proved resistant to reform in the past and were evaluated according to the following considerations:

- How *wide* is the reach of the regulation?
- How *deep* is the reach of the regulation? Does it have a significant effect on industries generating a large amount of GDP?
- How *large* are the costs to business and taxpayers of complying with the regulation?
- How *damaging* is the regulation to incentives for effort, risk-taking, entrepreneurship and innovation?
- How *large* are the impediments created by the regulation to workforce mobility and participation?

Each area was then categorised according to the desired level of regulatory change: mutual recognition, harmonisation or a national system.

- *More balanced incentives for regulators?* How regulations are administered is an important determinant of the overall regulatory burden. Excessive costs can arise from overly stringent requirements or prescriptive supervision. These can emanate from attempts to minimise rather than optimise risk, or simply from lack of attention to compliance costs relative to the principal objectives of a regulation. These behaviours are partly 'cultural' and can really only be remedied by governments modifying some of the incentives facing regulators. Regulation Taskforce proposals for the Australian Government to pursue this though clearer guidance in legislation and 'Statements of Expectation and Intent', together with the development of cost-related key performance indicators and requirements for better consultation and appeal mechanisms, were all accepted. But the extent of their implementation and how well they are operating is unclear and could usefully be reviewed.
- *More resourcing?* The reviews necessary to identify and implement regulatory reforms require people who are at least as skilled as those responsible for developing the regulations in the first place. The limited availability of the right people (and their opportunity costs) are important reasons for prioritising and sequencing their efforts. However, given the relatively large gains to be had

from well-targeted reforms, there may be a case for devoting additional resources to the reform task, and to regulatory reviews in particular. This applies both to the institutions overseeing and vetting new regulation, and to those monitoring and evaluating existing regulations. The specification of review needs when regulation is being developed should also make provision for their resourcing where this is likely to be necessary to ensure adequate evaluation.

1 What this study is about

Following four rounds of the Annual Review of Regulatory Burdens on Business, which covered all sectors of the economy, the Commission has been asked by the Australian Government to provide its assessment of 'frameworks and approaches' for identifying areas for further regulation reform and methods for evaluating reform outcomes. The terms of reference note the need to prioritise future regulatory reform efforts of governments. It is also important to evaluate reform outcomes effectively, including the impacts on administrative and compliance costs faced by business.

In brief the Commission has been asked to:

- examine the lessons from past reviews of regulation, both in Australia and overseas
- build on these lessons to suggest frameworks and approaches for identifying poorly performing areas of regulation and regulatory reform priorities, and methods for evaluating regulation reform outcomes (see the terms of reference for details).

1.1 The scope of this study

This study outlines frameworks, approaches, and methods for identifying priorities for regulation reform and for evaluating their impacts. It is not proposing areas of regulation for reform, although the application of the approaches would have implications for priority areas. Indeed, one of the lessons is that the review efforts to date provide information to inform priorities for the future.

The study focuses on approaches for 'managing' the *stock* of regulation in order to reduce the regulatory burdens imposed on business and achieve better outcomes for the community more widely. However, many of the strategies need to be considered at the time a regulation is introduced. So while the study does not examine the regulatory impact assessment system in place, it does consider actions at this point in the regulation cycle that can enhance the management of the regulation once it has been implemented. The Council of Australian Governments (COAG) has agreed to undertake a benchmarking study of the regulation impact statement (RIS) processes in place across all Australian jurisdictions in 2012.

This study also considers strategies applicable to reforming all forms of regulation (box 1.1) that affect businesses. (Some of these strategies are also applicable to regulation that do not have business impacts.) It draws on examples of approaches that have been taken to managing the stock of regulation, in the Australian jurisdictions and other relevant countries, to identify useful ways in which the Australian Government and COAG could improve the identification of priority regulation reforms and their evaluation.

Box 1.1 What is 'regulation'?

A regulation is most simply defined as a principle, rule, or law designed to control, govern or influence conduct. Regulatory instruments shape incentives and influence how people behave and interact, helping societies function well and deal with a variety of problems.

Regulation can be broadly divided into economic regulation (which can directly influence market behaviour such as pricing, competition, market entry or exit) and social regulation (which protects public interests such as health, safety, the environment and social cohesion). Some economic and social regulations apply widely to the community, while others apply only to certain industries, such as agriculture, and financial services.

Regulatory instruments in Australia can also be classified according to their legal basis:

- *Primary legislation* consists of Acts of Parliament. (A legislative proposal for enactment of a law is called a bill until it is passed and receives a Royal Assent, at which time it is a law (statute) and is no longer referred to as a bill.)
- *Statutory rules* are any regulations made under enabling legislation, with a requirement to be tabled in Parliament or be assented to by the Governor or Governor General-in-Council.
- *Other legislative instruments* include guidelines, declarations, orders or other instruments that have legal enforceability, but that are not tabled in Parliament.
- Apart from these regulatory instruments, there are also codes and standards that governments use to influence behaviour, but which do not involve 'black letter' law — these are known as *quasi-regulation*. Forms of co-regulation, such as legislative support for rules developed and administered by industry, and other instruments such as international treaties, are also used to directly or indirectly influence conduct.

Source: PC (2008a).

1.2 Regulation reform in Australia

Australian governments have made considerable efforts to reform regulation over recent decades. There have been three main waves of regulatory reform.

- First, the deregulation of trade and financial markets in the 1980s opened the Australian economy to international markets. The increased competition faced by many enterprises, in turn, highlighted impediments and costs within the domestic regulatory regime.
- This was a stimulus for a second wave of competition reforms of public monopolies in key infrastructure service areas and other government businesses, culminating in the National Competition Policy (NCP). The NCP's Legislative Review Program required the Australian, state and territory governments to examine all legislation that restricted competition. The Australian Government's review program was extended to include other regulation that had a major impact on business.
- In a third wave of reforms, COAG has sought to reduce the costs to business, and the community more broadly, that arise from compliance burdens, notably through differences in regulation across jurisdictions in Australia. The Seamless National Economy (SNE) initiative seeks to improve the national coherence of regulation and reduce its costs while maintaining or enhancing its effectiveness. This work has drawn on earlier stocktake assessments of regulation (notably the *Rethinking Regulation* report (Regulation Taskforce 2006)), and is being informed in part by the series of benchmarking studies undertaken by the Commission.

Progress in the SNE initiative and other streams of the COAG reform agenda is being monitored by the COAG Reform Council, with annual public reports on agreed performance indicators. In a related study, the Commission has been tasked by COAG with assessing the impacts and benefits of the COAG reform agenda (box 1.2). The impacts of the first round of SNE reforms will be one of the first areas to be assessed.

Box 1.2 **Assessing the impacts and benefits of the COAG reform agenda**

The Commission has been asked to undertake a stream of work assessing the impacts and benefits of the COAG reform agenda. The first study in this series is looking specifically at:

- 17 nominated regulation reforms from the Seamless National Economy (SNE) agenda
- vocational, education and training, and initiatives to support transitions from school to further education, training and employment.

Further reports will be provided every two to three years under a standing terms of reference (received June 2010) and according to reporting priorities provided by the Assistant Treasurer. The Commission released a framework report outlining its proposed approach in December 2010.

Source: PC (2010b).

In addition to national reforms pursued through COAG, individual governments have looked for ways to improve their regulatory systems and reduce the associated burden for business. Some state and territory governments have conducted stocktakes of their regulation, while others have established explicit targets for the reduction of red tape and compliance burdens.

These efforts, aimed at improving the stock of regulation, have been complemented by more comprehensive and analytical screening of new regulation, with all jurisdictions adopting RIS processes in line with principles agreed in COAG. As noted, these processes are to be the subject of a benchmarking study in 2012 and are not the principal focus of this study.

It is important to recognise that, over this period, many of the more pressing and achievable reforms have been accomplished (box 1.3). This makes finding the priorities for future reform a more challenging task.

Box 1.3 **Major Australian achievements in regulation reform**

Trade liberalisation — reductions in tariff assistance (that began in 1973) and the abolition of quantitative import controls — mainly in the automotive, whitegoods and textile, clothing and footwear industries — gathered pace from the mid 1980s. The effective rate of assistance to manufacturing fell from around 35 per cent in the early 1970s to 5 per cent by 2000.

Capital markets — the Australian dollar was floated in March 1983, foreign exchange controls and capital rationing (through interest rate controls) were removed progressively from the early 1980s and foreign-owned banks were allowed to compete — initially for corporate customers and then, in the 1990s, to act as deposit taking institutions.

Infrastructure — partial deregulation and restructuring of airlines, coastal shipping, telecommunications and the waterfront occurred from the late 1980s. Across-the-board commercialisation, corporatisation and privatisation initiatives for government business enterprises were progressively implemented from around the same time.

Labour markets — the Prices and Incomes Accord operated from 1983 to 1996. Award restructuring and simplification, and the shift from centralised wage fixing to enterprise bargaining, began in the late 1980s. Reform accelerated in the mid 1990s with the introduction of the *Workplace Relations Act 1996,* further award simplification (limiting prescribed employment conditions in enterprise bargaining agreements) and the introduction of individual employment contracts (Australian Workplace Agreements).

Human services — competitive tendering and contracting out, performance-based funding, and user charges were introduced in the late 1980s and extended in scope during the 1990s; administrative reforms (for example, financial management and program budgeting) were introduced in health, education and community services in the early 1990s.

'National Competition policy' reforms — in 1995, further broad-ranging reforms to essential service industries (including energy and road transport), government businesses and a wide range of anti-competitive regulation was commenced by all Australian governments in a coordinated national program.

Taxation reform — capital gains tax and the dividend imputation system were introduced in 1985 and 1987, respectively. The company tax rate was lowered progressively from the late 1980s. A broad-based consumption tax (GST) was implemented in 2000, replacing the narrow wholesale sales tax system and a range of inefficient state-based duties. And income tax rates were lowered at the same time.

Seamless National Economy (SNE) — this current COAG program aims to improve the national 'coherence' of regulation and reduce its costs, while maintaining or enhancing effectiveness. It covers 36 areas of reform, including 27 deregulation priorities, eight competition reform areas, and ongoing reforms to improve processes for regulation making and review.

Sources: Banks (2005); COAG (2008c).

1.3 How the Commission has approached this study

Regulation reform is important to ensure that the stock of regulation is achieving its purpose (is effective), is not imposing unnecessary distortions or burdens (is efficient), and by addressing real problems will deliver net benefits to the community (is appropriate) (box 1.4). While much attention has been given to compliance costs in excess of those required to achieve the objectives of the regulation, it is important that the regulation reform agenda goes beyond improving the efficiency of regulation to ensuring it is also effective and appropriate.

Box 1.4 The goals of regulation reform

There are three broad goals of regulation reform against which regulation and regulation reform efforts should be assessed.

- *Effective regulation* achieves the objective of the regulation.
- *Efficient regulation* does not impose any unnecessary distortions or burdens on the economy in achieving its objective. In other words, given a policy objective, the regulation is achieved at the least cost to society.
- *Appropriate regulation* addresses a real economic, environmental or social concern and actually delivers a net benefit to the community. A regulation may be effective and efficient but may not have an appropriate objective. 'Zero-waste' or 'zero-risk' are examples of inappropriately specified regulatory objectives. They are inappropriate because the costs of achieving the objective outweigh the benefits, or the objective is simply not achievable at any cost.

Reform frameworks and approaches

The terms of reference direct the Commission to evaluate 'frameworks and approaches' to identifying areas for regulation reform. The Commission has interpreted this to include any actions that governments can take to better manage the stock of regulation. This goes beyond approaches to identify the areas of regulation imposing the greatest costs on business or the community to include approaches that can promote continuous improvement in the efficiency, effectiveness and appropriateness of the stock of regulation and its administration. As such activities cannot be undertaken in isolation and need to be coordinated, and supported by systems and processes that also promote cooperation, consultation and communication, the overall framework for regulation reform is taken to be in scope for this study.

The study draws on examples of approaches to better management of the stock of regulation that have been adopted or promoted in Australia and other relevant countries. The approaches are examined against four criteria:

1. the extent to which the approach identifies regulations (in part, whole, or in combination) that are inefficient, ineffective and/or inappropriate
2. the extent to which the approach identifies alternatives that are efficient, effective and appropriate
3. the influence of the approach in achieving reform — in other words, real change for the better
4. the overall cost-effectiveness of the approach.

This last criterion is important, as efforts to manage and reform the stock of regulation are not costless — either for governments or for businesses and other stakeholders who are asked to contribute to the effort. A key theme of this study is the need to adopt approaches that are 'proportionate' — matching effort to the benefits expected.

Assessing evaluation methods

The second task set out in the terms of reference is to look at methods for the ex post evaluation of regulation reforms. While such evaluations can be undertaken as a stand alone exercise, most of the approaches to reviewing the stock of regulation involve evaluation or rely on information from evaluations of other changes in regulation. Hence the two parts of the study are strongly linked.

Approaches to evaluating and identifying regulatory reforms need to be considered as part of the regulatory system governments have in place to develop, establish, administer and review regulation. The Organisation for Economic Cooperation and Development (OECD 2010f), in its review of regulatory policy across member countries, has emphasised the importance of regulatory governance in achieving good regulatory outcomes:

> The relative failure of regulatory policy to deliver consistently effective regulation so far can be linked to inadequate and underdeveloped regulatory governance. (p. 49)

For these reasons this discussion draft, consistent with the inclusion of 'frameworks' in the terms of reference, looks beyond the discussion of individual approaches to consider how each forms part of a regulatory system. The study draws on the Commission's experience in undertaking stocktakes, benchmarking and in-depth reviews. It also draws on OECD and other sources concerning relevant

regulatory systems around the world to identify best practices, noting that the governance arrangements must suit the broader legal and political environment.

A work in progress

This discussion draft is still a work in progress. It aims to stimulate comment and obtain more focussed input on its draft findings and preliminary proposals. Given the six month timetable for the study and the nature of the topic, initial consultations have been limited to industry peak bodies, government agencies, as well as discussions with officials at the OECD and other countries involved in developing and implementing systems for regulation reform.

1.4 The structure of this draft

This publication presents an overview of the different approaches, frameworks and methods that have been used to identify priority areas for evaluating and reforming regulation. Detailed analysis and examples for each of the main approaches are provided in appendixes available on the Commission's website. These form the basis for the findings and proposals in this draft for improving the review and reform of the stock of regulation, including through improving evaluation of existing regulation and reforms to regulation.

The appendixes provide a range of examples of the various tools and approaches used in identifying and evaluating regulation reforms, with a more detailed analysis of what works or not and why. The discussion draft aims to provide a succinct summary of the material in the appendixes and present lessons based on these detailed assessments.

Chapter 2 sets up the broad context and rationale for analysing the stock of regulation. Chapter 3 describes the approaches that have been used to identify areas for, and promote, regulation reform in Australia and other relevant countries. Chapter 4 sets out the main lessons from the Commission's review of these frameworks, approaches and methods for identifying and prioritising regulations for reform. The methods and approaches for evaluating regulation reform are discussed in chapter 5. Chapter 6 brings the preceding chapters together to discuss how Australia's regulatory system could be refined to enhance its performance.

2 Why reform the 'stock' of regulation?

Key points

- Regulation provides key foundations for a well functioning economy. It can reduce risks to individuals and the community, and protect community resources. But regulation comes with costs.
- Some of the costs imposed by regulation may be unnecessary, with the objectives of the regulation able to be achieved at lower cost.
  - Excessive coverage, extensive and variable reporting requirements, inconsistent and overlapping regulations, and redundant and ineffective regulation can impose unnecessary compliance costs on business.
  - Unintended consequences, such as distortions that affect incentives for investment and innovation, can impose longer term and potentially higher costs on economic activity and result in poor social and environmental outcomes.
- But even regulation that is well made and cost-effective can require subsequent review as costs and benefits change over time. New technologies, changing demographics, preferences and resource ownership — and the accumulation and interaction of regulations — impact on the efficiency and effectiveness of regulation.
- Regulation policy should be aimed at ensuring the quality of regulation at entry, and throughout its implementation and administration. It should also include mechanisms for reviewing regulations, proportionate to the potential gains from reforms.
- Regulation reform itself is not costless, requiring skilled people and resources that have competing uses.
- A regulation reform agenda which aims to improve the efficiency, effectiveness and appropriateness of the regulatory stock must:
  - ensure ‘continuous improvement’ in the stock of regulation and its administration through ‘routine management’ and a program of reviews
  - strengthen the regulatory system to support these objectives
  - prioritise those individual areas of regulation where reform is likely to have high payoffs — ‘big reforms’ that warrant considerable effort.
- In assessing the net return to reform effort, the broad criteria to consider are the:
  - depth of the reform — the magnitude of the impact on compliance costs and distortions for those affected and any flow-on to the rest of the community
  - breadth of the reform — the share of the community affected
  - cost of making the reform — including the effort to build support for reform.

Reform means change for the better. Regulatory changes for the better need to enhance the appropriateness, effectiveness or efficiency of existing regulation (chapter 1). While reform announcements often focus on big specific changes, ensuring continuous improvement across-the-board should also be seen as an important part of a reform agenda.

Section 2.1 commences by outlining the importance and characteristics of 'good' regulation. Section 2.2 explains how this is developed within the context of a regulatory framework. The importance of stock management processes in developing good regulation is discussed in section 2.3. The final section (section 2.4) turns to priority setting and its importance in developing a reform agenda. Priorities include routine management strategies as well as ranking areas for 'big effort' reforms.

2.1 The importance of 'good' regulation

Regulations are requirements imposed by governments that influence the decisions and conduct of businesses, consumers, and other organisations. They may also restrict the range of activities that are undertaken. Expressed most succinctly, good regulation achieves worthy objectives at least cost. Over the years, analysts have identified a number of characteristics which regulation must satisfy to pass this test (box 2.1).

Box 2.1 **What is 'good' regulation?**

According to the Organisation for Economic Cooperation and Development (OECD 2005), 'good' regulation should:

- serve clearly identified policy goals, and be effective in achieving those goals
- have a sound legal and empirical basis
- produce benefits that justify costs, considering the distribution of effects across society and taking economic, environmental and social effects into account
- minimise costs and market distortions
- promote innovation through market incentives and goal-based approaches
- be clear, simple, and practical for users
- be consistent with other regulations and policies
- be compatible as far as possible with competition, trade and investment-facilitating principles at domestic and international levels.

Source: OECD (2005).

There are sound reasons for much regulation. It can reflect and enforce the community's values and the rights of the individual. It can also reduce risks to people's health and safety (such as through consumer policy), address discrimination (such as with equal opportunity laws), and protect the environment from overuse or degradation. Regulation is also part of the institutional architecture for markets to work efficiently, including by establishing property rights and enforcing contracts.

Much of this regulation is aimed at addressing sources of market failure, the main sources of which are: asymmetric information; monopoly power; externalities, and public goods. Market failures can reduce productivity, result in over- or under-production relative to community preferences, and distort consumption and production decisions. However, regulation to correct market failure still needs to be efficient and effective, with the benefits of such corrections outweighing the costs of implementing and complying with the regulation.

Regulation can be used to protect some producers at a cost to others, favour the use of some resources relative to others, and benefit some consumers over others. In some cases such changes are intentional and desirable — for example to look after vulnerable consumers and resources, or to reduce volatility and encourage longer-term sustainability. However, in other cases, there may be no particular merit in the policies and the costs imposed can be considerable.

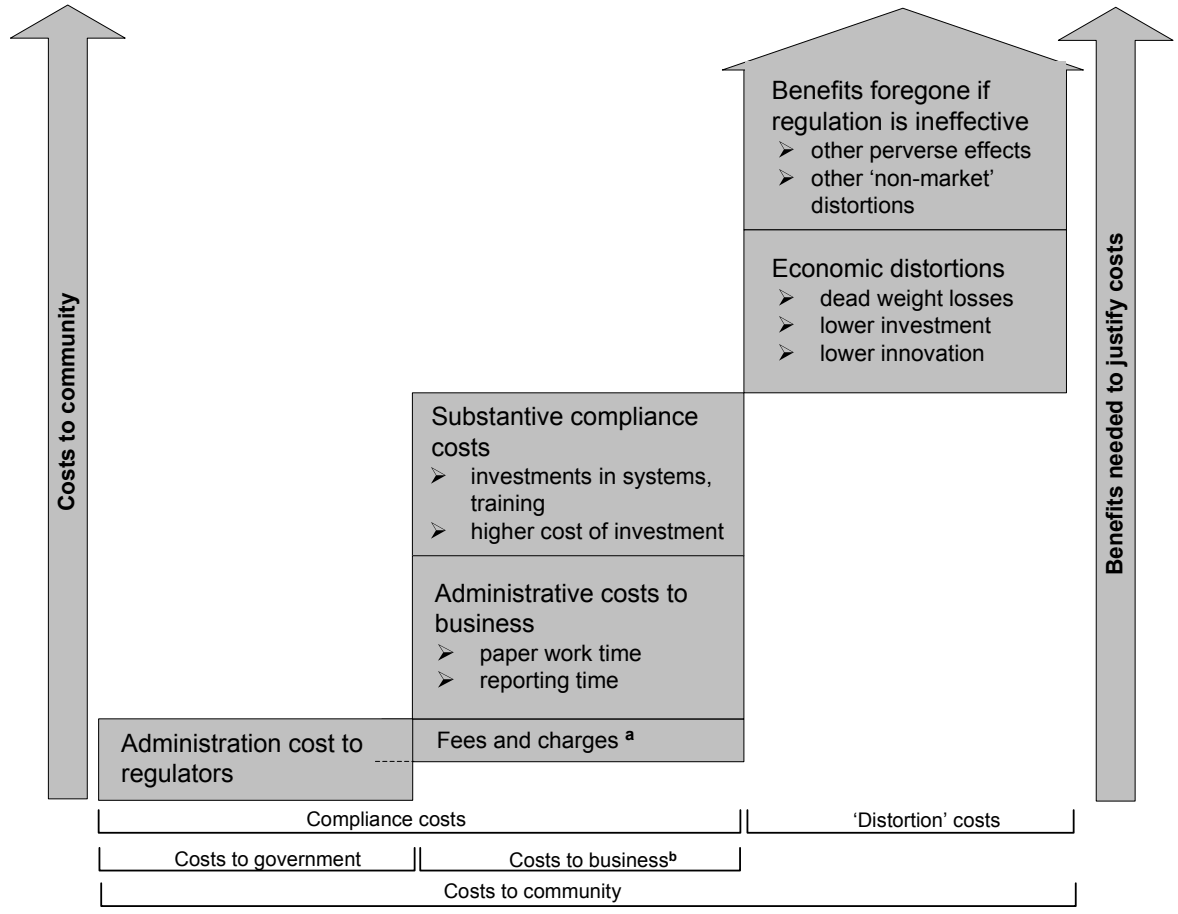
The benefits and costs of regulation

The benefits of a regulation may go beyond the increases in the market value of production and hence consumption. Benefits could include other outcomes that affect the standard of living, such as leisure time and the quality of the environment, and things that affect the quality of life such as personal safety, health and feeling connected to family, friends and the community. Similarly, not all costs will be financial. And, there may be losers as well as winners from the changes resulting from a regulation.

Financial costs are generally the easiest to identify. They include administration costs to governments, and compliance costs to businesses and households. Business compliance costs include the administrative costs of undertaking paperwork, compiling the information, and reporting to regulators. There can also be more substantive compliance costs, such as the investment in staff training and systems and other capital upgrades required to comply with regulation. From a business perspective, the fees and charges paid to regulators also impose a compliance cost, but from the community perspective it is the total cost of the regulator rather than just the costs they pass onto business through cost recovery that matters.

The range of potential costs of regulation are depicted in figure 2.1.

Figure 2.1 **Multiple potential burdens of regulation**
Costs to business and the community



a Cost to business depends on fees and charges passed onto business through cost recovery. **b** Some costs are passed through in prices, lower wages or lower returns on capital.

There may be economic costs arising from 'distortions' — the effects of regulation, for example on competition and incentives for investment and innovation. Such distortions (often unintended), can be due to:

- substitution effects resulting from changes in relative prices, including distorting investment decisions which have long-term consequences
- overly prescriptive regulation which prevents innovative or lower cost approaches to meeting the intended outcomes of the regulation
- interactions of regulations that can compound costs, create inconsistencies, or otherwise pose dilemmas for business compliance.

In addition, there may be other non-market costs arising from environmental and social changes. If regulation is not effective there can also be opportunity costs of the foregone benefits the regulation was intended to deliver.

The costs of administering regulation can be large. For example, *Regulation and its Review* (PC 2005a), reported that the administration expenses of 15 dedicated Australian Government regulatory agencies approached $2 billion in 2003-04, with the Australian Tax Office accounting for a further $2.3 billion in the same year.

The administrative costs to business of regulation are also considerable. For example, an early assessment by the Commission (Lattimore et al. 1998) estimated the administrative compliance costs on business from regulation at around $11 billion in 1994-95, of which around 85 per cent was borne by small and medium-sized enterprises. Based on a survey undertaken by the OECD in 2001, the Commission estimated that the compliance costs of regulations could be as much as 4 per cent of gross domestic product (GDP) (up to $35 billion in 2005-06) (PC 2006c). The Regulation Taskforce (2006) reported the estimates provided by the New South Wales (NSW) Chamber of Commerce that the average business in NSW spends 400 hours a year (or nearly $10 000) complying with regulations or meeting its legal obligations. The administrative costs of regulation in Victoria were estimated at $1.03 billion in 2006, based on the methodology applied in the United Kingdom (UK) (VDTF 2007).

In 2005, the UK estimated total administrative burdens associated with their regulation to be £20-40 billion (1.6 to 3.2 per cent of GDP). The Netherlands estimated their total administrative burden to be €16 billion (3.6 per cent of GDP) in 2002. Denmark and Belgium have also estimated the total administrative burden to be around 2 per cent of GDP (PC 2006c).

While some of these costs are unavoidable (being necessary to achieve the objectives of the regulation) excess costs or unnecessary burdens can be substantial, and have a number of origins (box 2.2).

The costs arising from incentive effects and other distortions are harder to estimate. However, limited evidence suggests that these may well be larger than compliance costs. Based on a regression analysis of a World Bank indicator of regulatory quality, the United States (US) Small Business Administration estimated the total cost of US regulations at US$1.2 trillion in 2008 (around 8.5 per cent of GDP) (Crain and Crain 2010). In addition, estimates of efficiency benefits from previous reforms have been large — for example, the Commission has estimated that real GDP was about 2.5 per cent higher as a result of National Competition Policy (NCP) reforms to utilities and infrastructure (PC 2005b).

Box 2.2 **Sources of 'unnecessary' regulatory burdens**

Rethinking Regulation identified five features of regulations that contribute to burdens on business not justified by the intent of the regulation.

- *Excessive coverage, including 'regulatory creep'* — regulations that appear to influence more activity than originally intended or warranted, or where the reach of regulation impacting on business, including smaller businesses, has become more extensive over time.
- *Regulation that is redundant* — some regulations could have become ineffective or unnecessary as circumstances have changed over time. Other poorly designed regulations might give rise to unintended or perverse outcomes.
- *Excessive reporting or recording requirements* — companies face excessive or unnecessary demands for information from different arms of government. These are rarely coordinated and often duplicative.
- *Variation in definitions and reporting requirements* —this can generate confusion and extra work for businesses than would otherwise be the case.
- *Inconsistent and overlapping regulatory requirements* — regulatory requirements that are inconsistently applied, or overlap with other requirements, either within governments, or across jurisdictions. These sources of burden particularly affect businesses that operate across jurisdictional boundaries.

Source: Regulation Taskforce (2006).

The administration of a regulation can also have an important bearing on both the effectiveness of the regulation and the compliance costs imposed. Heavy handed regulation can reduce innovation and act as a disincentive to investment, including through entry of new firms.

For example, the Department of Innovation, Industry, Science and Research (sub. 6) noted in the context of health regulation:

> Some aspects of regulation governing access to medicines are controlled by formal Agreements between specific stakeholder groups and the government. These Agreements, while designed to deliver the specific outcomes for patients and consumers of medicines, may, in some cases, do so at the cost of restricting businesses as well as service delivery innovation. Review of such regulation may lead to measures that provide such services in better and more efficient ways. (p. 20)

Uneven administration of regulation may confer advantage to some, while failure to enforce can impose costs on the compliant firms and on consumers. Inconsistent decision making by regulators can also result in businesses over-investing in compliance, while slow decision making leads to delays that can be costly to business.

2.2 Managing the stock of regulation

There has been considerable focus over the last decade or two on improving the quality of regulation through better management of the flow of new regulation (box 2.3). But, given its relative size, governments are increasingly looking at ways to better manage the stock of regulation. The OECD (2011a), in its draft recommendations on regulatory policy and governance, proposed that member countries:

> Conduct systematic programme reviews of the stock of regulation against clearly defined policy goals, including consideration of costs and benefits, to ensure that regulations remain up to date, cost justified, cost effective and fit for purpose. (p. 5).

The volume and scope of regulation continues to grow rapidly. *Rethinking Regulation* (Regulation Taskforce 2006) noted that in the sixteen year period from 1990 to 2006, the Australian Parliament passed more pages of legislation than in the previous ninety years. This trend shows no signs of abating. A survey of regulators at the Australian and state and territory government levels in 2008 identified 439 different business regulators (PC 2008a). The same study noted that at the Australian Government level there were 1279 Acts generating 98 486 pages of legislation and 18 000 statutory rules generating another 90 000 pages of subordinate legislation. Across all the jurisdictions, there was well over half a million pages of legislation by June 2007, with over 48 000 added in the previous year.

This growth in regulation is occurring partly in response to the increased complexity of markets and technologies, and greater recognition of the importance of managing non-market resources well. It is also in response to demands by parts of the community for formal institutions to take on social insurance roles previously left to the informal sector or social institutions. For different reasons, these two forces are reflected in the growing use of regulation to address perceived risks to the community. Government resistance to such pressures may be low, in part because of the low budgetary cost of regulation, but also because governments seek to be responsive to community demands.

Box 2.3 **Managing the flow of Australian Government regulation**

The Australian Government, in 1985, established a system of regulation impact statements (RIS) for all new regulation that imposes a burden on business. The RIS guidelines have been revised periodically, most recently in 2010. All states and territory governments have also implemented a RIS type system, which is now entrenched in Council of Australian Governments (COAG) under the National Partnership Agreement to Deliver a Seamless National Economy.

A RIS is mandatory for all decisions made by the Australian Government and its agencies that are likely to have a regulatory impact on business or the not-for-profit sector, unless that impact is of a minor or machinery nature and does not substantially alter existing arrangements. This requirement includes amendments to existing regulation and the rolling over of sunsetting regulation.

The RIS process is overseen by the Office of Best Practice Regulation (OBPR), previously located within the Productivity Commission, now in the Department of Finance and Deregulation. OBPR comments on compliance with the Government's RIS requirements and the adequacy of the RIS in its Cabinet coordination comments. The Cabinet Secretariat provides a gate-keeping role to ensure that regulatory proposals coming to the Cabinet and sub-committees of the Cabinet meet the RIS requirements. The Cabinet Secretariat will not circulate final Cabinet submissions or memoranda, or other Cabinet papers, without adequate RISs unless the Prime Minister has deemed that exceptional circumstances apply.

The OBPR maintains a central online public register of all RISs including those assessed as inadequate. In consultation with the agency, RISs and the OBPR's assessments of RISs are published on the register as soon as practicable from the date of the regulatory announcement.

Section 7 of the RIS guidelines (Implementation and review) requires that a RIS provide information on how the preferred option would be implemented, monitored and reviewed. Interactions between the preferred option and existing regulation of the sector should be clearly identified.

Source: Australian Government (2010b).

The need to actively manage the stock of regulation is increasingly recognised internationally. In the US, for example, the importance of managing the stock of regulation is currently being promoted. The former chief economist at the Council of Economic Advisers, Michael Greenstone (2011a), stated:

> Limiting evaluation to the period before implementation lacks common sense. … We should expect – in fact, demand – a similar form of performance evaluation for our nation's vast regulatory structure, based on hard evidence about what works. We need a culture of regulatory experimentation and evaluation that can measure a regulation's success. … This requires modest resources, but costs are small compared to the costs of regulations that stifle job growth or otherwise fail the American people. (p. 1)

Even if all new regulation were subject to rigorous ex ante assessment processes, some of the stock of regulation will inevitably impose an undue burden. Identifying regulation that imposes excessive costs, or does not meet its purpose, and rectifying such deficiencies can lift productivity and bring other benefits, such as improving choice and opportunity.

Stock management is part of a sound regulatory system

Active management of the stock of regulation is part of a sound regulatory system. Managing the stock effectively means retaining 'good' regulation, while removing or amending regulation that is no longer fit for purpose.

While regulation reform may suggest 'headline' changes, stock management encompasses a range of possible actions from routine to major. At the simpler end, regulators must fine tune the administration of regulations to reduce compliance costs imposed on the businesses they regulate. In the middle, uncertainty about the impact of some regulations can justify a review during implementation or early in its administration. At the more complex end, where a 'dangerous cocktail' of regulation could have emerged, a number of regulations may require substantial legislative changes. In such cases, the full range of regulations impacting on an industry may need to be examined, with a benefit-cost test applied to different options to select the most cost-effective approach, as well as to ensure that the costs are justified by the benefits of the regulation.

2.3 Marshalling reform efforts

Reforming regulation is rarely costless. It takes time and effort to examine a regulation and to develop alternatives, and then to implement any changes. Even repealing a regulation can involve adjustment costs. Therefore, for a reform to proceed, the benefits that reform brings — in terms of lower administration and compliance costs, better allocation of resources, increased competition, or greater incentives for innovation — must be greater than the costs of undertaking the reform.

Prioritising reform is important not only to reap the biggest gains, but also because the skilled people and other resources available for this endeavour are limited. Reviews can also place significant demands on the community and business — comments about review fatigue are increasingly common. Moreover, review activity can create uncertainty, especially where there are long periods between the announcement of a review and the adoption of recommendations.

Prioritisation should:

- focus efforts, including community input
- shorten the time required to make decisions, and
- raise the probability of successful reform.

This also involves paying attention to the sequencing and 'packaging' of reform — to ensure the groundwork is laid before other reforms (that may be dependent on these foundations for their effectiveness) are implemented.

Many reforms worth doing can be hard to sell, either because of the complexity of the issues or because of political sensitivities, particularly where the evident losers are more vocal than the potential winners. Concentrating resources and public attention allows a more rigorous analysis of the net benefits of identified reforms and a more focussed consultative process, increasing the likelihood that reform will be successful.

There are other actions in a reform agenda that, by their nature, are better as on-going activities. Here the issue is less about prioritisation than about an efficient process to ensure these activities are undertaken in a cost-effective way.

Proportionate effort

In developing a regulation reform agenda, governments need to consider the return on their efforts, which should be proportionate to the expected benefits. For example, relatively low return activities, such as fine tuning, may be warranted because they can be achieved with relatively little effort.

More substantial reviews need to be prioritised, recognising that different reforms have different time profiles of costs and benefits. To maximise the returns to reform effort, a reform agenda will need to allocate the scarce available resources to the pursuit of those reforms that offer the highest returns to the community. It must also provide a way of ensuring reform efforts are cooperative and coordinated. Uncoordinated reform efforts can result in overlap or duplication of reviews, reform fatigue for business, implementation overload, and poor sequencing of important reforms that can undermine their success. To enhance the success of these efforts, the reform agenda should build public and political support for reform.

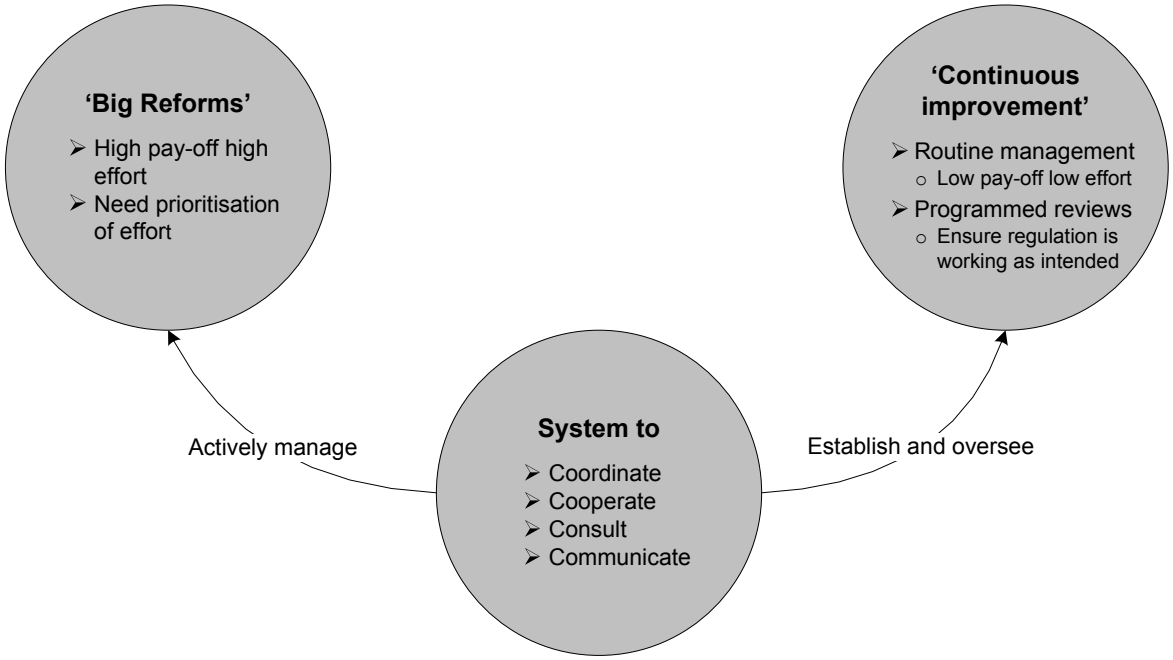
Governments have applied a number of criteria to assist in identifying where the rates of return from reform are likely to be higher. The assessment criteria need to vary for different sources of burden. However, the rate of return from reform will be influenced by factors which either affect the costs or benefits, including its probability of success. There are three primary determinants.

- *Depth of reform* — the extent to which the existing situation differs from the achievable ideal and the impact this has on the community. Big costs imposed on businesses and large distortions in the allocation of resources usually offer greater returns to correcting these problems, especially if the gains are widespread.
- *Breadth of reform* — the share of the economy or community affected by the changes. Some reforms may affect a relatively small share of the economy or community, (such as local pollution levels). Others can affect almost everyone (such as food standards for milk) where there is a trade-off between reducing risk and cost.
- *Cost of reform* — the cost of making the change is distinct from any change in the compliance cost or other burdens as a result of the change in the regulation. This cost of reform includes the time and financial cost for government, business and others to make the case for, then implement, the reform. It also includes the cost to: investigate the changes needed and propose and assess the options for change; consult and test the proposed changes; and build support for the reform. Reforms that are expensive to undertake require a larger pay-off to warrant this investment.

In short, a reform agenda (figure 2.2) should:

- prioritise 'big effort' reforms — by setting out a process for establishing priority reviews and then following through to progress reform in a sequenced way
- oversee an ongoing strategy of continuous improvement — putting in place the processes to fine tune regulation to enhance its efficiency and effectiveness, ensure regulation is working as intended, remove redundant regulation, and flag opportunities for more substantial reform effort
- strengthen the institutional architecture and governance arrangements to support a continuous improvement strategy and prioritisation of the big reform efforts. This should include strengthening processes to promote the completion of reforms in a timely way.

Figure 2.2 **The elements of Regulation Reform**



The rest of this study focuses on the frameworks, approaches and systems that governments can draw on. Chapters 3 and 4 look at different approaches to reviewing regulation and identifying reform needs, their relative merits and lessons from their use. Chapter 5 discusses the evaluation techniques that such reviews can employ. Finally, chapter 6 considers the framework or system for regulation reform and scope for improvement.

3 Approaches to reviewing and reforming the stock of regulation

Key points

- A variety of approaches have been used in seeking to reform the stock of regulation. The approaches vary in their depth (the nature of the burdens and benefits they consider) and breadth (the number of regulations and industries covered).
- *Management* approaches such as regulator strategies, regulatory budgets, 'one-in one-out' rules and red tape reduction targets, address unnecessary administrative costs in a routine or incremental way.
- *Programmed* reviews are undertaken on a planned basis to ensure that regulation is needed and is working as intended. They include:
  - sunsetting, where legislation (usually subordinate) lapses after a specified period if not renewed
  - embedded statutory reviews, which are set out as requirements in the legislation that established the regulation
  - post-implementation reviews, which in the Australian Government jurisdiction are required where initial regulation impact statement (RIS) requirements have not been met.
- More significant reviews are often undertaken on an *ad hoc* basis. They include:
  - public stocktake reviews to identify regulation that is imposing unnecessary burdens. Stocktakes tend to be broad, but the depth of the issues covered can be limited by the 'complaints-based' nature of the approach
  - principles-based reviews, which apply a common principle as a screening mechanism to identify the need to review a regulation. The most generally applied principle is that restrictions on competition need to be justified, but other principles include national and international coherence
  - benchmarking seeks to compare regulation, regulatory processes, and/or regulatory outcomes across countries or jurisdictions.
  - in-depth reviews devote resources to achieving a full understanding of the regulatory issues and developing options for reform, typically focusing on a single industry or category of regulation.

A number of different and often overlapping frameworks and approaches to identifying areas requiring regulation reform are used in Australia and other countries. Some of the approaches are complementary, others duplicate effort. Some are well suited for identifying high return priority areas and options for reform. Others are well suited for identifying small but common burdens that can easily be removed and should be included in any program of regulation reform. Some provide the options for reform, while others indicate that reform is needed.

An efficient and effective system for managing the stock of regulation system would assign each approach to where it is best suited to the task required so as to maximise the overall payoff to review and reform effort.

Approaches to reviewing and reforming the stock of regulation include: in-depth reviews; embedded statutory reviews; principles-based reviews; post-implementation reviews; sunset clauses; stocktakes; red tape reduction targets; stock-flow linkage rules such as regulatory budgets and 'one-in one-out' rules; and regulator management strategies. This chapter briefly summarises each approach and gives some examples of its application. Section 3.1 outlines three types of approaches to reviewing and reforming the stock of regulation. The following three sections go on to describe the different approaches within each category.

An analysis of each approach and lessons on its application is provided in chapter 4. More detailed examples of each approach are in appendixes B to G.

3.1 Three broad types of approaches

Over the last few decades, governments have put considerable effort into establishing systems to improve the quality of new regulation. There has been some concern, however, that this has diverted attention from the task of managing the stock of existing regulation. Effort is required on all fronts, as the Organisation for Economic Cooperation and Development (OECD 2010h) noted recently:

> The assessment of ex ante regulatory impacts improves policy design but it only constitutes one part of regulatory management. Institutionalising accountability and results in regulation may need to be adjusted to practical outcomes after policy implementation. Closing the loop is essential if regulatory policy is to be performance-driven and politically accountable. This requires ensuring that ex ante impact assessment foresees the need of future ex post consideration of regulatory impacts. A fully integrated approach to regulatory policy therefore needs to include considerations for ex post evaluation at an early stage, with a full approach of regulations "from cradle to grave". This is essential as sun-setting clauses can only be effective if accompanied by a requirement for ex post evaluation. These should be associated with a cycle of periodic reviews of the stock of existing regulations to ensure that the instruments are still achieving their intended objectives and to identify needed adjustments. (p. 6)

There are three broad types of approaches that governments, overseas and in Australia, have used to reform the stock of regulation.

- *Management approaches* have been introduced as part of a general 'good housekeeping' approach to managing the stock of regulation. This category includes regulators' feedback processes and requirements to take account of existing regulation in proposing new legislation.
- *Programmed reviews* examine the performance of specific regulations at a specified time, or when a well-defined situation arises, to ensure regulation is working as intended. The scope of these programmed reviews varies, but they may consider the efficiency, effectiveness and/or the appropriateness of a regulation. This category includes sunsetting legislation, embedded statutory reviews and post-implementation reviews (PIRs).
- A*d hoc reviews* have been commissioned as a need arises. They include public stocktakes and principles-based reviews, that look at a wide range of regulation, and targeted reviews and benchmarking exercises that look at specific regulations or sets of regulation that might affect a particular industry or outcome area.

These categories are somewhat arbitrary and some approaches cross the boundaries. This includes sunsetting, which has some characteristics of a routine management tool.

Table 3.1 summarises the main approaches identified that governments have adopted for reviewing and reforming the stock of regulation.

Table 3.1 **Approaches to managing the stock of regulation**

	Main features	*Use (examples)*
Management approaches		
Regulator management strategies (appendix G)	Includes complaints portals, regular reviews to examine complaints and other problems identified by the regulator.	Office of the Registrar of Indigenous Corporations Australian Securities and Investments Commission Australian Tax Office
Regulatory budgets (appendix G)	Departments are assigned a 'budget' of compliance costs that regulation can impose on businesses. New regulations that impose an additional cost must be offset by reductions in the costs imposed by existing regulations.	United Kingdom 2010 — onwards (partial application)
'One-in one-out' rules (appendix G)	Introduction of a new legislative instrument is to be offset by the removal of an existing instrument.	No examples — much discussed but possibly never applied
Other stock-flow linkage rules	Requirement to consider scope to remove or reduce other regulation when introducing new regulation	Australian Government RIS requirement
Red tape reduction targets (appendix G)	Targets for savings in compliance costs through agency actions to reduce paperwork and reporting requirements for compliance with business regulation.	Netherlands (2003–2010) South Australia (2006–2012) Victoria (2006-2012) United Kingdom (2005-2010)
Programmed reviews		
Sunset clauses (appendix D)	Requirement for all (usually subordinate) legislation to lapse after a specified period. Remade legislation with significant impacts on business is required to go through the regulation impact statement (RIS) process.	Australian Government — every 10 years
Embedded statutory reviews (appendix D)	Identified during the development of the legislation. A requirement for a review (often 2 to 5 years after implementation) usually where there are significant uncertainties about the impact of the regulation. The scope of the review varies.	Part IIIA of the *Competition and Consumer Act 2010* *Wheat Export Marketing Act 2008*
Post implementation reviews (appendix D)	Required for all Commonwealth legislation that was exempted from the RIS process or was non-compliant.	Office of Best Practice Regulation (OBPR) — one completed, around 40 required

(continued next page)

Table 3.1 **(continued)**

	Main features	*Use (examples)*
Ad hoc reviews		
Public stocktakes (appendix B)	Broad reviews calling for businesses to identify areas of regulation imposing excess burdens. Follow up analysis screens the 'complaints' to assess validity and options for reform.	Small Business Deregulation Taskforce (1996) Regulation Taskforce (2006) Western Australia (2009)
Principles-based reviews (appendix E)	Broad reviews that use a principle to screen legislation for further review. May require that the legislation be repealed or amended unless the failure to satisfy the principle can be shown to be in the public interest.	National Competition Policy Legislative Review Program (1995–2006) Council of Australian Governments (COAG) Seamless National Economy (2008-09 – 2012-13)
Benchmarking (appendix F)	Comparisons of specific aspects of regulation across countries or jurisdictions, such as administrative costs of compliance, numbers of legal restrictions, delay time and other indicators of the performance of regulation.	World Bank — *Doing Business* 2004 – onwards OECD benchmarking such as the index of product market regulation Productivity Commission series for COAG
'In-depth' reviews (appendix C)	One-off, usually ad hoc, comprehensive reviews, focusing on specific industries or sectors. Commissioned by government and usually independent.	Wallis (1996-97) and Campbell (1979) inquiries into the Australian financial system Review of Quarantine and Biosecurity (Beale) (2008) Chemicals and Plastics Regulation (PC 2008)

Sources: Appendixes B to G.

3.2 Management approaches

As noted, management approaches involve mainly incremental changes that occur though the ongoing development and administration of regulation. These approaches are discussed in detail in appendix G.

Regulator management strategies

The way in which regulators interpret and administer the regulation for which they are responsible can have a major bearing on the compliance costs for business. Any regulation reform agenda would need to consider whether regulators give sufficient

attention to applying regulations in ways that are effective and efficient, and to assess whether the regulators are achieving this in practice.

The scope regulators have for 'fine tuning' regulation depends on the extent to which the regulation prescribes the way it is administered. Where regulation sets out objectives and principles, rather than explicit requirements, regulators have greater scope to apply the regulation in a way that can minimise the regulatory burden. Regulators may also be able to seek minor amendments to the regulation they administer through the use of omnibus bills. These allow a number of minor amendments of a machinery nature to be put through as a package, without the need for a RIS.

Regulators adopt various strategies to identify the need for fine tuning the regulations they administer. Strategies include:

- moving to risk-based compliance and enforcement approaches, with the OECD (2010d) noting that around half the regulators in Australia have moved to a more 'light handed' approach
- monitoring of complaints and issues, with periodic reviews and consultation to test validity and develop strategies to address the problems
- use of stakeholder 'consultative' groups to provide feedback and identify problems and solutions that are within the scope of the regulator to implement
- monitoring of indicators such as time spent completing forms and turn-around time for applications.

Regulator management strategies may be part of a formal continuous improvement program conducted by the regulator. For example, the Office of the Registrar of Indigenous Corporations (ORIC) maintains a list of complaints and problems that ORIC review using consultative processes every three years (ORIC, pers. comm., 27 July 2011). Regulators may also take action to review practice in response to one-off events or a build up in pressure from their clients.

Box 3.1 provides examples of the strategies adopted by regulators.

Box 3.1 Examples of regulator management strategies

A range of strategies appear to have been used by regulators to improve both the stock of regulation, and their administration of it.

A number of regulators have established consultative forums, which facilitate consultation and feedback from industry or the community. Examples of regulators using consultative forums include Australian Securities and Investment Commission, Australian Communications and Media Authority, and the Therapeutic Goods Administration.

Some regulators also have internal mechanisms for appealing and reviewing enforcement decisions. One example is the Industry Complaints Commissioner within the Civil Aviation Safety Authority. The Commissioner is a co-ordinating point for all complaints about the authority, and may recommend changes to the authority's processes.

Feedback obtained from these mechanisms and processes, or other consultation or complaints processes, can be used to improve the stock or administration of regulation, or be the trigger for a review of the regulation. For example ORIC cut the number of reporting requirements in annual reports by 30 per cent in response to industry feedback.

Regulators may also commission a review of their processes. For example the Victorian Environmental Protection Authority, commissioned an independent review of its monitoring and enforcement processes. The review made 119 recommendations, which are in the process of implementation.

Source: Appendix G.

Stock-flow linkage rules

'Stock-flow linkage' rules require action to reform or maintain the stock of regulation in order to introduce new regulation.

Regulatory budgets are often proposed, but rarely implemented. This approach requires agencies to ensure that the total compliance costs imposed by the regulation remains within a designated 'budget' constraint. Additional compliance costs imposed by new regulation must be offset by reductions in costs imposed by existing regulation. In some proposals, a trading of budget across agencies could ensure that the total compliance costs imposed on business are not increased, while allowing more valued legislation to be introduced. (Under this scenario, those agencies would have to 'buy' some budget from other agencies.) However, the implementation of regulatory budgets poses considerable challenges, including allocation of budgets and the costs of measurement. The United Kingdom (UK)

appears to be the only jurisdiction to have actually implemented this approach, and only to a partial extent (HM Government 2011).

A 'one-in one-out' rule requires a regulation to be removed for each new piece of regulation that is introduced. This rule could be applied at a government level or agency level. Again, while often raised, examples of its application in practice are hard to find. Variants suggested include a 'one-in two-out' rule (proposed by the Opposition in Tasmania), or the targeting of pages of legislation rather than the number of instruments.

RIS requirements (including the Australian Government's) can include a provision that consideration be given to existing regulation when new regulation is being introduced. Agencies are typically required to document why existing regulation is not adequate, and can be further required to assess whether it could be reduced as part of the new regulatory proposal.

Red tape reduction targets

Perhaps the best known efforts to reduce the burden of regulation on business are the red tape reduction programs. These have been adopted in most Australian jurisdictions, and considerable compliance cost savings have been reported (box 3.2).

Both percentage reductions and dollar targets for compliance cost savings have been used in Australia and abroad. A reduction in compliance costs of 25 per cent has been the most common target, although this is generally converted to a monetary value. The 25 per cent target was first used by the Netherlands, adopted on the basis that savings in business administration costs of this order could be achieved without reducing the effectiveness of the regulation. The Netherlands, having achieved this target, then instituted another 25 per cent cut (OECD 2007a).

The percentage reduction approach requires some baseline measurement of the costs of compliance imposed across the economy. This exercise can be expensive — the UK spent £18 million to estimate the administrative cost of regulation at £20-40 billion (NAO 2008). The Victorian Department of Finance and Treasury (2007) reasoned that the burden of regulation in Victoria was likely to be a similar share of economic activity as in the UK (1 per cent of GDP, with 44 per cent of this estimated to be imposed by state regulation) imputing $1.03 billion as the administration costs of regulation in 2006.

Box 3.2 **Red tape reduction targets in Australia**

Several Australian states have used red tape reduction targets to reduce regulatory burdens on business, including Victoria, South Australia, New South Wales and Queensland.

Victoria — Victoria has a target of a $500 million reduction in compliance costs to business by July 2012. The costs covered include administrative costs, substantive compliance costs, and delay costs. As at July 2010, Victoria had estimated a reduction in the compliance burden of $401 million.

In order to help meet the target, Victoria used incentive payments — including a $42 million tender fund. A model based on the Dutch standard cost model was used to estimate the regulatory savings of the reforms.

South Australia — In 2006, South Australia set a target of a $150 million reduction in net administrative and compliance burdens to business by 2008. Agencies were requested to develop plans outlining potential reforms, and a series of reviews were undertaken. The Australian Government OBPR business cost calculator was used to estimate the burden reductions associated with the reforms.

An independent audit by Deloitte (South Australian Government 2008) suggested that the reduction target was exceeded. Following this, the South Australian Government announced another $150 million reduction target by 2012.

New South Wales — New South Wales has a target of a $500 million reduction in red tape (including both administrative and substantive compliance costs). As at June 2010, an estimated $400 million of reductions had been achieved.

Queensland — The Queensland Government set a target of a $150 million reduction in the administrative and compliance burden to business between 2009 and 2013. Departments have submitted simplification plans, which outline a range of potential reforms.

Source: Appendix G.

The monetary target approach still requires agencies to assess the savings resulting from their efforts to reduce administrative or compliance costs. A range of 'cost calculators' have been applied to make these estimates of savings (chapter 5; appendix I). (Such calculators are also used in estimating the cost of new regulation.)

An alternative approach focuses on the number of 'must comply' provisions within the legislation and regulation. The Canadian province of British Columbia appears to have been successful in reducing compliance costs through targeting reductions in such requirements (box 3.3).

Box 3.3 **Cutting compliance requirements — the British Columbia example**

The Canadian province of British Columbia's approach to reducing red tape has focused on the number of regulatory requirements. In 2001, when the scheme was announced, there was an estimated 360 000 regulatory requirements associated with regulation. The objective of the scheme was to reduce the number of requirements by 33 per cent by 2004.

This target was exceeded, with the number of regulatory requirements dropping by 36 per cent by 2004. Following this, a further target of 'no increase' in the number of regulatory requirements between 2004 and 2012 was announced. As of March 2011 this target is also on track to be exceeded, with the number of regulatory instruments actually dropping by 10 per cent since 2004.

Some examples of requirements removed include:

- reducing the number of reporting requirements for schools by 10–15 per cent, and reducing the timing load of the remaining reports
- removing a requirement for travel agents to have commercial premises
- allowing a greater range of vehicles to be used without a policy-issued permit.

Source: Appendix G.

3.3 Programmed reviews

Programmed reviews refer to reviews that are set out in legislative requirements. These tend to focus on a single regulation or, for sunset reviews, potentially a package of regulations. Most have a specific time period in which a review must be undertaken. Further details on these approaches are in appendix E.

Sunsetting

Sunset requirements, initially introduced as clauses in specific pieces of legislation, now generally provide for all legislation of a specified type to lapse unless remade. The motivation for sunsetting is the presumption that most regulation in its original form has a 'use by' date. Sunsetting provides a useful housekeeping mechanism for dispensing with redundant or increasingly inappropriate regulation. Given that automatic lapsing would be problematic for much primary legislation, most sunset arrangements are confined to subordinate legislation.

Where governments do not want the regulation to lapse, it must be remade and meet the same procedural requirements as new legislation (including regulatory impact assessment). Most sunset programs provide for agencies to package a number of regulations together for review, and the clock for sunsetting is reset for legislation renewed in this way.

Most jurisdictions in Australia have a 10 year sunset period (including the Australian Government, Victoria, Queensland, South Australia and Tasmania). New South Wales has a five year term. For most jurisdictions, sunset requirements when introduced applied only to new instruments. However, the sunset requirements introduced by the Australian Government and Queensland also apply to the pre-existing stock of regulation. The large volume of legislation annually means that even if old legislation does not sunset, a large number of instruments could sunset in any given year. Where the existing stock is included, the initial workload can be considerable unless the sunsetting of existing legislation is staggered (box 3.4).

Other residual review requirements

The Australian Government, following a recommendation of the Regulation Taskforce in 2006, introduced a further requirement that all regulation not subject to sunsetting or other evaluation be reviewed every five years. (It appears that, in practice, very few regulations would now fall into this category.)

Box 3.4 The work load from sunsetting regulation

The sunsetting provisions for Commonwealth subordinate regulations, as set out in the *Legislative Instruments Act 2003* (LIA), require that 18 months before a given sunsetting date a list of instruments due to sunset be tabled in Parliament. The Parliament then has six months in which to pass a resolution to allow a legislative instrument or provisions of a legislative instrument on that list to continue in force as if remade (Australian Government 2009).

Australian Government legislation will start coming into review in 2013, with instruments sunsetting from early 2015. Estimates provided by the Attorney-General's Department indicate that around 14 000 principal instruments are scheduled to sunset between 2015 and 2022. The bulk of these will sunset on or before 1 April 2018, including all regulations made prior to the commencement of the Legislative Instruments Act in 2005. The bulk of these are legislative instruments made prior to the introduction of the LIA.

Instruments scheduled to sunset range from a large number of relatively minor regulations to more complex regulations with more significant impacts on business. It is not clear how many of these instruments will need to be remade, and if so, how many of the remade instruments will have an impact on business and trigger the Government's best practice regulation requirements for the preparation of a RIS. Currently, around 2-3 per cent of new instruments require a RIS.

While the exact extent of the forthcoming review task facing departments and agencies is not known at this time, the task is potentially very large. Concerns have been expressed for some time about how this will be handled. The 2009 review of the LIA commissioned by the Attorney-General (Australian Government 2009) warned that:

> Sunsetting may place acute demands on drafting resources if agencies propose that legislative instruments due to sunset should be remade. This will have a flow-on effect for [the Attorney-General's Department's] lodgement and registration workload. (p. 48)

New South Wales' (more frequent (five-yearly)) sunsetting requirement has seen substantial numbers of regulations scheduled to sunset being postponed. For example, a report on regulatory impact assessment in New South Wales showed that, of the statutory rules that were due to sunset on 1 September 1998, 63 were repealed and 101 were retained. For approximately 70 per cent of those 101 rules, the sunsetting date had already been postponed by between three and six years (OECD 1999).

Source: Appendix E.

'Embedded' statutory reviews

Some legislation includes a requirement for a review to be conducted and sets out the specifics of the review, such as timing, the scope of the review and the governance arrangements. Such 'embedded' reviews have been used for significant areas of regulation where there are uncertainties about the efficacy or impacts of the

legislation (including potential for collateral effects or other unintended consequences), or where the regulatory regime is transitional. Embedded statutory reviews also appear to have sometimes been used to give comfort to stakeholders concerned that they might be adversely affected by new legislation (box 3.5).

The scope of embedded statutory reviews can vary considerably. For some, such as the Commission's review of the 'Part IIIA' regulations governing third party access to essential facilities, major changes or repeal of the legislation were within the scope of the review (PC 2001). The scope of the wheat marketing arrangements review undertaken by the Commission (PC 2010f) included regulatory arrangements to protect growers while encouraging competition, but did not allow the option of a the return to a single desk. More limited embedded reviews may only consider implementation design features.

Embedded statutory reviews are typically designed to commence around five years after implementation (to allow time to assess how the regulations are working). Alternatively, legislation could specify an event which, if observed, will trigger a review. There do not appear to be any rules or guidelines about when an embedded review should be included in legislation, nor about the scope of the review.

Post-implementation reviews

In the Australian context, a post-implementation review (PIR) refers to a review which is required for any legislation that has avoided or is non-compliant with the RIS process and has been exempted or permitted to proceed. The *Best Practice Regulation Handbook* (Australian Government 2010b) notes that while the terms of reference can vary depending on individual circumstances, PIRs should generally be similar in scale and scope to what would have been prepared for the decision-making stage, including assessing impacts of the regulation and whether the Government's objectives could be achieved in a more efficient or effective way. However, there is no mandatory requirement that a PIR follow all seven steps required in a RIS.

PIRs are to be commenced within two years of the regulation being implemented. It was anticipated that few regulations would need PIRs, but the numbers have risen significantly. While only one has been completed to date, around 40 are required to be conducted over the next few years. In keeping with the PIR being a failsafe mechanism where a RIS was not undertaken, the process is overseen by the OBPR.

Box 3.5 Examples of 'embedded' reviews

Price regulation of airport services

In the Commission's first review of price regulation of airport services (PC 2002), the Commission recommended a shift to 'light handed' regulation. As this represented a substantial shift from existing arrangements, the Commission recommended that 'price regulation of airports should be reviewed towards the end of the five-year regulatory period. The review should be independent and public. Its objective should be to ascertain the need for any future price regulation of airports (including price monitoring or more stringent price regulation)' (recommendation 6, p. XLVII).

Wheat Export Marketing

Section 89 of the *Wheat Export Marketing Act 2008* required that the Productivity Commission commence a review of the new arrangements by 1 January 2010. The review commenced in September 2009 and a final report was provided to the Government in July 2010.

Fuel standards

Under the legislation for national fuel quality standards statutory independent review was required two years after the first set of standards come into effect and thereafter every five years. The *Fuel Quality Standards Act 2000* provides, in section 72, for a review of the operation of the Act, to be undertaken as soon as possible after the second anniversary of the commencement of Part 2 of the Act. The review was completed in 2005.

National Access Regime

The Commission completed an review of the National Access Regime in 2001. In April 1995 the Australian, state and territory governments signed three Intergovernmental Agreements, including the Competition Principles Agreement (CPA), which established the framework for competition policy reforms. The CPA required that its own terms and operation be reviewed after five years of operation. Terms of reference for that review specified that the review of Clause 6 of the CPA be incorporated into the competition policy review of Part IIIA of the then *Trade Practices Act 1974*.

Telecommunications Competition Regulation

The Commission's inquiry into Telecommunications Competition Regulation released in 2001, stemmed from a requirement in section 151CN of the *Trade Practices Act 1974* for a review of Part XIB of that Act which deals with anti-competitive conduct in the telecommunications sector.

Fisheries Management (New South Wales)

In its Better Regulation Statement for proposed amendments to the *New South Wales (NSW) Fisheries Management Act 1994* the NSW Department of Primary Industries stated that a statutory review of the Act would be undertaken in 2009-10, in accordance with section 290 of the Act.

Source: Appendix D.

PIRs are also required in Queensland in similar circumstances. A PIR must be commenced within two years of the implementation date of any regulation with significant impacts where a Regulatory Assessment Statement was not conducted. The PIR should assess the impact, effectiveness and continued relevance of the regulation to-date and analysis should be proportionate to the issue being addressed (Queensland Government 2010).

A PIR would be limited in its ability to assess the appropriateness of a regulation where a full RIS was not required in the first place. At the Commonwealth level, only an 'implementation' RIS is required for regulation that is regarded as meeting an election commitment:

> … where a regulatory proposal implements a specific election commitment, the RIS should focus on the commitment and the manner in which the commitment should be implemented, not on the initial regulatory decision. (Australian Government 2010b, p. 15)

3.4 Ad hoc reviews

A variety of other types of reviews are commissioned by governments on a more or less ad hoc basis. There are two main types:

- general reviews covering a wide range of regulation — these include public stocktakes (appendix B) and principles-based reviews (appendix D)
- reviews that focus on a particular area of regulation — these include benchmarking (appendix F) and in-depth reviews (appendix C).

It should be noted that some kinds of benchmarking are of a more routine nature so do not fit well into these categories. But as they can be a useful tool they are included here.

Public stocktakes and 'perceptions' surveys

Public stocktakes are defined here as consultative reviews that invite businesses to provide information on the burdens imposed by regulation. This is different to regulation stocktakes undertaken internally by departments and agencies without widespread consultation. Public stocktakes are 'complaints'-based exercises, with submissions, roundtables and other approaches used to gather information from industry and other interested parties. The problems raised by business are then subject to scrutiny to see if they are significant, and to assess whether there are alternative approaches that can reduce the burden without detracting from the policy objective.

The stocktake of Australia's regulation by the Regulation Taskforce (2006) was the most recent economy-wide exercise. This followed the Small Business Deregulation Task Force (1996) a decade earlier, which was focused on small business. Several states have also undertaken stocktakes, most recently in Victoria (VCEC 2010). Stocktakes can also be done at a sectoral level. The Commission has undertaken a series of such stocktakes of Australian Government regulation (box 3.6).

Box 3.6 Examples of public stocktakes in Australia

- The **Small Business Deregulation Task Force** (1996) was led by Charlie Bell, CEO of McDonalds, and supported by a secretariat from the Australian Government Department of Industry, Trade and Commerce. It reviewed the compliance and paperwork burden imposed on small business across the economy. The report made 62 recommendations in the areas of taxation, employment, reporting burden, streamlining government processes and regulation, changing the regulatory culture, and making it easier to deal with government. In its response in March 1997, the Australian Government accepted all recommendations.
- ***Rethinking Regulation*** was the report of a specially commissioned Regulation Taskforce (2006). It was led by Gary Banks (Chair of the Productivity Commission), and supported by a secretariat drawn from across government, including secondees from the Productivity Commission. The review was required to identify reforms to reduce burdens on business from across the spectrum of Commonwealth regulation in Australia, including areas of overlap with state and territory government regulation. The Australian Government accepted 160 of the 178 recommendations.
- The **Productivity Commission** has conducted a series of sector-level stocktakes to identify specific areas of regulation that are unnecessarily burdensome, complex or redundant; or that duplicate regulations or the role of regulatory bodies. These included: Primary Sector (PC 2007c); Manufacturing and Distributive Trades (PC 2008f); Social and Economic Infrastructure Services (PC 2009c); and Business and Consumer Services (PC 2010h).
- The **Victorian Competition and Efficiency Commission** examined Victoria's regulatory framework (VCEC 2011). The final report, submitted to the Victorian Government in April 2011, included proposals to improve the operation of Victoria's regulatory management system and identified specific areas of Victoria's regulation that are unnecessarily burdensome, complex, redundant or duplicative. Five areas of regulation that should be reformed as a matter of priority were identified.
- In Western Australia, the final report of the **Red Tape Reduction Group** was released in February 2010. The report contains 107 recommendations including reforms which aim to: improve the regulatory culture, performance and accountability of government agencies; maintain an impetus and mechanisms for on-going red tape reduction by government; and address specific areas of concern raised during the consultation process. The report contains 16 specific reform chapters across a broad spectrum of government activity.

Source: Appendix B.

'Perceptions' surveys are sometimes used as part of a stocktake review, or as input into estimates of the compliance burden of red tape. They seek the views of business on the magnitude and/or trends in the burden of regulation. VCEC commissioned a perceptions survey in Victoria as part of its stocktake exercise (Wallis Consulting 2011). This elicited views from a wide range of businesses on the trends in the overall burden and on the areas of regulation that imposed the greatest burdens (box 3.7). The Business Council of Australia (BCA) conducts a regular survey of their member's views on the trends in the regulatory burden for each jurisdiction, which are complied in their *Scorecard of Redtape Reform* (BCA 2010). The Australian Industry Group is currently conducting a survey of its members that seeks to identify and measure regulatory burdens.

Principles-based reviews

Principles-based reviews are a way of identifying the need for reform for a specific, often a broad, set of legislation with certain features in common that potentially give rise to excessive regulatory burdens. The principle(s) provides an initial filter or screen to identify which regulations may warrant reform.

The most extensive example of a principles-based review is the National Competition Policy (NCP) Legislative Review Program (LRP) (box 3.8). This required all Australian, state and territory government legislation to be screened for anti-competitive effects. Some 1800 regulations found to be anti-competitive were then subject to review, with the onus on those benefiting from the regulations to demonstrate that retaining the restrictions imposed in the regulation were in the public interest. Jurisdictions were given flexibility in how the LRP reviews were conducted, with a range of in-house and consultancy options used. Incentive payments from the Commonwealth to the states and territories were also provided to encourage the completion of the reviews. The impacts of regulation on competition has since become a key principle in screening for the potential burden of new regulation.

Box 3.7 **'Perceptions' surveys**

The Victorian Competition and Efficiency Commission perceptions survey

VCEC commissioned a perceptions survey in 2011 as part of its review into Victoria's regulatory framework. The survey yielded some insights into business perceptions of Victoria's program of cutting red tape, including that:

- 56 per cent of businesses stated that they had noticed a net increase in the cost of Victorian regulations over the previous three years (3 per cent noted a net decrease)
- businesses reported that the most burdensome aspects of regulation were: complying with requirements (31 per cent); completing paper work (27 per cent); and paying a fee (18 per cent)
- 58 per cent of businesses stated that they dealt with legislation that was unnecessarily burdensome.

The New South Wales Business Chamber survey

The NSW Business Chamber conducted a survey of 373 businesses in 2011. Key findings of the survey included that:

- 46 per cent of businesses reported that preparing information was the most costly phase of compliance
- 70 per cent of businesses had noted an increase in the cost of regulation over the previous two years
- over 50 per cent of businesses nominated the following factors as having the most impact on reducing the burden of regulation: better consultation during the development of regulation; reducing the frequency of reporting requirements; and establishing a single agency to collect required information.

International surveys

Perceptions surveys have also been used overseas. Two examples are:

- Denmark's business panels process, which surveys a panel of firms about the effects of proposed reforms
- the United Kingdom (UK) National Audit Office (NAO), which conducted a series of perceptions surveys relating to the UK Government's red tape reduction program. A key finding was that only one per cent of businesses had noted a net decrease in the regulatory burden between 2008 and 2010.

Sources: Appendix G; Appendix I.

Box 3.8 National Competition Policy and the Legislative Review Program

In April 1995, the Australian Government and state and territory governments committed to the implementation of a wide-ranging National Competition Policy (NCP) — which included a legislative review program (LRP) for all jurisdictions to review their regulation in regard to the impact it had on competition.

Australia's NCP initiative stemmed from a recognition that aspects of Australia's wider competition policy framework were impeding performance across the economy and constraining the scope to create national markets for infrastructure and other services.

Overall, LRP resulted in the identification of around 1800 laws regulating areas of economic activity for review under the NCP. In aggregate, governments reviewed and, where appropriate, reformed around 85 per cent of their nominated legislation. For priority legislation, the rate of compliance was around 78 per cent (NCC 2010).

A Productivity Commission review in 2005 found that the LRP had played an important role in winding back barriers to competition and efficiency across a wide range of economic activities. It also found that most of the NCP reforms were in place and that overall NCP had yielded substantial benefits to the Australian community. The success of Australia's NCP reforms saw them hailed internationally as a successful example of nationally coordinated reform.

NCP was completed in 2005. It was succeeded by Australia's National Reform Agenda, which included a stream of work on achieving a Seamless National Economy (SNE). The competition principle remains an important part of Australian regulatory policy, and is applied as part of the assessment of new regulation in all Australian jurisdictions.

Source: Appendix E.

The approach taken to developing the COAG SNE reform stream has elements of a principles-based approach. This process has evolved over several years. In July 2006 COAG:

> … agreed to make a 'down payment' on regulatory reduction by taking action to address six specific 'hot spots', namely: rail safety regulation; occupational health and safety; national trade measurement; chemicals and plastics; development assessment arrangements; and building regulation. (COAG 2006, p. 1)

COAG also agreed to pursue further regulatory reform across several other areas (including business registration, personal property securities and product safety regulation) at the same time. The Commission, in 2006, identified a number of further areas of regulation where national 'coherence' — through mutual recognition, harmonisation, or uniform national regulation — had the potential to reduce the costs imposed on businesses that operated across jurisdictions (PC 2006c). COAG subsequently invited jurisdictions to identify additional areas

where national coherence could be improved to the benefit of business (COAG 2008b). COAG then assessed the proposals against a set of criteria, eventually determining 27 'deregulation priorities' for reform under the SNE (see chapter 6 for a discussion of these criteria).

Commonwealth commitments to international regulatory agreements can lead to changes in regulation in Australia at federal, state and territory levels of government. For many international obligations, a removal of unnecessary regulatory burdens on business is not a focus and they can involve an increase rather than a decrease in regulation. Others, such as adoption of international standards and commitments to remove barriers to trade and investment both at and behind the border, may be an impetus for regulation reform as well as helping prevent backsliding on reforms already achieved.

Benchmarking

Regulatory benchmarking is a process for comparing aspects of regulation across jurisdictions in order to highlight which jurisdictions are leading or lagging, or to identify leading regulatory practice. The aspects of regulation which can be benchmarked include: requirements and their cost to business; outcomes; and administration and enforcement.

Some types of benchmarking are regular and broadly based, whereas others are selective or targeted exercises.

Regular international benchmarking

The World Bank *Doing Business* Report is perhaps the best known of the international benchmarking exercises (World Bank 2010). It benchmarks five aspects of regulation that can impose compliance costs on business across nine areas of business activity, using a standard cost methodology (box 3.9).

The OECD also has several series that benchmark the restrictiveness of regulation in the labour market, trade and investment areas (OECD 2010g). For example, the OECD product market regulation index converts qualitative data on laws and regulations, collected in a survey of national governments, into a quantitative indicator that is consistent across time and countries. The index shows a broad decline in product market regulation over the past ten years, but notes scope for further liberalisation (Wölfl et al. 2009). Where Australia ranks on these various measures can point to areas where regulation may be lagging other developed countries, and hence areas that warrant attention.

Box 3.9 Construction of the World Bank's *Doing Business* indicators

The *Doing Business* indicators cover five aspects of regulation.

- Degree of regulation, such as the number of procedures to start a business or to register and transfer commercial property.
- Regulatory outcomes, such as the time and cost to enforce a contract, go through bankruptcy or trade across borders.
- Extent of legal protections of property, for example, the protections of investors against looting by company directors or the range of assets that can be used as collateral according to secured transactions laws.
- Tax burden on businesses.
- Various aspects of employment regulation.

The indicators cover nine regulated activities: Starting a Business; Dealing with Construction Permits; Registering Property; Getting Credit; Protecting Investors; Paying Taxes; Trading Across Borders; Enforcing Contracts; Closing a Business.

The methodology behind the *Doing Business* indicators is based on the standard cost model whereby a 'standard business' is constructed with assumptions about its size, location and the nature of its operations. The cost of meeting regulatory requirements is estimated in terms of the time taken for that business to comply.

The World Bank collects cost information from more than 8 200 local experts, including lawyers, business consultants, accountants, freight forwarders, government officials and other professionals routinely administering or advising on legal and regulatory requirements.

Source: . World Bank (2010).

Whether these prove to be priorities for reform (or even in need of reform) would require further investigation.

Specific benchmarking exercises

Australia's federal structure provides 'natural experiments' in comparative approaches to regulation. Indicators of the effectiveness and efficiency of various types of government expenditures are benchmarked annually by the Commission in the Review of Government Services reports (SCRGSP 2011). This allows jurisdictions to learn from each other about best practices, with the greater transparency of regulatory performance providing an incentive to improve. In an important extension of this approach, the Commission was asked to explore the potential to benchmark regulation, based on a proposal in the Regulation Taskforce (2006) report. The Commission concluded that benchmarking of regulation would

be difficult to do on a comprehensive basis, but that it would be possible to benchmark some aspects of regulation across jurisdictions in a way that would provide useful insights (PC 2007).

Over the past four years the Commission has undertaken a series of benchmarking studies of regulation commissioned by COAG. The first focused on quality and quantity indicators of regulation, in part to establish a baseline. The second benchmarked business registration costs for five different types of economic activity. The subsequent exercises benchmarked the collective sets of regulation on food safety, OHS, and zoning and planning (PC 2008a; PC 2008b; PC 2009b; PC 2010a; PC 2011c). The Commission is currently benchmarking local government regulation.

Benchmarking areas of specific regulations has the potential to promote regulation reform nationally. Provided regulatory objectives are broadly the same across jurisdictions, benchmarking the cost of the regulatory process by which this outcome was achieved can be a useful way of highlighting where a jurisdiction is falling behind its peers.

Benchmarking can also be used to identify alternative approaches that are more effective, efficient, or both. A 'leading practice' identified by a benchmarking exercise sets out the principles and practice that could be adopted by a jurisdiction to achieve the regulatory objective in the most cost-effective way. The Commission's series of benchmarking studies has moved toward identifying leading practice as a useful source of information for reform and does not rank jurisdictions in terms of the compliance burdens imposed for specific regulatory outcomes (box 3.10).

'In-depth' reviews

An important category of (ad hoc) reviews are those that examine a particular area of regulation in detail. Such reviews can take a comprehensive approach to examining the impact of existing regulation, need for regulation in a specific area, or on particular industries or a sector. They usually arise in response to a perceived problem or could be identified through other reviews, such as public stocktakes, as areas requiring more detailed examination.

Governments have generally commissioned in-depth reviews on an ad hoc basis as the needs arise (box 3.11).

In-depth reviews utilise a mix of approaches, but have usually included extensive consultation at key stages (particularly early on and following release of a draft report) and empirical and other analysis of the impacts of current regulations and

the alternatives. They will often establish a set of principles against which the performance of the current regulation and recommended changes are assessed. Hence they draw on aspects of the approaches discussed above, but generally to a greater depth and in a more targeted way.

Box 3.10 **Benchmarking to identify leading practice**

Commission benchmarking exercises on food safety (PC 2009b), occupational health and safety (OHS) (PC 2010a), and planning and zoning (PC 2011c) did not apply the standard cost model, but undertook a more detailed examination and comparison of the various regulatory systems. As well as comparing administrative costs to business, the Commission benchmarked regulators, regulatory processes and regulatory outcomes.

This wider and deeper approach (wider than administrative costs; deeper than costs to one representative business) was necessary in order to identify leading practices among jurisdictions. It can be difficult to draw conclusions about leading practice from synthetic benchmarking (the World Bank approach) where outcomes vary, and where the distribution of costs is not symmetric. That is, while a 'representative business' may reflect the average experience, businesses in the upper tail of the cost distribution may face considerably higher costs.

To provide options for a jurisdiction's reform agenda, leading practices must be transferable between jurisdictions. In the planning and zoning study, the Commission (PC 2011c) found that each jurisdiction has a planning system that has evolved independently, so while there were some broad commonalities, the structural differences were significant, and could lie behind the different observed outcomes, such as time limits for development assessment.

Principles are more likely to be transferrable than details as to the implementation of those principles. For example, timeliness and transparency are principles that can be applied to any system but don't need to be applied in a uniform way. Other leading practices drew on common elements of the regulatory systems so they would be generally applicable. For example, a risk-based approach to development assessment — whereby applications are streamed into different processes depending on the level of assessment required — was considered leading practice, and was already being used in all jurisdictions, but to varying degrees and with different levels of success.

Lessons from intra-country benchmarking are more likely to be transferrable than international benchmarking, even if state and territory institutions have evolved differently. For example, New South Wales has more in common with Victoria than Japan.

Source: Appendix F.

Box 3.11 **Examples of 'in-depth' reviews**

In-depth reviews have been conducted in Australia by a range of taskforces, panels, government departments and agencies. In considering regulations, or issues with a strong regulatory dimension, these have generally (though to varying degrees) shared a common approach involving: consultation; research and the search for evidence in assessing the impact of current regulations; and identification of alternatives.

Some examples of in-depth reviews conducted by taskforces include the current Victorian Taxi Industry Inquiry headed by Professor Alan Fels; the 2011 transparency review of the Therapeutic Goods Administration; the 2008-10 Australia's Future Tax System (Henry) Review; the 2009-10 (Cooper) Review of Australia's Superannuation System; the 1998 (West) and the 2008 (Bradley) reviews of higher education; the 2009 National Health and Hospitals Reform Commission; and the 2008-09 (Hawke) Review of the *Environment Protection and Biodiversity Conservation Act 1999*. Other reviews using aspects of this approach include the 2004 (Hogan) Aged Care Review; and the Wallis (1996-97) and Campbell (1979) inquiries into the Australian financial system.

Regulatory reviews and inquiries undertaken by the Productivity Commission and the VCEC also use an in-depth approach. These reviews have tended to involve long time frames and extensive opportunities for public input, including through draft reports. They have been able to examine alternatives to regulation and use a community wide approach in considering costs and benefits.

Parliamentary Committee inquiries into current or prospective regulations also share some (if not all) of the characteristics of in-depth reviews. These inquiries tend to share a strong focus on public consultation via submissions and hearings. However, Committee reviews tend to be more lightly resourced, with less capacity for detailed analysis, than those conducted by standing bodies, panels and taskforces.

Source: Appendix C.

4 Lessons from past reviews of regulation

Key points

- The various approaches to reviewing and reforming regulation have different applications.
  - Although public stocktakes have breadth rather than depth, they have proved effective in *identifying the areas in greatest need of reform*.
  - Principles-based reviews have also proven an excellent screening tool to identify key areas of regulation in need of reform.
  - Only in-depth reviews and, to a lesser extent, benchmarking exercises are designed explicitly to *develop and test reform options* within targeted areas. Embedded statutory reviews and post-implementation reviews (PIRs) should also examine options for change.
  - Most of the approaches generate information on areas of regulation that might warrant consideration for more in-depth review.
- The influence of the review approach in promoting reform depends largely on the governance arrangements and government commitment.
  - Red tape targets have received a lot of attention, and substantial savings in compliance costs are reported, but businesses are more sceptical about the real savings achieved. There is a concern that regulations will be considered to have 'been reviewed', when only a subset of costs will have been considered.
  - Stocktakes need independence and good stakeholder engagement to be influential.
  - In-depth reviews are essential for major areas of regulation or where there are complex interactions between regulations, and the recommendations have generally had a high acceptance rate — though this can depend on the timing in the short term.
  - Principles-based reviews supported by a strong commitment and incentives (as for the National Competition Policy) can be very effective in promoting reform if they have sufficient time to be done well.
- The greater the depth and broader the scope of a review the more expensive it is to undertake. Hence matching effort to the expected pay-offs is critical. It is also important to undertake each approach in the most cost-effective way.

(continued next page)

Key points **(continued)**

- The examples of the applications of the approaches yield some useful lessons:
  - Sunsetting requirements ensure that legislation is reviewed periodically, with a regulation impact statement (RIS) required to remake the legislation that impacts on business. But good planning is needed to ensure that the reviews are adequate, and packaging of related regulation for review would be more efficient and effective even if some was not due to sunset.
  - The one-in one-out rule may not be effective and regulatory budgets would be costly and complicated to implement. Both could have perverse effects.
  - Red tape targets can also be costly to administer, depending on the approach. They have had some success and play an important role in raising awareness of the burdens imposed by regulation in agencies making regulatory policy.
  - Regulatory management strategies, including feedback mechanisms and risk-based enforcement, hold promise and could be developed further.
  - Embedded statutory reviews are ideal where there are substantial uncertainties regarding the effectiveness or efficiency of the regulation. Guidelines on when a review needs to be embedded could assist in ensuring this tool is used more effectively.
  - Better information systems to inform businesses of reviews and proposed changes in regulations will promote more efficient use of sunsetting and assist in testing proposed reforms.
- Good governance, in which roles and responsibilities for reviews and following up are clearly specified and adequately resourced, is essential for all the approaches to be effective.
  - Independence is most important in ad hoc reviews, notably in-depth reviews and public stocktakes, but can also be important in embedded statutory reviews and principles-based reviews.
  - Stakeholder engagement is important in all the approaches.

Chapter 3 described a number of approaches that have been used to manage different aspects of the stock of regulation in Australian and other countries. The approaches fall into three broad groups: management approaches, programmed reviews, and ad hoc reviews. Some approaches straddle several categories, such as benchmarking, which can report on standard indicators on a regular basis or be used to investigate leading practice, and sunsetting, which could be regarded as routine if regulations were typically allowed to lapse, but often requires the regulation to be reviewed and then remade.

This chapter considers in greater detail the lessons arising from the various approaches to regulation stock management, and assesses them against four broad criteria — ability to identify areas requiring reform, identification of options for change, how influential they are, and their overall cost-effectiveness.

4.1 Different approaches target different burdens

As discussed in chapter 2, regulation 'costs' include:

- administration costs for government, some of which are passed onto business in the form of fees and charges
- paperwork and other administrative costs to business, and more substantive compliance costs such as training and investing in systems and capital in order to comply with requirements
- distortions to resource allocation, investment and innovation that result in economic costs, which are 'opportunity costs' to business in terms of lost profits, their workers in terms of lost wages, and consumers in the form of unrealised consumption opportunities
- broader 'opportunity costs' for the community arising from non-economic distortions, and opportunity costs of benefits forgone if the regulation does not achieve the intended welfare enhancing objectives.

The 'deepest' approaches to reviewing regulation examine all of these sources of cost as well as the benefits the regulation achieves. This level of analysis allows the appropriateness of the regulation to be assessed — that is, whether it is the best way to address a problem or pursue an objective and that the benefits of the regulation justify the costs it imposes. The Commission's review into the chemicals and plastics industry (PC 2008c) is an example.

Some approaches take the benefits of achieving the objectives as given and focus on assessing whether the most cost-effective way of achieving them is the regulation. This has been the case for some reviews embedded in legislation, such as for the wheat export marketing arrangements (PC 2010f).

Other stock management tools target improving the efficiency of regulation by lowering the compliance costs to business of the current regulation. The red tape reduction targets, that most Australian jurisdictions have implemented, are a good example of these more 'shallow' approaches.

The other way to categorise the approaches to stock management is to look at the breadth of industries or sectors, or the regulations, covered by the review. A review may cover all the regulation impacting on a sector, such as the Wallis and Campbell inquiry into the financial sector (Campbell 1981, Wallis et. al. 1997), or all the regulation impacting on a number of industries or sectors, as with the 2006 economy-wide stocktake review (Regulation Taskforce 2006). Alternatively, a review may cover only a specific regulation or set of regulations, such as the benchmarking exercise for occupational health and safety (OHS) regulation (PC 2010a).

Table 4.1 summarises the approaches considered by their depth and breadth of analysis.

4.2 Strengths and weaknesses of the approaches

The approaches to identifying areas for regulation reform discussed in chapter 3 have various strengths and weaknesses that provide a guide to their most appropriate application. This section briefly indicates how well the approaches perform in four areas (detailed analysis is provided in appendixes B to G):

- discovering (priority) areas for reform
- developing options for reform
- building support and momentum for implementing the reform
- cost-effectiveness.

Some potential 'pitfalls' or unintended outcomes that could arise with some approaches are raised along the way.

Table 4.1 Approaches to identifying reforms to the stock of regulation

By their depth and breadth

	Depth	*Breadth*
'In-depth' reviews	Able to examine the objectives of the regulation and apply a benefit-cost test	Usually limited to a specific industry or sector, can look at interactions among regulations and with other interventions
Embedded statutory reviews	May examine the objectives, or be limited to cost-effectiveness of approaches	Usually limited to the specific legislation in which the review is embedded
Post-implementation reviews	Should be able to examine the objectives of the regulation and apply a benefit-cost test	Usually limited to the specific legislation under review
Public stocktakes	Usually focus on compliance costs for business	Economy-wide or sectoral. Includes all regulations that impose costs, including the interaction of regulations
In-principle reviews	Depends on the principle used — generally include a public interest (benefit-cost) test	Potentially broad – screened according to relevance to the principle
Benchmarking	Varies with what is being benchmarked — regular benchmarking is usually tightly focused on a specific set of costs	Regular benchmarking is usually at an economy wide level Intra-national benchmarking varies
Red tape reduction targets	Usually limited to administrative costs to business, some include substantive compliance costs	Wide coverage of business and not-for-profit organisations. Some include government administration costs
Regulatory budgets	Limited to administrative costs to business	Uncertain — depends on the agency making new regulation
'One-in one-out' rules	Uncertain – does not explicitly consider regulatory burden	Uncertain —– depends on the agency making new regulation
Other stock-flow linkage rules (RIS requirement)	Potential to examine all regulation related to new regulation	Focus on an area of regulation
Regulator management strategies	Mainly administration costs within the regulator's administrative powers	Businesses and not-for-profit organisations in the sector or activity regulated

How well do the approaches identify areas in need of reform?

Stock management approaches

The more routine stock management approaches, such as red tape targets and regulator management strategies, aim to identify (and address) areas for ongoing incremental improvement rather than large important areas for reform. However, these ongoing improvements add up and can make a considerable difference to the overall burden of regulation.

Perhaps the approach best suited to identifying areas of unnecessary cost are regulator management strategies. The regulators are well placed to engage with their business 'clients' and to identify areas for improvement. But this requires the regulator to have both the incentives and scope to be flexible and responsive, and good governance arrangements are needed to avoid 'capture'.

One concern with these approaches is that regulations can be viewed as 'having been reviewed' although some of these approaches (or their application) do no more than consider administrative costs imposed on business.

Whether one-in one-out and regulatory budgets would assist in identifying areas for reform is likely to depend on the preparatory work done by the agency in order to meet these requirements. Hence they may be a motivating factor for agencies to look at where costs imposed on business could be lowered. But they can also introduce perverse incentives, such as to delay beneficial changes in order to meet future obligations under these rules. More flexible stock-flow rules, such as a RIS requirement to report on and consider changes to existing regulations as part of a proposal for new regulation, avoid such incentives but have lacked sufficient discipline.

Programmed reviews

Sunset clauses require the policy agency to review each regulation prior to a specified date to assess whether it is still needed and, if so, whether it needs amendment. These can be regarded as a failsafe mechanism rather than a detector of priority reforms and generally only focus on subordinate legislation. They do not contribute to identifying whether other regulations are also in need of reform, unless agencies take the opportunity to look at a package of related regulation, including primary legislation. Sunset clauses are, however, good at removing redundant regulation.

The other types of programmed reviews ensure that regulation that avoided good process post-implementations reviews (PIRs) or that faced significant uncertainties at the time they were developed (embedded statutory reviews), are subject to review. Since these are important sources of regulatory failure, they should be priorities for review and having this 'internalised' is a strength of these approaches. These reviews should identify whether changes are needed to the regulation concerned.

Regular benchmarking can identify where a jurisdiction has fallen behind its peers, which may point to areas in need of reform. For example, the Australian Services Roundtable (sub. 9) observed:

> … all of the World Bank *Ease of Doing Business* indicators where Australia falls outside the top 20 should be targets for reform: namely Dealing with Construction Permits, Registering Property, Protecting Investors, Paying Taxes, and Trading Across Borders. (pp. 2–3)

Further investigation will generally be needed, however, as such benchmarking exercises necessarily employ relatively blunt indicators. This methodology is best suited for areas of regulation where continuous improvement is possible, as it is generally a longer term exercise. Constructing indicators using a standard methodology may not be sensitive to local differences that warrant different approaches to regulation. This also suggests the need for higher level indicators that capture outcomes (such as the registration of a business), rather than comparisons of each step of the process (appendix F).

Ranking jurisdictions can create pressure for reform, but to do so the index must be credible and the ranking organisation must have some standing in the international community.

Ad hoc reviews

Public stocktakes and principles-based reviews are designed to identify areas for reform that may not be known to government.

Public stocktakes are designed as a 'discovery' mechanism for regulatory burdens. They are particularly suited to identifying areas imposing high compliance costs on business, including potentially where the accumulation of regulation has compounded the costs of doing business. They are also suited to identifying inconsistencies in regulatory requirements. The Regulation Taskforce (2006), for example, identified some 150 regulatory burdens on business across all sectors of the economy (appendix B).

Many of the areas for reform identified in a stocktake are nuisances arising from inconsistencies and overlaps in regulation. A good example is the inconsistency in environmental and OHS requirements in relation to automotive repair identified by a sector stocktake approach in New South Wales. The barrier to prevent the spread of oil spills required by the environmental regulation was banned as a safety hazard in the OHS regulation (Small Business Regulation Review Taskforce 2006).

Public stocktakes have also been effective in throwing up challenging areas requiring more detailed examination, helping identify priorities for in-depth reviews. This may include reiterating areas that continue to be raised by business as imposing considerable compliance burdens and other costs on business, such as planning and zoning and industrial relations. As a complaints-based approach, stocktakes are less well suited to identifying regulations that restrict competition, or confer advantage to incumbents, unless raised by aspiring entrants.

For stocktakes to be effective mechanisms for identifying areas for reform they need to engage widely and effectively with businesses. It is business input that makes stocktakes work well. If review fatigue sets in, because there are too many reviews or little is seen to be achieved from them, it can be difficult to elicit the necessary information. (This proved to be an issue for some of the sectoral stocktakes that followed the Regulation Taskforce exercise.)

Principles-based reviews can be very useful in identifying areas that are potentially in need of reform. The application of the principles in themselves reveals areas of regulation where costs may be excessive, distortions sizable, or where gains from greater coherence may be large. But principles-based reviews usually only apply one principle, and there may be other problems that mean the regulation imposes unnecessary costs or does not deliver a net benefit. For example, while National Competition Policy (NCP) applied the competition principle, in most jurisdictions only the regulation that failed was subject to further analysis. This is not a failing of this approach, as the principle itself can be a powerful indicator of potential reform gains but, as for other areas, it suggests that this approach needs to be supplemented by others.

One area where there may be scope to apply a principles-based approach to identify opportunities for reform is where international standards provide adequate protection for Australian consumers. As Accord (sub. 8) noted in its submission to the study, it:

> … has itself embarked on a trade-related project to map how unique Australian requirements are acting as a barrier to trade and the transfer of new technologies into Australia. Much of Australia's regulation of chemicals and plastics is unaligned with

> that of our major trading partners and these, in essence constitute a 'behind-the-border' barrier to trade. (p. 6)

In terms of other principles that could be used in the future, the current structural pressures within the Australian economy would support an approach based on detecting undue regulatory impediments to adjustment and factor mobility more generally.

In-depth reviews can confirm the need for reform in an area, and specific needs within it, particularly where 'dangerous cocktails' of regulations have emerged. However, in-depth reviews are not a primary mechanism for identifying the broad areas that need to be examined. Rather, in-depth reviews should be commissioned where the need for reform has been identified, but options need to be developed and the returns better understood.

Identifying the best reform option

A reform agenda needs to identify and prioritise areas for reform. Some of approaches discussed above are good at identifying where reform is needed, but are less informative about what should be done, while the reverse is true for others.

Management approaches

Most management approaches have a fairly clear reform option defined by the approach. They tend to be at the extremes of either removing the regulation altogether or fine tuning its administration.

The main reform option for one-in one-out is lapsing or repeal of legislation. Red tape reduction and regulatory budgets options are limited to reducing administrative compliance costs, mainly through reduced reporting requirements and by streamlining and simplifying the interactions businesses have with regulators. The regulator's capacity to fine-tune is generally limited to their administration of the regulation, although some have greater discretion to make the rules than others (box 4.1).

'One-in one-out' rules and regulatory budgets, by themselves, do nothing to identify options for reform. It is possible that agencies can take pre-emptive action to identify requirements in regulations imposing unnecessary costs. However, these rules, unless carefully designed, would not provide an incentive to act unilaterally to remove such burdens. A more flexible stock-flow linkage rule is the RIS requirement to consider other regulations when introducing new regulation. If

enforced, this provision could help in identifying better ways of achieving the regulatory objective.

Box 4.1 The scope of regulators to address burden varies

While the power of some regulators in reducing the regulatory burden is limited to changing the way they administer regulation, other regulators have power to grant exemptions from regulatory requirements. One such example is the Australian Securities and Investments Commission (ASIC), which can grant exemptions, including class orders. Example of class orders issued by ASIC relate to:

- reporting requirements for small short selling positions
- half yearly reporting requirements for start-up entities with an initial financial year of 8 months or less.

A further example of exemption powers are those granted to the Office of the Registrar of Indigenous Corporations under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006*. Under section 225 of this act, the Registrar may:

> … exempt an Aboriginal and Torres Strait Islander corporation from some or all of the provisions of this Chapter. The Registrar may do so on application or on his or her own volition. (*Corporations (Aboriginal and Torres Strait Islander) Act 2006*, section 225)

Source: Appendix G.

Programmed reviews

The scope for most programmed review mechanisms to consider options for reform is generally defined by the review requirements.

The extent to which sunsetting can identify options for reform depends on the approach taken by policy agencies wishing to retain, and hence remake, the regulation. This mechanism should enable proper reviews of any significant regulation that goes forward for approval to ensure it is the best way of achieving a relevant objective. The Australian Government's Best Practice Regulation requirements need to apply to any regulation remade due to sunsetting — a RIS where there is a significant impact on business. However, it is unclear that agencies are adequately prepared to provide this level of review where it would be needed (appendix E). In other jurisdictions, there are mixed messages about the adequacy of such reviews in seeking to assess alternatives to the existing regulation.

An embedded statutory review is restricted by the terms of reference set out in the legislation to specific areas of the regulation (although this could include examining if the regulation is needed). As discussed above, embedded statutory reviews can vary in breadth and depth, depending on the areas of uncertainty that motivated the

inclusion of the embedded review. Embedded statutory reviews work best if targeted at the areas of uncertainty in the impacts of the legislation. The need for an embedded statutory review is identified during the development of the regulation. As far as the Commission is aware this is done on an ad hoc basis by the departments drafting the legislation. Where the new regulation is introduced in response to a review, the need for a review point during or after implementation may be set out in the review recommendations.

Ideally, PIRs should meet the same requirements as a RIS. As such they need to examine the alternatives for achieving the regulatory objective and assess costs and benefits to ensure that the regulation is appropriate. However, there is some expectation that PIRs may in practice only look at implementation issues. This would provide little opportunity to make significant changes where they were called for to address unexpectedly high costs or poor efficacy.

Benchmarking that ranks countries (or jurisdictions) according to performance across a range of regulatory areas can identify a need for reform, but does not necessarily identify leading practices that are transferable across borders. Nevertheless, it does provide governments with relatively poorly performing regulation to observe and consider alternatives in use elsewhere.

Ad hoc reviews

Ad hoc review approaches targeted at specific areas of regulation are ideally suited for identifying options for reform. However, the more general ad hoc approaches tend to be fairly limited in the range of options they can identify.

Public stocktakes, although ideal for identifying areas where regulation can be removed or fine-tuned, rarely have the capacity to examine more complex problems that have been identified in the depth required to formulate options. As noted, however, they can and do identify a need for in-depth reviews in these situations. For example, the Regulation Taskforce (2006) identified 14 regulatory areas deserving further in-depth review, of which 11 have since been completed (box 4.2).

Box 4.2 **Regulation Taskforce recommendations**

Rethinking Regulation made 178 recommendations (160 related to specific regulation), of which 160 were accepted wholly or in part by government following the release of the report. 110 have now been completed, 42 are in progress and eight are not proceeding.

Priority reforms

The report's recommendations included 66 priority reforms. These were based on a judgement of the prospective gains of the reform (in terms of breadth and depth of impact), the ease of implementation, and logistical considerations — for example, the need to avoid overloading COAG or particular portfolio areas.

14 regulatory areas were indicated as priorities for review. 11 of them have since been commissioned and completed:

- Superannuation tax provisions — Super System Review Panel (2010)
- Anti-dumping regulations — Australia's Anti-dumping and Countervailing System (PC 2009d)
- Wheat export ('single desk') arrangements — Wheat Export Marketing Arrangements (PC 2010f)
- Childcare accreditation and regulation — Early Childhood Education and Care Quality Reforms (Early Childhood Development Steering Committee 2009)
- Privacy laws — ALRC (2008)
- Food regulation — PC (2009b)
- Chemicals and plastics regulation — PC (2008c)
- Consumer protection policy and administration — PC (2008d)
- National trade measurement — 2006 review commissioned by the Ministerial Council on Consumer Affairs
- Implementation of procurement policies — Department of Finance and Deregulation (2008)
- Health technology assessment — Department of Health and Ageing (2009)

Reviews yet to be concluded include:

- Energy efficiency standards for premises — the CSIRO has been tasked with the review and it is scheduled to be completed by the end of 2012
- Private health insurance regulations — no review is required following a package of important changes to private health insurance arrangements in April 2006
- Directors' liability provisions under the Corporations Act — Treasury released an issues paper in 2007.

Source: Appendix B.

Principles-based reviews inherently provide guidance on what is a valid option for reform. In the NCP, the principle was to remove anti-competitive provisions unless they could be demonstrated to be in the public interest. However, beyond the 'remove the provision' option, further assessment was required to develop what the alternatives to such anti-competitive restrictions were. The options for achieving greater national coherence are fairly clear in the broad (box 4.3), although which is the most appropriate option, and which is the best specific regulatory design within it, still needs to be assessed (as does the issue of whether the benefits of change exceed the costs).

Applying the principle of coherence in regards to international standards also provides guidance on what options might be acceptable. The Australian Services Roundtable (sub. 9) sees value in greater use of international standards, recommending:

> Greater reliance on international standards over domestically developed rules and standards which have the effect of facilitating international trade and competition, combined with a stronger effort to progress Australian interests in the development of international standards. (p. 2)

In-depth reviews are usually designed to provide recommendations on the options for reform, and often make specific recommendations on the best way forward. These reviews seek ways in which regulation can be made more efficient and effective, as well as examine whether it is appropriate. In-depth reviews generally undertake an evaluation of the current regulation as part of the analysis. A major task of a review team is to analyse the current approach and alternatives, and to identify the best option which may be to repeal or reform the regulation (see chapter 3).

Benchmarking specific areas of regulation across jurisdictions can help identify leading practice. This was done explicitly in the Commission's study for the Council of Australian Governments (COAG) on planning and zoning systems in the states and territories. Further value can be added where these exercises go the extra step of assessing the extent to which approaches in one jurisdiction are transferable to other jurisdictions.

Box 4.3 National regulatory 'coherence': approaches

The principle of *subsidiarity* holds that central authorities should perform only those tasks that cannot be performed effectively at a more immediate or local level. For issues where there is no cross-jurisdictional intersection, the issue of national coherence does not arise. But there are many regulatory areas where it does, and judgement is called for to assess the merits of a more 'coherent' approach. Ultimately, the pursuit of national 'coherence' reflects a recognition by jurisdictions that the net benefits outweigh the reduction in sovereignty. However, determining appropriate standards has many challenges — with the potential that efforts to achieve a national approach could lead to either 'lowest common denominator' outcomes or alternatively 'gold plating', where the requirements of the most stringent jurisdiction are adopted.

There are three broad approaches to implementing a nationally 'coherent' approach.

- *Mutual recognition* of requirements usually imposes few negotiating and administrative costs on regulators and stakeholders. If existing requirements are capable of meeting the objectives of regulation (for example, protection of the public or the environment), an agreement by jurisdictions to mutually recognise compliance with each other's requirements will lower the costs associated with mobility and transactions across their borders. Thus, required regulatory outcomes are maintained and some degree of jurisdictional independence is preserved. The scope for jurisdictions to modify unilaterally their requirements within a mutual recognition regime has the added benefit of promoting regulatory competition.
- *Harmonisation* of requirements means that differing requirements are aligned or made consistent. Harmonisation offers the advantage of greater certainty for stakeholders. However, when the requirements are far apart initially, the costs of negotiating alignment may be high. Of greater importance, the harmonised requirements may be more burdensome than the pre-existing ones for some stakeholders.
- *Uniformity* of requirements means that a single standard applies across all jurisdictions. Uniformity removes any doubt stakeholders may have had regarding the quality of goods or practitioners from other jurisdictions. This can help promote trade and labour mobility. As with harmonisation, however, implementing this model can involve high negotiating costs and the risk of a 'hold out' by a jurisdiction. Moreover, the uniform requirement that is adopted may not be readily achievable by all jurisdictions.

All of these approaches can lower regulatory burdens, but for some jurisdictions the burdens may rise, for example if the change means higher standards have to be met.

Source: Appendix D.

How influential are the approaches in achieving regulation reform?

Some approaches can be influential in promoting reform because the approach itself necessitates a regulatory change. Examples include red tape reduction targets or where governments are required to act on the findings of an embedded statutory review. Approaches can also be influential where they build momentum and support for reform.

Management approaches

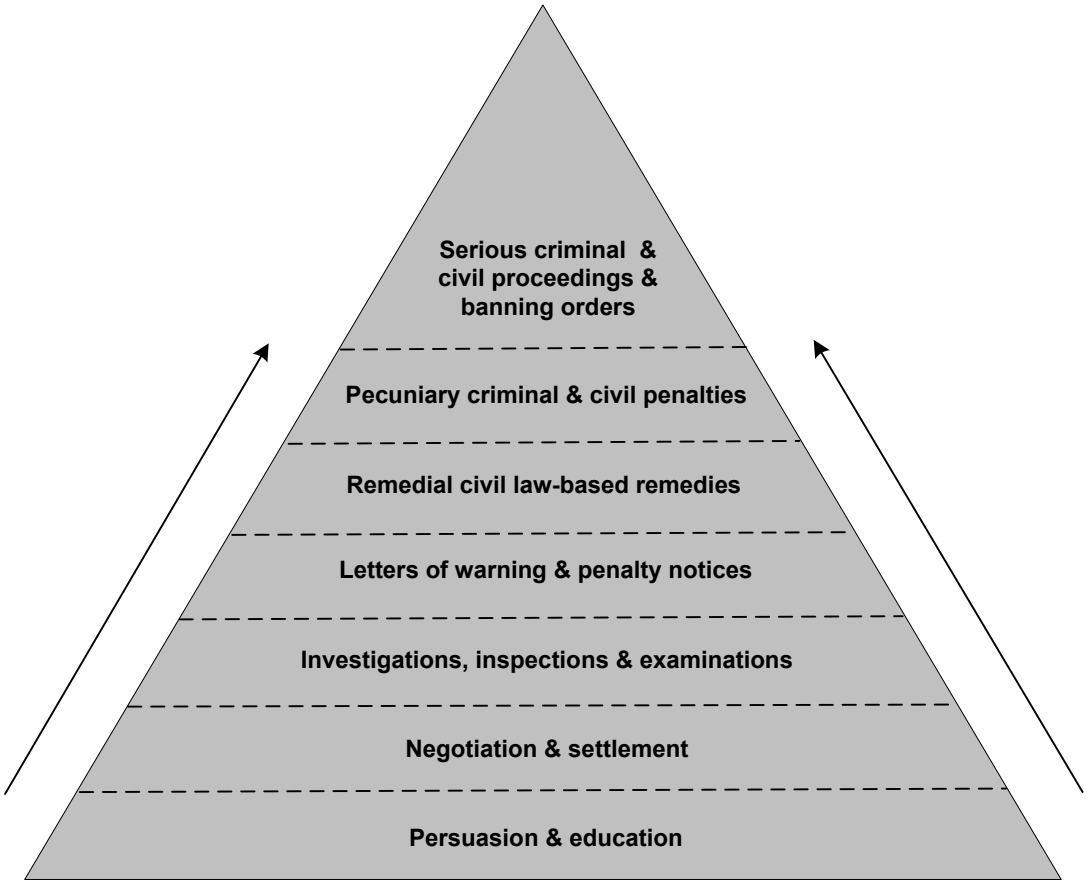
Where little attention has been paid to the stock of regulation, there can be considerable gains from basic approaches such as simplification of paperwork or reduction in reporting requirements. These are the options inherent in most *red tape reduction programs*, although some go further and address other sources of costs such as delay times, and fees and charges (often related to the administration costs of the regulator). Governments that have instituted red tape reduction programs report considerable savings in compliance costs. However, where surveys of business are available, they generally do not report noticing a significant reduction in compliance costs. The Commission understands that this is one reason for the Netherlands moving away from the approach that was 'invented' there (appendix G).

Perhaps more importantly, requiring agencies to assess compliance costs can raise awareness among regulatory agency staff of the burdens that regulation can impose. This awareness may feed back into greater attention being paid to these potential burdens in proposing, designing and administering a regulation (appendix G).

The move to less prescriptive 'risk-based' regulatory approaches can provide major savings for business without compromising the objectives of the regulation. For example, the emphasis in a 'responsive regulation' model is on a risk-based approach to administering the compliance and enforcement pyramid (figure 4.1). However, regulators may lack the scope or authority to introduce a risk-based approach without a change in legislation. The Organisation for Economic Cooperation Development (OECD 2010g) noted in its recent review:

> States are taking strong action toward relying on risk-based enforcement strategies. In all States, at least half of business regulators had risk-based enforcement strategies as of June 2007. (p. 69)

Figure 4.1 **The regulation compliance and enforcement pyramid**[a]



a Adapted from Gilligan, Bird and Ramsay (1999).

Data source: PC (2010c).

Programmed reviews

It is too early to tell how influential Commonwealth PIRs are likely to be in improving the quality of regulation, with only one undertaken to date. As noted, such reviews need to encompass the possibility of making significant changes to the regulation. However, in many areas, the reasons that led to a RIS exemption are likely to remain relevant two years after implementation.

It is also too early to tell how well the Australian Government's sunset legislation will work — both in improving the quality of regulation that government wishes to retain and in removing redundant regulation. Exemption rules and rollover time limits would need to be strictly applied. That said, it would be desirable to have some flexibility in timing where this was needed to allow groups of related regulation to be considered together. Extra time may also be called for to allow adequate reviews to be conducted where many are required in the same period. In other jurisdictions, the influence of sunsetting has been mixed. There have been a

number of ways that governments have avoided or delayed addressing problems (appendix E).

The number of embedded statutory reviews and the scope of these reviews is not recorded in any consistent way, other than being flagged in agencies' annual regulatory plans. However, where the reviews have been undertaken in a transparent manner they appear to be a highly effective mechanism for promoting changes to the regulation to make it more efficient and effective (appendix E). Well targeted embedded statutory reviews can be highly cost effective if they focus on areas of uncertainty that could impose unnecessary costs, data collection has also been embedded or is otherwise available, and they have some authority to recommend changes.

Regular broadly-based benchmarking, such as *Doing Business*, has to adopt a relatively 'synthetic' approach to measures of regulatory burden or restrictiveness. While broadly indicative of the relative performance of a country's regulatory system, for developed countries with relatively open economies the measures are generally too approximate to send a clear signal about priority reform areas. This is not the case for developing countries, where they can be a major motivating factor. Nevertheless, where reported discrepancies are substantial among comparable economies, this information can be influential in developing interest in reform in these areas (appendix F).

Ad hoc reviews

The record of general ad hoc reviews in achieving reform is mixed. Some, such as the Regulation Taskforce (2006) and NCP have had relatively high 'strike rates'. The profile of these initiatives, the commitment of quality resources, and the strong political backing they received, all appear to have contributed to their success (PC 2005b; Banks 2007b).

The Commission's sectoral stocktake program had some 'wins' in terms of removal or amendment of costly regulations in specific sectors, though fewer than had been expected. In part this may have been due either to a lack of significant residual problems after the earlier Regulation Taskforce (2006), review fatigue, or a lower profile of the studies relative to the major exercise that preceded them.

Many in-depth reviews have been influential in driving reform in Australia. The Campbell (1981) and Wallis et a1. (1997) inquiries were instrumental in changing the regulatory landscape for the financial system. The Commission has conducted many inquiries with significant regulatory dimensions, with a majority of its recommendations being accepted overall (appendix C). Most of these have had the

advantage that all related regulations could be examined and reforms considered in the wider context of the range of policies involved. For example, the Private Health Insurance Inquiry (IC 1997) recommended a change to the long-standing 'community rating' regulation that was accepted and implemented. The Commission's study on the not-for-profit sector (PC 2010e) has seen the Australian government adopt the recommendations for major changes to the Commonwealth regulation of these organisations. This followed a series of studies supporting reform including the Industry Commission's 1995 report on charities. The Commission's inquiry into executive remuneration (PC 2010g) is another example of an in-depth inquiry that resulted in adoption of the recommended reforms. The review was sparked by concerns arising from the global financial crisis.

But there are less successful examples too. A lack of progress following the Commission's inquiry into chemicals and plastics (PC 2008c) was raised in several submissions to this study. An earlier example of recommended reforms not being accepted was the Broadcasting Inquiry (PC 2000), and a recent one is the ban on parallel importation of books (PC 2009e). That said, these reports could potentially have a long shelf life (appendix C).

How cost-effective are the approaches?

Getting value for money from efforts to manage and review the stock of regulation requires that the approach be directed to where it can bring the highest returns. Effort includes not just the financial costs to government of undertaking reviews, but the costs to others who contribute, both in terms of time and financial costs. It can also include political capital that might have to be expended to commission the review and have its recommendations implemented.

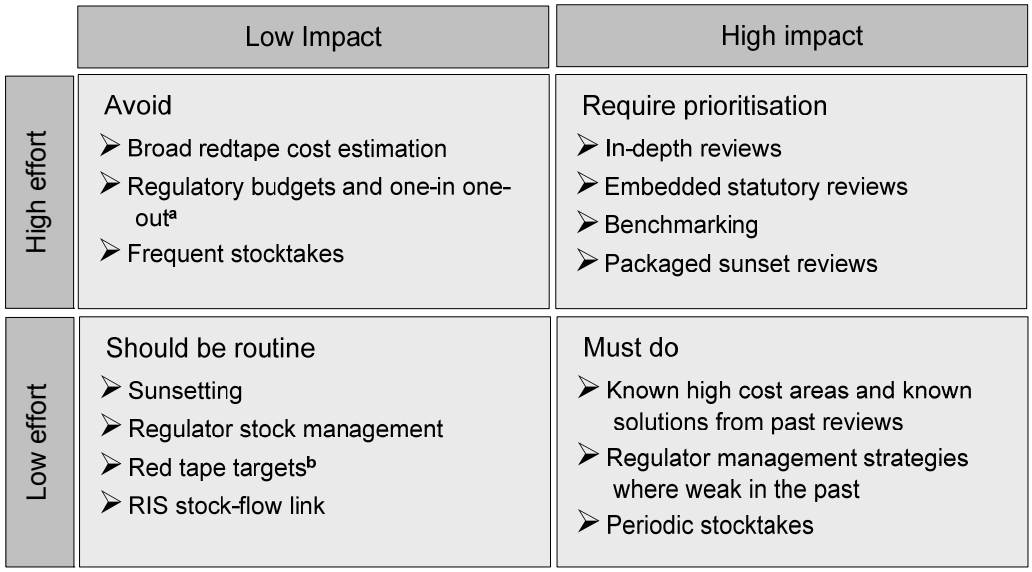
The costs of the various approaches have varied considerably even within each category. For example, the costs of running a red tape compliance cost assessment in the United Kingdom amounted to around £18 million.

Some approaches involve greater effort than others. For example, while running a sunsetting program is high effort in total, on an individual regulation level the effort is relatively low. In-depth reviews, on the other hand, are inherently high effort, requiring the prospect of a high reward.

Based on the costings and analysis of influence set out in appendices B to G, figure 4.2 gives a rough indication of how the approaches are likely to fit into an effort-return matrix. The columns are the expected return to the reform effort, while the rows are the cost of undertaking the approach.

Figure 4.2 **Approaches to managing and reviewing the stock of regulation**

An effort-impact matrix for individual areas of regulation



a These could also cover perverse impacts. **b** Where the awareness of compliance burdens is still lacking.

The *high effort-low return* quadrant should be avoided. This category could include major red tape costing exercises, stocktakes that are too close together, and risky approaches such as regulatory budgets. One-in one-out rules appear easy to implement, but would be low return at best and could have perverse outcomes. However, the more flexible stock-flow linkage rule set out in the RIS requirements, (for consideration of options to ensure regulation is not overlapping and to take the opportunity to streamline existing regulation) is relatively low cost.

In the *low effort-low return* quadrant, there are a number of routine management tasks. For regulator management strategies and red tape targets, the challenge is to undertake these as efficiently as possible given that the returns per regulation considered are relatively low (unless little has been done to limit the burden of regulation in which case these are ideal tools). The routine or 'housekeeping' element of sunsetting could be placed here where regulations are allowed to lapse after an initial screening.

Ideally most reforms in the *low effort-high return* quadrant would have been achieved. But there may be proposals 'on the shelf', where the review work has been done, but recommendations have yet to be implemented. In some such cases the political 'effort' required to implement the reform may be high. This low effort-high return quadrant may also have reforms that have yet to be fully implemented. A common opinion expressed in consultations was that finishing the current COAG agenda should take precedence over embarking on new areas of regulation reform.

There may also be low cost approaches that regulators can take which deliver much lower compliance costs and reduce distortions. In addition, stocktakes may also turn up some unexpected alternatives facilitated by changing technology, market structure and preferences.

The *high effort-high return* quadrant is where prioritisation of the review activities is most important. Embedded statutory reviews, sunset reviews for regulation that needs to be remade, in-depth reviews and specific benchmarking can all provide a thorough analysis of the costs of regulation and options for reform.

Governments will clearly continue to need a mix of tools in order to minimise regulatory burdens while achieving the benefits of regulation. A good regulatory system should apply the right tools in the right places and at the right times, as discussed in chapter 6. But any overall regulatory system will be better for all tools being applied in the most cost effective way. And the review of the uses of these tools provides a number of lessons on how their use could be improved.

4.3 Lessons in applying the approaches

There are some general lessons about what works well in regard to the stock management approaches. In addition to matching the approach to the need as discussed above, good governance is critical. Good governance arrangements include:

- the processes by which the approach is initiated
- how the review is conducted
- the processes in response to the findings.

There are five broad elements to good governance relevant to some, if not all, of the approaches to managing the stock of regulation. These are independence, transparency, consultation, coordination and oversight. These features of an approach are not costless, so the level of effort needs to be matched to the scope of the approach to discover problems and identify solutions. That is, governance arrangements need to be proportionate.

There are elements of the governance arrangements that are more specific to each approach. In addition, the examination of examples of how the various approaches have been applied and where they work well (or not) have provided a number of lessons for how these approaches can be applied in a cost-effective way. This section draws together these lessons.

Stock management tools

Red tape reduction targets

There are a number of design features of red tape reduction targets that should be considered in order to make them work more effectively. These include the scope of the target, the size of the target itself, incentives for departments, reviews, and the flexibility of the targets.

Red tape targets work best where little attention has been paid to the compliance costs that regulations impose on business, and by extension on the wider community. They are good at raising awareness in policy agencies and regulators of the paperwork related time and other costs imposed by the regulations. The target should challenge the agencies to ask whether the information required is really needed to ensure compliance, needed as often, or whether a different mechanism can be used for reporting the information (for example, moving from paperwork to electronic applications). They should also ask whether other agencies require similar information and whether a single report would suffice for all purposes. And in looking at 'must comply' provisions, the agencies should think about what would happen if the business did not comply — would it matter?

- Once red tape targets have been in place for some time, they can be expanded beyond administrative costs to include substantive compliance costs and, as the Victorian Government has done, the costs of delays. Red tape targets should include the administration costs of the regulator, particularly where those costs are passed on to business in the form of fees and charges.
  - While expanding the scope of the red tape target has the potential to improve the effectiveness of the approach in addressing regulatory burden, this brings additional costs. There is no real advantage in efforts to measure the overall burden of regulation, and such exercises are very costly if they are to be done well.
  - An incremental approach involving successive red tape reduction targets may be an effective mechanism.
- In setting targets, the central agency should take account of the relative burden imposed by each agency's regulation. In assessing this, they can draw on past stocktakes, perceptions surveys and experiences in other jurisdictions. There is no 'right' target, but a 25 per cent reduction or monetary equivalent appears to have been relatively easy for agencies to achieve.
- Quantification of savings achieved is essential to provide discipline on agencies to meet their targets. This could be in terms of the dollars of compliance costs

saved, or (as in British Columbia) a reduction in the number of 'must comply' provisions or other measure of burden. Quantification also allows businesses to scrutinise the changes to confirm the stated savings are likely to be, or have been, achieved. This requires that the savings claimed are made public in a timely way. An independent body to review the estimated cost savings of reforms achieved during red tape reduction schemes can also reduce the scope for 'gaming' by agencies, and enhance the credibility of the scheme.

- Central agencies should consider what incentives other agencies and regulators face to meet the red tape targets. Publication of the targets and the claimed savings provide some discipline. Incentive payments to agencies, particularly to reduce their own administration costs, may prove effective. These payments could be targeted to strengthening the agency's capabilities in evaluating the effects of regulation on business and the community.

Regulator management strategies

The Commission has heard that there is considerable potential for regulators to reduce the costs of compliance imposed on business. Some practices are emerging that hold promise.

- Regulators should have documented strategies for consultation with stakeholders and getting feedback on the regulations and how they administer them.
  - Consultation panels are valuable. They should have an appropriate balance of interests and skills, including a capacity to provide feedback on compliance costs.
  - Regulators need effective mechanisms to monitor complaints and to review decisions. Internal review mechanisms should be independent of the original decision maker.
  - Periodic reviews of the administrative processes of the regulator can be useful. Reviews should be arms-length from the policy agency and regulator, consult extensively, and be able to make recommendations for improvement.
- Regulators should be encouraged to be proactive in reducing burdens associated with the regulations they administer. They should have strategies to reduce the burdens within their control, and have mechanisms to provide feedback to policy agencies on aspects of the regulation that are inefficient or ineffective. The Australian National Audit Office's (ANAO) guide to administering regulation can be used to assist regulators in reducing the burden they impose.
- Regulator management tools are likely to be more effective where the regulator has the power to differentiate approaches across reported activities including

granting exemptions. Policy agencies, in designing and reviewing regulation, should ensure that regulators have some scope to address unintended compliance costs on business, consistent with the objectives of the regulation.

Ultimately the behaviour of regulators will reflect the nature of the regulation and the incentives they face in exercising any administrative discretion. The Regulation Taskforce recommended a range of actions to help re-balance incentives and encourage approaches imposing lower costs on business (appendix G). There would be value in reviewing the experience with these, the findings ANAO performance audits of regulators, and in benchmarking regulators to identify strategies and practices that work well.

Stock-flow linkage rules

The lack of adoption of one-in one-out and regulatory budgets around the world suggests that, while conceptually appealing, these approaches are quite difficult to implement as an effective stock management tool. The Commission has not identified a 'gap' that only these tools would fill. If they were to be contemplated it would be sensible to pilot their use on a small scale.

The RIS requirement that the stock of regulation be considered in introducing new regulation is less risky and a potentially more useful mechanism. However, it is not clear to what extent this mechanism has been utilised or enforced. Ideally, it should also involve an assessment of the scope to rationalise existing regulation.

Programmed reviews

Sunsetting

Most of the lessons in relation to sunsetting are about managing the sunsetting legislation in a timely and comprehensive way to avoid the need to seek deferrals, and to make better use of the sunset trigger to review the stock of regulation (appendix C).

The effectiveness of sunset clauses lies in the strength of their trigger; namely regulation will lapse if it is not remade. Strict conditions for exemptions or deferral are therefore needed.

For the Commonwealth LIA, agencies that wait until the Attorney-General tables the list of instruments due to sunset in 18 months time, will only have six months to review the sunsetting instruments before Parliament has to determine which

instruments should continue. For agencies with large numbers of instruments this may place a significant drain on available review resources.

- Agencies need to establish a clear and transparent process to manage the flow of sunsetting legislation. This requires effective planning and early engagement with affected parties, including through the publication of a forward program of sunsetting regulations and associated reviews.
- To ensure a proportionate response, and avoid excessive strain on the available resources of the policy agencies, effective filtering or 'triage' processes are essential. They should identify which regulations are likely to impose high costs or have unintended consequences that warrant a more in-depth review.
- Packaging regulation for review, that is overlapping or addressing similar issues, can be cost-effective and should be done even if it means bringing forward the review of some legislation due to sunset later (and vice versa). Agencies should also be encouraged to take this opportunity to review related primary legislation. While limits on the deferral of sunsetting are important and need to be enforced, some flexibility could be provided for legislation that is scheduled for review with a package of related regulation.
- Action to 'triage' and then schedule the necessary reviews should be taken sooner rather than later. Business can play an important role in checking whether the proposed level of review is appropriate for the regulations that affect them. Hence business should be provided with the opportunity to comment and mechanisms installed to achieve this.

'Embedded' statutory reviews

Embedding reviews into legislation has proven an effective approach where there has been uncertainty surrounding its impacts — particularly where new regulations could have significant impacts on business or the economy. There may also be uncertainty about how effective the regulations may be in meeting policy objectives.

- Embedded statutory reviews should have the scope to address areas of significant uncertainty in the regulation, including whether it will remain appropriate in the light of any changes in the economy. In planning for the review, consideration should be given to other reviews that may be scheduled in a complementary way.
- For such embedded reviews to work well, they require an appropriate level of independence and transparency. While it may be suitable for the policy agency to conduct the review, whether this is likely to be adequate should be considered at the legislation drafting stage.

- Regulators need to build in data collection as part of the operation of the regulation. While costs will vary depending on the data requirements, it could be expected that the costs of data collection will be much lower if they are collected as part of the day-to-day operation of the regulator rather than after a period of time (such as by an external reviewer).

It is a requirement of the Commonwealth Government's 'best practice regulation requirements' that a RIS outline how a regulation will be reviewed. The *Best Practice Regulation Handbook* (Australian Government 2010b) states that a RIS (should) set out when the review is to be carried out and information on how the review will be conducted, including if special data is required to be collected. However, the handbook does not specify what type of review will be required, such as when an embedded review should be included in legislation. Nor does it provide guidance on the appropriate scope, independence or transparency of reviews for regulations with a significant impact on business.

There is a good case for having a stronger RIS requirement for ex post review, particularly where there remains significant uncertainty about likely impacts. Requiring that all regulation that requires a RIS either to have an embedded statutory review, or be reviewed within five years, would remove the need for the current five yearly 'default reviews'. In the cases where there are not specific aspects of the regulation that need special attention, the embedded review requirement could be satisfied by earlier review of the regulation as part of a package.

Post implementation reviews

PIRs are most effective when they not only serve as a 'fail safe' mechanism, but also act as a deterrent to avoidance of adequate regulatory impact analysis at the decision-making stage.

The Office of Best Practice Regulation (OBPR) provides a publicly accessible list of Commonwealth level PIRs that it determines are required in the future. Since 2009 the OBPR has advised that around 40 PIRs have been required for regulatory proposals either due to a Prime Minister's exemption or due to non-compliance with best practice regulation requirements. It had been anticipated that there would be few 'exceptions'. However, the numbers have been rising and include important areas of regulation with significant potential impacts (box 4.5)

- PIRs should require the same rigour as the RIS process and need to examine the net benefits as well as the alternatives. Consideration should be given to

requiring PIRs to be undertaken at arms-length from the policy agency to enhance the credibility of the process.

- To utilise the capacity to observe the actual impacts following implementation, provision needs to be made for data generation (as for embedded statutory reviews).

The Commission understands that, contrary to the original conception, some departments are anticipating that PIRs would only address relatively limited implementation matters. If this mechanism were to be used as a means of evading the RIS process, it would pose a considerable risk to the integrity of the Government's best practice requirements.

Box 4.4 Some regulations requiring PIRs

The OBPR has advised that exemptions from the Government's RIS requirements, triggering a need for post-implement reviews, have been granted for some 40 regulatory initiatives across a range of areas. They include:

- changes to the arrangements for executive termination payments (2009)
- carbon pollution reduction scheme legislation (2009)
- industrial relations legislation (including the *Workplace Relations Amendment (Transition to Forward with Fairness) Act 2008* and the *Fair Work Act 2009)* (2010)
- pharmacy location rules (2010)
- live cattle exports to Indonesia (2011)
- responses to the Australia's Future Tax System (Henry) Review, including the minerals resource rent tax and the targeting of not-for-profit tax concessions (2011).

Source: OBPR Best Practice Regulation Report 2009-10. Further examples are provided in appendix E.

Ad hoc reviews of specific areas of regulation

Benchmarking exercises

Benchmarking has proven a useful tool in our federal system. It reveals where Australian jurisdictions do things differently, and can identify, and develop a better understanding of, leading regulatory practice where this is unclear or unknown.

- In the COAG context, benchmarking should test whether there is potential gain from greater inter-jurisdictional harmonisation. Where possible, benchmarking should provide a guide to the terminology used in different jurisdictions to assist stakeholders who have to navigate more than one system.

- Benchmarking should seek to provide quantified indicators of relative performance where possible. In providing such estimates, guidance should also be given on the range of experiences of businesses. This is particularly important where 'synthetic' and 'case study' approaches are used for benchmarking. Where quantifiable indicators are likely to be misleading or very expensive to construct, comparative descriptions should be framed to encourage governments to ask "why is it so?".
- Benchmarking should not be limited to comparisons of regulatory provisions. Where possible, analysis of differences in the administration and enforcement of regulation (the behaviour of regulators) should be benchmarked. Standards benchmarking, which compares actual practice against agreed best practice, is particularly useful when benchmarking administration and enforcement. The analysis should extent to the examination of whether this behaviour is related to the content of the regulation, or a result of the history of the regulator.
- Where possible, benchmarking exercises should identify leading practice. The analysis should include an assessment of the transferability of the practice across jurisdictions.
- When benchmarking cost, common outcomes from the regulation should not be taken as given, but tested to see if this is the cases. Where the outcomes achieved are not common across jurisdictions, outcomes should be included in the benchmarking exercise. This rule should also be applied where processes are benchmarked.
- While benchmarking has to be an arms-length exercise to be credible, the Commission's exercises for COAG have benefitted greatly from having an Advisory Panel comprising relevant senior officials from each participating government. Such a panel can help mediate relations between the reviewer and the regulators, and provide a good testing ground to ensure that the information gathered accurately reflects the situation in the various jurisdictions. The involvement of each jurisdiction in the process can also encourage governments to address the "why is it so?" question and help generate momentum for reform.
- Surveys can play an invaluable role in ensuring the collection of information and impressions on a consistent basis. As they can be expensive to undertake, including in terms of the time burden placed on respondents, consideration should be given to improving the consistency of data collection by regulators to enhance the potential use of these data sets for benchmarking purposes.

When identifying priorities for regulation benchmarking studies, consideration should be given to:

- the potential for greater national coherence to add value without significant downsides from loss of state experimentation
- whether jurisdictions do things sufficiently differently that lessons on leading practices are likely to emerge
- whether there is scope for reform, but lack of agreement as to which systems lead to the best results.

In-depth reviews

To work well, and be influential and credible, in-depth reviews of key regulatory areas should be based on extensive consultation, use transparent processes and be independent. Given their often significant cost, they need to be undertaken into areas where the payoff from carefully developed reform is likely to be high.

- The public release of issues papers, submissions, and perhaps most importantly draft reports, allows stakeholders to engage with the review process. This is particularly useful in testing and 'reality checking' recommended reforms.
- It is important that those heading such reviews are able to exercise independent judgment, and have a secretariat reporting directly to them comprising experienced analysts.

Ad hoc broadly-based reviews

Principles-based reviews

Reviews motivated by attainment of key reform principles, such as competition and coherence, have been influential in Australia.

Reviews based on the 'no undue restrictions on competition' principle have worked well, with the NCP reforms seen by the OECD as a potential model for other countries.

- The breadth of coverage of competition policy reviews across all jurisdictions meant that prioritisation was essential. Even so, the period for completion of all reviews had to be extended from five to ten years. Political leadership played a key role, as did financial incentives for jurisdictions to follow through with agreed reforms.

- The principle of competition has been embedded in the RIS process in all jurisdictions since the completion of the NCP reviews. However, there may be some regulation that avoided adequate scrutiny. Hence continued application of the competition principle in all reviews of regulation should be encouraged.
- It was envisaged in the NCP program that reviews would be repeated after ten years. While the blanket application of this is unlikely to be warranted, given the costs involved and the significant number of reforms that have taken place, follow-up reviews could usefully be conducted for those anti-competitive regulations that remained in place, primarily those with potentially significant economic impacts. Major areas of regulation that failed the principle, but were not adequately tested in reviews during NCP (or since), should be subject to in-depth review.

Australia has had some success in promoting greater national coherence in regulation across states and territories. Progress has been slower than envisaged due to complexity, the involvement of many different regulators and stakeholder groups, and resource constraints in dealing with many different regulatory areas simultaneously.

- It is important that the current Seamless National Economy reform agenda be substantially completed and implemented before embarking on further reforms.
- The criteria established for assessing priorities are broadly appropriate, though there is scope to extend them (see box 4.6). However, the experience thus far suggests that more attention should be devoted to sequencing the resulting agenda, to account for capacity constraints in evaluating and advancing specific reforms.

There is further scope to apply the competition and coherence principles to regulatory reform. As noted, certain competition regulations that withstood the NCP review process could be revisited. And the 'coherence' agenda remains active. In considering additional 'principles' to apply in advancing reform, the structural pressures facing the Australian economy suggest that a focus on regulatory impediments to adjustment, particularly mobility of labour, could be productive.

Box 4.5 Factors to weigh up in assessing potential reforms to promote a national approach

Where the promotion of a national approach appears prima facie to be a desirable policy objective, relative to differential reforms at the state level, the benefits need to be weighed up against the costs.

Questions to consider in weighing up possible benefits of reform options include:

- Will the reform lead to reductions in transaction/compliance costs for business operating across multiple jurisdictions?
- What is the potential for the reform to open and integrate economies, enhancing trade and investment and economic welfare?
- Will it lead to the elimination of negative externalities in other jurisdictions (for example intellectual property)?
- Are there economies of scale in regulation which can be achieved (where these exist, or alternatively, a reduction in regulatory duplication which can reduce real resource costs of policy making)?

Questions to consider in weighing up possible costs of reform options include:

- Will it lead to inefficiencies by imposing (harmonised) laws that are inappropriate for the unique conditions of a particular jurisdiction's economy? (In other words, is the reform likely to lead to harmonised but inefficient laws?)
- Is there a likelihood of a loss of regulatory competition between jurisdictions?
- What are the likely resource costs for government, such as reviewing existing regulations and negotiating agreement on a more coherent regulatory framework?
- What are the likely transition costs for market participants — such as costs incurred in changing internal processes and documentation to comply with new laws?
- Is there likely to be a loss of domestic policy flexibility (where jurisdictions cannot respond as quickly to changing market circumstances? (Though this may also bring benefits if it limits growth in poor quality regulation.)
- Is there likely to be dilution of jurisdictional policy participation?

Source: Appendix D.

Public stocktakes

Like other reviews, the value of regulatory stocktakes depends on their governance arrangements, consultative and other processes and their resourcing. Stocktakes are especially reliant on business for information on regulatory burdens which they are best placed to provide. Their cooperation is vital.

- An independent panel which includes business representation helps inspire confidence in the process, increasing business participation.

- Getting business to engage requires effective strategies. Political support for the stocktake helps by improving perceptions about the likelihood of action.
- The supporting secretariat requires evaluation skills and subject knowledge that may not be available in a generalist review team. Seconding staff from relevant agencies for the support team therefore has advantages, though it is desirable to forge an independent 'culture'.
- Effective screening of complaints is needed. Both complaints and reform options should be tested with policy departments and regulators. Draft recommendations for reform and further review should be subject to public scrutiny.
- To avoid 'review fatigue' stocktakes should be infrequent, and not occur until the recommendations of previous stocktakes have been advanced. Ten yearly intervals for a general stocktake looks about right (the period between the Bell (Small Business Deregulation Taskforce 1996) and Regulation Taskforce (2006) stocktake exercises). For industries that are experiencing rapid change, or where there are a large number of new regulations, more targeted reviews in the intervals between the wider stocktakes could be undertaken.
- As stocktakes are well suited to identifying areas of regulation or sectors that warrant additional in-depth review, they should be required to indicate priorities in this respect (as in the Regulation Taskforce (2006)).

The level of sophistication of the evaluation used in reviews, particularly the extent to which quantification is feasible and useful, has not been detailed in this chapter. The next chapter looks at the range of evaluation methods and how they are best used.

5 Evaluation methods

Key points

- The evaluation methods used to review the performance of existing regulations can also be used in most cases to evaluate the regulatory reform process.
- Most evaluation methods collect evidence to assess the causal links between the regulatory (or policy) changes and the target outcomes:
  - These include performance measurement, impact assessment and cost-benefit analysis.
  - Process audits assess the achievement of the processes set out in the reform program.
- While many countries have adopted regulatory impact assessments (which require ex ante evaluation of proposed regulatory changes), few countries have undertaken ex post evaluations of reforms. Rather, evaluation is generally undertaken as part of an in-depth or other review of regulation.
  - This is changing with a number of countries introducing programs of ex post evaluation of new regulation.
  - The Council of Australian Governments has established a system of process reviews and asked the Productivity Commission to undertake an assessment of the 'impacts and benefits' of regulatory reforms in the 'Seamless National Economy' stream. Sunsetting provisions for subordinate legislation should also see more systemic evaluation efforts.
- Ex post evaluations should:
  - report on change relative to a counterfactual — what would have happened in the absence of the reform
  - be proportionate — the effort to undertake the evaluation reflecting the expected value of the information generated by the evaluation
  - be explicit about what is being evaluated, note significant gaps that are not covered by the evaluation, and be clear about the underlying assumptions
  - apply a 'benefit-cost' or 'results-based' framework, even if the evidence on impacts is qualitative rather than quantitative, and a formal cost-benefit analysis is not possible.

(continued next page)

Key points **(continued)**

- Quantification of the impacts of regulation reform brings additional rigour to ex post evaluation, and can provide better insights about net outcomes. However, not all outcomes may be able to be quantified, or may only be quantified in units that are not easy to compare.
- Quantitative approaches ideally involve: specification of the counterfactual; empirical evidence to test the assumed relationships between reforms and desired outcomes; identification of distributional effects; and assessment of the net gain or loss from the reform.
- Different quantitative evaluation methods (for example, standard cost models, partial equilibrium models, computable general equilibrium models and econometric analyses) are designed to estimate different types of reform outcomes (such as time costs for business, compliance costs, behavioural responses, cost savings and economy-wide flow-on effects).

Chapters 3 and 4 described a number of approaches to reviewing and reforming the stock of regulation. To use these approaches, it is necessary to evaluate the effects of regulations and reforms. There are a number of approaches and tools that can be used. At the most basic level, process audits seek to assess whether the reform has been implemented. Performance measurement usually seeks to establish whether the reform has met its objectives (is 'effective'). It may also assess whether the approach is undertaken at least cost (is 'efficient'). At the broadest level, impact assessment seeks to report on the full range of outcomes of a reform, including unintended impacts. Cost-benefit analysis seeks to quantify and add up all the costs and benefits to answer the question of whether, once all the impacts are taken into account, the reform added to or detracted from community wellbeing (is 'appropriate'). With the exception of process audits, all these approaches sit within a broad benefit-cost (summative) evaluation framework.

The methods that are potentially relevant to evaluating *reforms* are essentially the same methods that can be used to evaluate regulations generally, or indeed to evaluate regulatory *proposals*. Most of the review approaches discussed in the preceding chapters could make use of such methods. In practice, there appears to have been more reliance on qualitative than quantitative methods.

Section 5.1 notes the role of evaluation in the regulatory system. Drawing mainly on appendix H, section 5.2 describes the methods and approaches that have been applied to undertaking evaluations of regulation reforms. Section 5.3, which summarises appendix I, focuses on quantitative methods of evaluation, and determining the most suitable approach given the nature of the reforms being evaluated.

5.1 The role of evaluation

Evaluation of regulation and reforms can be undertaken before a regulation or reform has been implemented (ex ante evaluation), or after it is in place (ex post evaluation). The key difference is that ex ante evaluation is based on an estimate of the potential effects of a reform (taking into account the probability of the reform being implemented as intended), whereas ex post evaluations are based on observed impacts.

While there is a strong rationale for applying the results from previous ex post evaluations and for undertaking evaluations throughout the regulatory cycle (chapter 6), this does not mean that evaluations should always happen (nor that they are necessarily useful when they do). Evaluations are not costless, results can be difficult to interpret, and if not undertaken well can be misleading. Ensuring the right type of evaluation is applied consistently and at the right time is crucial.

Internationally, evaluations of regulations are not undertaken on a systematic basis, and rarely occur for regulatory reforms as such. (Systematic evaluation of expenditure programs is more common, but still not widespread.) Moreover, where evaluations have been undertaken, many have not been very influential. However, there is some evidence that governments are moving to strengthen the role of evaluation in the regulatory systems (box 5.1).

In Australia, ex post evaluations of regulations and reforms have tended to be undertaken on an ad hoc basis as part of the more in-depth reviews, rather than as an automatic part of the regulatory cycle. A key exception is National Competition Policy (NCP), where the Commission was asked to evaluate the impacts of the reforms.

There has been a move toward more systematic evaluations of expenditure programs in the Australian Government. Ex post reviews of regulation are a natural complement to this. The Council of Australian Governments (COAG) reform agenda includes systematic performance measurement and impact assessment, including a review of the impacts of the Seamless National Economy regulation reforms (PC 2010b). The introduction of sunsetting should see the scope of evaluations widened. In states with red tape reduction targets, efforts have been made to evaluate the reduction in compliance costs that have been achieved (chapter 3).

Box 5.1 **International experience of ex post evaluation**

An Organisation for Economic Cooperation and Development (OECD 2010f) review of regulatory systems in a number of countries concluded:

> Ex post evaluation — whether of individual regulations, regulatory processes, or regulatory frameworks — is a near universal weakness. No country is strong in all aspects of regulatory management across the cycle. (p. 50)

United States

Greenstone (2009) suggested that ex post evaluation of regulations is seldom undertaken in the United States. Hahn and Tetlock (2007) found 'little evidence' that evaluations of regulatory decisions over a number of decades had had a 'substantial positive impact'. However, in 2011, the Obama administration made Executive Orders requiring federal and independent regulatory agencies to undertake retrospective reviews of existing regulations. (Obama 2011a, b)

United Kingdom

The United Kingdom National Audit Office (NAO 2010b) stated:

> In 2007 we reported that there continued to be an unstructured and ad hoc approach to post implementation review across all departments. Since then, we have found greater numbers of Impact Assessments include a statement of when a review should be conducted, although relatively few have been carried out to date. (p. 9)

In addition, sunset clauses and the 'one-in, one-out' rule appear to have provided incentives for evaluations.

European Union

Although there are requirements that regulations be subject to interim and/or ex post evaluations, the scope of the evaluations has been described as limited to 'outputs and internal efficiency, and not results' (Rambøll Management/Euréval/Matrix 2009, vol I, p. vi.). Furthermore, evaluations 'are less influential in the setting of political priorities or choosing between different options *per se*.' (EC 2005b, p. ii), and are used more for fine-tuning. However, the European Commission has 'started to systematically evaluate existing legislation ex post, indicating that all major existing policy instruments, whether expenditure programmes or regulatory measures should be evaluated on a regular basis'. (EU 2010, p. 124)

Source: Appendix J.

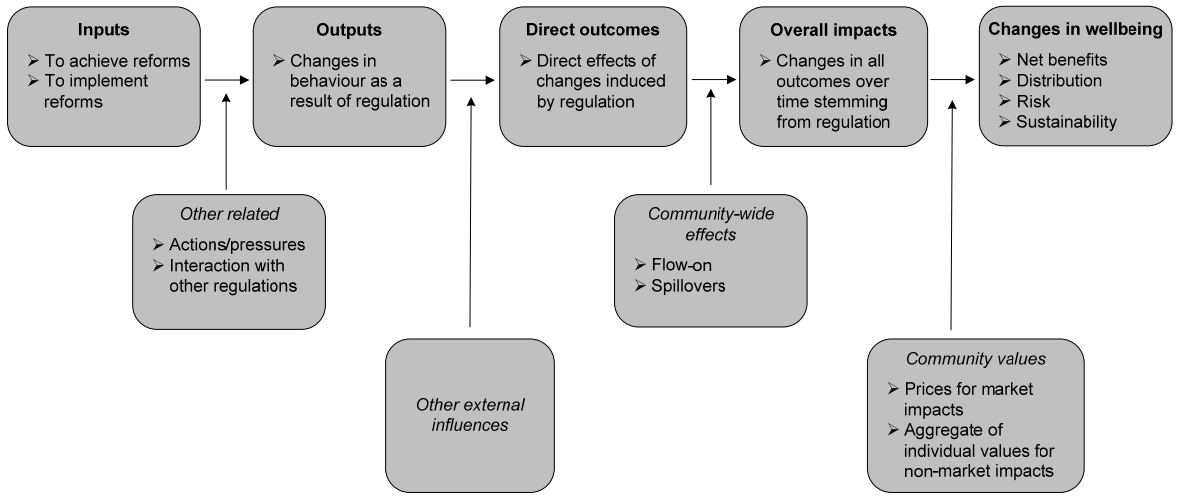
5.2 Ex post evaluation methods

Evaluations can cover some or all of a range of impacts

Most evaluation methods seek to test the causal relationships between the changes induced by a regulation and the outcomes that the regulation aimed to achieve. To

do this, they seek evidence on the changes in inputs, outputs, outcomes, impacts and overall community wellbeing that result from, or are part of, the reform (box 5.2). Figure 5.1 sets out a framework based on these relationships. The evaluation task usually becomes increasingly complex as the assessment moves from the input-output end of the spectrum to the net effects on community wellbeing. This is in part because external factors play an increasingly larger role along this assessment spectrum, and because the relationships become more complex.

Figure 5.1 **The broad evaluation framework**



If the impacts have not happened as expected it is usually for one of three reasons:

- the reform was not fully implemented as designed
- the reform may have been based on a false premise – the theoretical relationships on which the reform was based was not applicable for the objectives of the reform
- changes in the external environment could have occurred that undermined the effectiveness of the reform. That is, the assumptions about the external environment were not fulfilled.

Box 5.2 **The effects of regulations and reforms: some definitions**

Inputs — the effort required to develop, design and implement the reform, as well as the effort required to enforce and fine tune regulations.

Outputs — a direct consequence of inputs to a reform that can have several levels, including:

1. the legislation (or its removal), and the systems and processes put in place to administer the regulation — direct consequences of the inputs
2. the change in behaviour of businesses or others in response to the new regulation.

Direct outcomes — the direct consequences of the changes in the behaviour of businesses or other directly affected entities. They include adjustment costs, changes in compliance costs, prices, production processes allowed, and market access for businesses and regulators that are directly affected. These outcomes are usually intended effects, but can include unintended direct outcomes. While they depend on the outputs, these outcomes also can vary with the external environment.

Overall impacts — the full set of changes, including 'community-wide' effects, once the flow-on and spillover effects are taken into account. Flow-on effects arise as resources are reallocated through the economy in response to changes in demand and supply, and as reforms affect investment decisions and innovation. Spillover effects include any other type of change (intended or otherwise) that results from the direct outcomes.

Changes in wellbeing represent the final cumulative effect of the reform on the community's wellbeing. If all the impacts are economic in nature, they can be expressed in dollar terms and 'added-up' to estimate the net benefit, providing a single measure of the change in wellbeing resulting from the reform. But if some impacts are changes in the natural environment, or in social outcomes, it is more difficult to assign monetary values to these impacts (appendix I). Hence many evaluations do not take this extra step of assigning relative values to move from impact analysis to cost-benefit analysis.

Evaluations can be quantitative or qualitative

Both quantitative and qualitative approaches can be applied to testing the underlying theoretical relationships on which a reform is based, and for reporting on the outputs, outcomes and impacts of regulations and reforms. Most in-depth reviews use both quantitative and qualitative evidence.

Quantitative methods

There are three broad types of quantitative evaluation — performance measurement, impact assessment and cost-benefit analysis.

The least complex approach is *performance measurement*, where the results of a reform are measured relative to a target. Performance measurement approaches only report on the outcomes being sought by the government. They rarely report on unintended outcomes. Performance measures also tend to focus on direct outcomes, where there is a clear line of causality running from the policy change to the outcome. The choice of indicator is critical in determining how useful performance measurement is in assessing whether the reform objectives are being achieved. Performance measures should be independently verifiable, meaningful and understandable. They also need to be timely and cost-effective (TBCS 2009b).

An important example of performance measurement is the monitoring and evaluation of the COAG reform agenda by the COAG Reform Council (CRC) (box 5.3). The CRC monitors, assesses and publicly reports on the performance of the Australian, state and territory governments in achieving the outcomes and performance benchmarks specified in the six National Agreements. In addition, for the six National Partnerships with reward payments, the CRC provides COAG with an independent assessment of whether predetermined performance benchmarks have been achieved prior to reward payments being made.

The COAG reporting exercise has demonstrated the use of qualitative as well as quantitative application of performance measurement. The CRC's reporting for the Seamless National Economy reform agenda, for example, is limited to process indicators. It tracks progress in achieving the intended reforms rather than the impacts of the reforms.

Impact assessment approaches seek to identify the full range of impacts, although often only some types of impacts are amenable to quantitative analysis. Impact assessment can include evaluation of the distributional effects of regulations and reforms. The Commission's analysis of the impacts of NCP is one example. The Commission evaluated the change in economic activity once the full effects of the NCP reforms had worked through the economy. It also estimated the distribution of the change in household income and regional economic activity (PC 2005b). The current study on impacts and benefits of the COAG reform agenda will use an impact assessment approach (PC 2010b).

Box 5.3 **Performance indicators for the COAG reform agenda**

The CRC monitors and reports on milestones for progress of governments for the COAG reform agenda. Each National Partnership is underpinned by an implementation plan which articulates the outcomes sought in each reform area and, where possible, identifies key milestones for jurisdictions. The CRC's assessment of performance is evidence-based and draws on a range of inputs, including:

- detailed progress reports and formal comments provided by jurisdictions
- additional information from jurisdictions requested to assist the assessment process (such information is treated as an addendum to jurisdictional progress reports)
- independent research on legislative and regulatory activities of governments, based on publicly available information.

Results are reported in summary form, using a 'traffic light' representation of progress against milestones. Where a reform stream has more than one milestone and the CRC's findings result in different ratings being applied to the individual milestones, the overall summary rating is determined by giving greater weight to milestones requiring more substantive reform action. Where this is the case, the basis for its weighting of the milestones is provided.

Source: CRC (2010).

Cost-benefit analysis (CBA) is the most demanding of the quantitative evaluation methods, and for that reason is less commonly undertaken in full. It requires estimation of the flow of both costs and benefits over time that result from a reform. This involves identifying the impacts that arise over time, and converting them into a common metric (generally dollars) that is discounted to express the 'net present value' of effects over time.

CBA is most commonly applied for major expenditure programs, where both the benefits and costs are expressed in monetary terms. CBA is usually applied ex ante, to identify the best option where the flows of benefits and costs vary across options. CBA also enables comparisons, based on discounting, where the impacts occur over various periods. The choice of discount rate can be critical for long periods, such as estimating the impact of climate change policy (Stern 2006; Baker et al. 2008; Harrison 2010). CBA can be applied where reforms have non-market effects, but have to use methods such as contingent valuation and choice modelling to put monetary values on these non-market outcomes (appendix I).

The results of the different types of evaluations can be presented using various summary measures, depending on which effects are being evaluated (box 5.4).

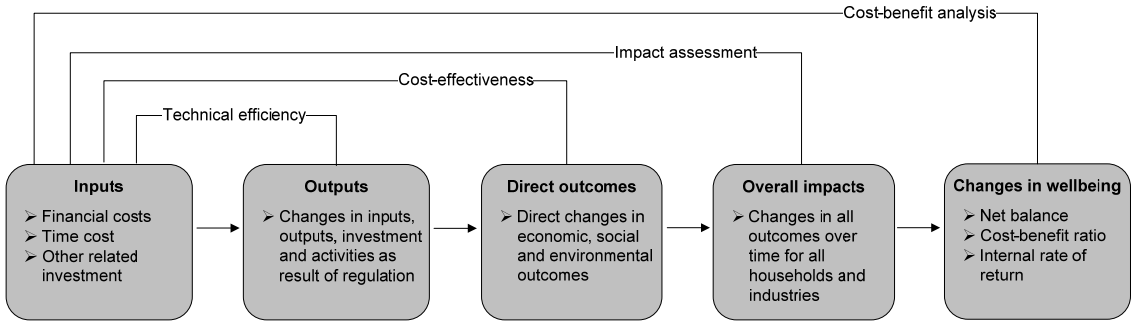
Box 5.4 **Summary measures of the effects of reforms**

The effects of reforms can be presented using a variety of summary measures:

- technical efficiency — which measures the relationship between inputs and outputs
- cost-effectiveness — which measures the relationship between inputs and outcomes (usually only intended outcomes)
- impact assessment — which lists the full set of outcomes, intended and unintended, including the input costs to identify the 'net balance'
- cost-benefit analysis — which expresses all impacts in a common metric and time period to be able to 'add-up' the impacts to estimate the net benefit, or to express the benefits as a ratio of the costs of undertaking the reform.

The figure below applies these measures to the framework set out in figure 5.1.

Some evaluation summary measures



Qualitative methods

Qualitative evidence typically comes from consultations where respondents provide 'narratives' about their experiences. For example, in submissions to this study, a number of narratives are provided about the burdens of specific regulation. The Commission's inquiry process is designed to harness narrative evidence, through consultations, submissions, roundtables and public hearings.

'Perceptions' surveys can also be used to capture the assessment of business about the changes that result from a reform. For example, the Business Council of Australia (BCA) conducts a regular survey of its members on their perceptions of the level of red tape. The scope for such information to be used to assess the impact of a reform depends on the alignment of the reform with the impacts of regulation that are reported in the survey.

Evaluation that focuses on processes is inherently qualitative in nature, even if assessments of process are reduced to numerical indicators. Process audits (formative evaluations) are commonly undertaken for both regulation and expenditure programs during their implementation. These are often conducted internally by agencies, but can also be external audits. In the Australian Government case the Australian National Audit Office (ANAO) undertake process audits and performance audits. Performance audits expand the scope of process audits to consider the achievement of the policy or program objectives or intent as well as the achievement of process. The CRC reporting of the Seamless National Economy (SNE) is effectively a process audit.

Essential features of robust evaluation

Regardless of the method of ex post evaluation chosen and whether it is qualitative or quantitative, there are some features that lead to more robust evaluation. Two that are particularly important are evaluation against a 'counterfactual' and 'sensitivity analysis'. These are described below. (More detail is provided in appendixes H and I.)

Change should be reported against the 'counterfactual'

Whether quantitative or qualitative approaches to evaluation are used, the evidence should be presented in terms of the change relative to what otherwise would have happened in the absence of the reform. This is known as the 'counterfactual'. Defining a counterfactual is challenging, but failure to report changes against it can lead to the net impact of the reform being under- or over-stated.

There are several ways to define a counterfactual, including:

- 'natural experiments' where some jurisdictions implement a reform and others do not
- before and after evidence — this can be qualitative or quantitative, and involves looking for the change in the outcomes of interest before and after the reform
- deviation from historical trend — where the baseline is projected based on historical trends (before and after effectively assumes a no change trend)
- deviation from baseline — where the baseline is adjusted for changes in other variables that also influence the outcomes of interest (deviation from historical trend is a special case where the changes in other 'exogenous' variables remain the constant).

Changes from a counterfactual can be measured in quantitative terms or described in qualitative terms. The important thing is that observed change is not just attributed to the reform: careful consideration of what would have happened in the absence of the reform is essential.

Performance measures report on change from a baseline through the choice of the target. If, for example, the trend is for improvements in the absence of the reform, the target will need to be higher than this underlying trend to be meaningful. Where an outcome is deteriorating, the most appropriate target may well be lower than the current level if the policy cannot completely reverse this trend. This can be difficult to explain if the trends are not well known.

Quantitative evaluation methods can use statistical and modelling tools to explicitly define the counterfactual. But even qualitative methods can apply the concept. For example in 'most significant change' methodology, the questions are framed to compare actual experience against a 'without reform' scenario.

Despite the importance of reporting changes relative to a counterfactual, it is not common for policy evaluations to do so. For example, the EC (2006) review of a large number of cost-effectiveness evaluations of expenditure programs noted that only one established a counterfactual — most just focused on program expenditure and intended outcomes, and ignored other costs and impacts.

Sensitivity analysis – reporting confidence in the assessment

Evaluations should provide an assessment of the confidence that can be attached to the evidence presented. Quantitative evaluations can use statistical methods such as confidence intervals or other forms of sensitivity analysis. This can include testing the validity of the evaluation approach (for example, testing the assumptions that underpin economic modelling frameworks).

'Triangulation' is often applied to qualitative evidence. This method of testing the robustness of the evidence relies on obtaining different perspectives. For example, a business will view the impacts of a regulation reform one way while the firm's workers and customers may have different views. An industry representative may have a wider perspective, as may experts in the field. If all concur on the conclusions drawn from their different perspectives, then this strengthens the confidence in these conclusions. Methods, such as the Delphi method, can also be applied to find common ground.

Choosing the right evaluation method

Embedding evaluation in the regulatory cycle is integral to good regulatory practice. In order to gain the greatest benefit from evaluation, it is important to choose the right approach to evaluation. This will depend on the nature of the reform and the circumstances of the evaluation. Each approach and measure has strengths and limitations, and there is no 'gold standard' that is the best in all situations. So how should the choice be made?

One important selection principle is 'proportionality'. Evaluation effort should be warranted by the benefits that can arise from resulting improvements in regulation, and/or the lessons the evaluation provides for future reform efforts. For example, the European Union includes this principle in its evaluation guidelines and it is embedded in legislation that requires evaluations be undertaken such that:

> … the *scope*, *frequency* and *timing* of evaluations should be adapted to *decision-making needs* and to the *life cycle* and *nature* of each activity, as well as to the *resources* available. (EC 2004, p.16).

In considering how ex post evaluation methods can be best matched to the uses to be made of them, important questions include:

- what impacts are to be assessed, including over what time period?
- how is the evidence is to be collected, verified and analysed?
- how is the information generated in the evaluation to be communicated?

Deciding which impacts to include in an evaluation

As discussed in chapter 2, regulation reforms can have several types of impacts, including direct effects, spillover effects and unintended consequences (box 5.5). Reforms can change both the sources and the magnitude of the costs and benefits of regulations. Reforms can also change the distribution of costs and benefits — who faces which types of costs, and who benefits. These costs and benefits may be economic in nature, or may include non-market outcomes such as change in the quality of the natural environment. Other aspects of changes that may impact on individual, and hence community welfare, include changes in the exposure to risk and changes in expectations about the future.

Box 5.5 Impacts of regulation reforms

The impacts of regulation reforms could potentially include:

- *Direct effects* of reforms on target groups which induce a change in behaviour. This includes:
  - lower fees for business from savings in the administration costs of regulators, or lower costs to government where administration costs are not passed on in fees
  - savings in administrative activities and hence costs arising from lower compliance requirements
  - reductions in the need for training staff and investments to remain compliant
- *Dynamic effects* of reforms on target groups arising from changes in incentives that influence investment and innovation
- *Flow-on effects* to other industries and groups as relative prices and opportunities change, which lead to changes in distribution of resources (such as labour and capital) through the economy. These indirect effects are a consequence of the direct and dynamic changes induced by the reform, and may be intended or unintended
- '*Spillover' effects* — other effects, direct and indirect, that are usually unintended.

These impacts are generally long lasting, although they may take some time to become manifest. There may also be some temporary impacts including:

- the costs to government and business of implementing the reform
- adjustment costs — these are transitional effects that arise as part of the process of change that is induced by reforms, such as underemployed resources.

Impact assessment seeks to identify and quantify the full range of outcomes that arise over time in response to the reform to facilitate the comparison of the positive and negative effects on the community.

Whether a reform is worthwhile depends on the balance of the costs and benefits. A full evaluation will seek to report evidence to confirm (or deny) the full set of potential costs and benefits that might result from the reform. However, given the difficulty of undertaking a full impact assessment, most evaluations report on only a subset of the potential impacts. The decision about what types of impacts to evaluate should be guided by the principle of proportionality. It could take into account factors such as:

- the objective of the evaluation (what it is trying to discover) — for example, there could be a particular interest in the effects of a reform on business compliance costs, or on the environmental impacts of a reform
- the scope of the regulation or reform — reforms with relatively narrow (or shallow) impacts might only justify a simple evaluation, particularly if theory

suggests that some of the potential impacts (such as the flow-on and spillover effects) are likely to be very small and in any case unlikely to be observable.

Where some impacts are unambiguously positive, but require further effort to estimate — the evaluation could report a lower bound estimate of the benefits of reform. For example, a reduction in compliance costs for businesses is unlikely to have a net negative flow-on effect. Moreover, while evaluating the distribution of these gains could be of interest, it would not always be warranted.

Collecting and analysing the evidence

A second important consideration in choosing the right approach to a particular evaluation is the availability of evidence. Each approach has different requirements, and the availability of data and other sources of evidence can limit what can be employed.

For this reason, the regulation-making process should include planning for data collection so that the information is available for the evaluation. For example, embedded statutory reviews should identify the data needed to undertake the evaluation required by the legislation. If an evaluation has to rely on secondary data, this may limit the scope of the approach.

Qualitative evidence is more robust when the full range of stakeholders in the reform is consulted. Evaluators of reforms may find that stakeholders, having achieved the reform, have moved on and so are less interested in reporting on the changes. It can also be difficult for businesses to make 'before and after' comparisons (appendix I).

Matching the evaluation method to the requirements

Table 5.1 sets out the main evaluation approaches, indicating how well they are suited for different applications in terms of the impacts covered, the evidence and analysis required, and the purpose of the evaluation. Choice of an appropriate method for evaluation largely depends on the nature of the reform and the purpose of the evaluation.

Table 5.1 **Matching evaluation approaches to requirements**

Evaluation approach	*Uses*	*Purpose of evaluation*	*Evidence needed*
Process audits	Reporting on implementation progress, adoption of good practice and continuous improvement	Efficiency at process level	Only to the extent to which process guarantees an outcome
Performance audits	As for process audits, but wider scope to identify strengths and weaknesses	Efficiency (potentially effectiveness)	Can include performance indicators of target outcomes
Performance measurement	Monitoring and reporting on achievement of objectives	Effectiveness assessment	Measures of indicators relative to target
Impact assessments			
Compliance cost calculators	Evaluating regulations that largely change administrative costs	Lists subset of benefits and costs	Changes in paperwork time, training, investments in systems etc.
Partial equilibrium	Evaluating regulations that directly affect incentives or relative prices, or other outcomes	Lists benefits and costs	Direct changes in decisions about production, consumption, investment etc.
General equilibrium	Evaluating regulations that affect incentives or relative prices and the distribution across the economy	Lists benefits and costs	Direct and flow-on changes in decisions about production, consumption, investment etc.
Cost-benefit analysis	Evaluating regulations and reforms that have large costs and benefits. Ex ante evaluations feed into decision making processes. Ex post evaluations identify what works and why.	Net return on reform - appropriateness	As above plus the values the community places on the various impacts

Presenting the findings

So how should the results of evaluation be presented when setting regulatory reform priorities? The European Commission (EC 2007) has suggested that:

> The information needs to be politically relevant, concise and easily comprehensible. Evaluation functions should therefore promote the use of evaluation decision-making by ensuring that policy implications and lessons learnt from (and across) evaluations are synthesised and appropriately disseminated. (p. 11).

A comprehensive evaluation report would:

- describe the reform being evaluated, including the timetable followed, agencies involved and others affected by the reform
- identify the expected impacts of the reform, including the causal sequence from inputs to impacts (this should have been set out in the regulation impact statement (RIS) for the reform if associated with new legislation, or in the review that underpinned the reform)
- set out how evidence on the impacts of the reform was collected, including the parties consulted, and other sources of data and information
- present the analysis of the impacts of the reform in a clear and concise manner, explaining the assumptions made to undertake the analysis (including the counterfactual) and draw conclusions about the overall impact of the reform using appropriate summary measures
- discuss the confidence in the evidence and the conclusions drawn about the impact of the reform
- draw out any lessons from the analysis about how to improve future evaluations, and how to improve the effectiveness of future reforms (or fix problems with the one being evaluated).

The level of detail in each of these categories would depend on the audience for the report. Technical detail on the analytical approach, and the assumptions that underlie it, are needed for the experts in the policy agencies, but would not be included in a report prepared for general public information. However, the availability of this level of detail is important to ensure that the evaluation can be scrutinised by those with expertise in the area.

Performance measurement reports should set out the indicators and report on each relative to the target. They may also provide an overall summary of achievement based on a scoring type system, that aggregates up the performance. (For example, management consulting has come up with a number of different ways to report performance measures, such as 'balanced score cards', 'goal attainment scores' and 'traffic light' approaches.) However, such scoring systems should be applied with caution, particularly where the different components are 'weighted' to provide a single overall measure of performance (appendix H).

Process audits also need to describe the reform, but rather than impacts, they need to identify the processes that the reform was intended to follow. The report should assess the achievement of process objectives in a sensibly graduated way in order to move the evaluation beyond a check list approach.

The approach of the ANAO in making the results of its performance audits more meaningful to a wide variety of audiences is also useful to consider. While performance audits do not typically comment on the merits of government policy, they can comment on the impact of a policy measure. To improve the communication value of its reports the ANAO has:

- reduced the number of recommendations to focus only on more significant matters (less significant matters are referred to in the body of the report)
- endeavoured to answer the 'so what' question: *'So what do all these findings mean?'*. This is to draw out, where significant, messages of importance for all agencies, even though our audit may be directed to a single program. (McPhee 2010, p. 13).

5.3 Methods for quantifying the impacts of reform

This section sets out the strengths of quantification as part of the evaluation process, and some of the important features of quantitative evaluation. It focuses on four methods for quantifying different types of impacts (compliance cost accounting, partial equilibrium modelling, general equilibrium modelling and econometric analysis) (box 5.6). Some guidance on selecting the right method to evaluate a reform based on the nature of its impacts is also provided. (The section draws on a more detailed discussion of the various methods and their strengths and weakness in appendix I.)

Why quantify?

Quantification has several strengths and can significantly enhance evaluations of regulations and reforms. It can add rigour, improve understanding of impacts and enable estimation of the 'net effects' of regulations and reforms.

It should be noted that quantity measures do not necessarily have to be expressed in money terms, although this is the natural metric for most economic outcomes. For example, an increase in household income is most easily expressed in dollars, whereas the impacts of regulation to reduce pollution are quantified in terms of units of the various pollutants. The following discussion applies whether the metric used is dollars or other empirical quantity measures.

Box 5.6 **Key methods for quantification**

Compliance cost calculators

The Standard Cost Model (developed by the Netherlands Government) seeks to estimate the reduction in administrative compliance costs. These costs include paperwork costs, and the cost of time involved in completing the paperwork. More sophisticated versions of the cost accounting approach (such as the Business Cost Calculator developed by the Office of Best Practice Regulation) broaden the scope to include substantive costs such as investment in training and equipment required for compliance, and the costs of delay.

Econometric analysis

Econometrics is a set of statistical tools that can be used to determine whether there is a mathematical relationship between two (or more) variables, what effect the variables have on each other, and the robustness of the relationship. Econometrics provides a way to test whether relationships set out in economic theory hold in practice by applying real world data to theoretical models. In the context of evaluating regulations and reforms, econometrics can be used to determine whether regulations and reforms affect individual variables of interest.

Economic modelling

Partial equilibrium models describe the relationships between the variables that change directly in response to the reform and the target variables. Economic partial equilibrium models might look at a specific industry to estimate the effect on investment and/or innovation that results from reforms. The models may then be used to estimate the effect of these changes on industry inputs, output and profitability over time.

General equilibrium (GE) models capture the main relationships between inputs and outputs in the economy, and are used to estimate the flow-on effects to other sectors in the economy from changes at an industry level or to the availability and quality of the resources (labour, capital and land). Partial equilibrium models are generally used to estimate the 'shocks' that are fed into a GE model.

Source: Appendix I.

Quantitative approaches add rigour

Quantification in ex post evaluation adds rigour to the evaluation process because it imposes a discipline on the analyst to:

- clearly define a counterfactual and measure the changes that result from the reform relative to it
- seek evidence that changes have actually occurred
- identify who benefits and who loses from the reform

- draw some conclusions about the overall net benefits of a reform where there are both winners and losers.

Not all reforms lead to clear cut outcomes that can be easily and robustly quantified. In fact some may have few outcomes other than cost that are easily quantified. One of the strengths of quantitative analysis is that the analyst has to quantify the effects that can be measured (including by using specialised approaches to measure non-market effects). They should also document the effects that cannot be measured where there is evidence that these outcomes have occurred. The alternative is to rely on impressions and opinions (Dee 2005).

Quantification improves understanding of the impacts of reforms

Quantifying outcomes (where there is sufficient evidence available to make an estimation with any degree of confidence) improves understanding of the impacts of the reform.

The process of choosing a quantitative approach should involve identifying the most important impacts of a reform. Quantifying the impacts of reforms can help to identify the distributional effects of reforms (which groups face benefits and which face costs) and the time profile of the effects (when the costs and benefits arise).

While qualitative evaluation can shed light on the effects of regulations and reforms, it may lack the objectivity that quantification can often provide. However, where only some impacts are quantified, care is needed to present the findings in a balanced way with qualitative evidence of the impacts that are not quantified also provided.

The costs and benefits can be weighed against each other

When the impacts of regulations and reforms are quantified, the costs and benefits can be added up to determine if the net effect is positive (a net increase in wellbeing) or negative (a net reduction in wellbeing). Again, it is possible to consider the net effects of a reform using qualitative evidence, but it can be more difficult to weigh up the net effect then when quantitative evaluation is used.

Two challenges that arise in carrying out cost-benefit analysis are that it requires expressing all the impacts in a common metric and discounting over time to convert the values to a common time period. Economic analysis has developed tools to do both (appendix I).

A further challenge is explaining the distributional effects — costs and benefits are generally expressed in aggregate terms, but the distribution of these costs and benefits is also often of interest to policy makers. This is particularly important where the impacts differentially affect disadvantaged households or regions.

Quantitative estimates of the impacts of a reform should be complemented with qualitative evidence to support the estimates. Where possible, qualitative evidence for those impacts that cannot be quantified with any degree of confidence should form part of the ex post evaluation. As discussed above, methods such as triangulation can improve the quality of this kind of evidence. And such methods are also important for improving the confidence in quantitative measures.

Important features of quantitative evaluation

Quantitative evaluation approaches are based on assumptions, and rely on the availability of reliable data. For quantification to be meaningful, the analyst must be aware of the assumptions that underpin the analytical approach. The methods can then be tested to see how robust the estimates are to variations in these underlying assumptions.

Reliable data are essential

The first assumption that affects all quantification is the quality of the data and whether it actually measures what it purports to measure. Issues that can arise include:

- do reliable data exist (or can they be collected easily)?
- is it reasonable to use estimates of the impacts of regulations and reforms of the 'average businesses'? (Or the 'average household' or 'average consumer'?) In some cases, averages can mask important effects (for example, very large or very small businesses might face particular cost burdens that are hidden by averages, but could be addressed if they were identified)
- if proxy variables are used (as is often the case in econometric analysis), do they reflect the variables of interest?

Reforms should be evaluated against a realistic counterfactual

As stated in section 5.2, robust evaluations of the effects of reforms should be evaluated against a clearly defined counterfactual. Each of the approaches to quantification described in this section can be used to define a counterfactual. In the

case of business cost calculators, counterfactuals are often defined by surveying businesses about the change in costs arising from a reform. Modelling approaches adopt a more formal approach to defining a counterfactual. The issues associated with defining a counterfactual under each approach are discussed in greater detail in appendix I.

Testing the assumptions inherent in the approach

Quantitative approaches are based on assumptions, and the quality of the evaluation will be influenced by how closely these assumptions relate to reality. One of the strengths of quantitative approaches is that the assumptions can be clearly identified. In many cases it is also possible to carry out empirical tests to determine what effects the assumptions have on the final results.

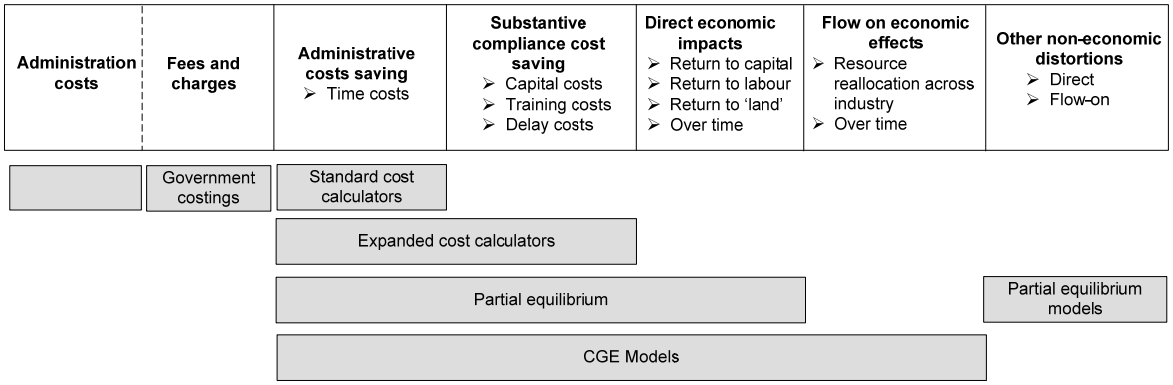
Choosing the right approach to quantification

As discussed in chapter 2 (and summarised in box 5.6), regulations and reforms can have a range of effects on businesses and the economy, the broader community and the environment. When choosing which approach to use to quantify the effects of a reform, the first step is to consider the types of benefits and costs the reform could have brought about. These could include administration and compliance cost reductions (or increases), broader flow-on effects and spillovers, and social, environmental and distributional effects. If it is considered likely that a reform has brought about significant benefits or costs in any of these areas, it might be worthwhile to conduct a quantitative evaluation. (Reform could also have changed exposure to risk, or the long term outcomes for standard of living or quality of life that can be achieved — although these can be much harder to measure.) Different quantitative approaches measure different types of impacts, and this can help guide the choice of which approach to use (figure 5.2).

- If the main effect of the reform was to change the compliance cost burden of a particular regulation, and the reform did not have the potential to introduce broader distortions, the appropriate tool is probably a compliance cost calculator.
- If the goal of the evaluation is to understand the direct economic impacts of a reform (changes in particular variables in direct response to a reform including over time) econometrics or partial equilibrium modelling could be useful.
- In the case of reforms that have broad distributional effects, modelling (such as general equilibrium modelling) can be used to understand the flow-on effects.

For all of these approaches, the availability of relevant data is an important pre-requisite.

Figure 5.2 **Matching the evaluation method to the nature of the expected impacts**



If a full cost-benefit analysis is needed, it may be necessary to use all of these tools to estimate the full set of outcomes arising from the reform and to 'add them up'. For example, the Business Cost Calculator might be applied to estimate the change in compliance costs (box 5.7). This might be complemented by the use of more sophisticated accounting tools to estimate other 'first round' changes in costs to firms. These could then be inputs to partial equilibrium models to identify how firms in the industry respond to these changes in costs, and other changes resulting from the reforms such as increases in competition or removal of price distortions or market access restrictions. The industry level changes in supply or demand can then be used in a CGE model to estimate the effects on other industries. Some industries (and their workers and owners of capital) may benefit if they use the products or services of the industry. Others may find that they face a disadvantage, for example from stronger competition for workers or for the consumer's dollar.

For each of these approaches, an important part of the evaluation process is the interpretation and communication of the results. Numbers can be influential in policy debates, so care should be taken in presentation. This includes undertaking a sensitivity analysis that provides information on the confidence in the results. Inevitably, the results of quantitative analysis reflect assumptions made in the evaluation process and are restricted by the availability of data. Any such limitations should be acknowledged, and the policy implications discussed.

Box 5.7 Using the Business Cost Calculator to estimate changes in compliance costs

The Allen Consulting Group (2009) used the Office of Best Practice Regulation's Business Cost Calculator to estimate the effects on industry compliance costs of a proposal to develop a National Construction Code (NCC). The NCC would consolidate existing building and plumbing standards into one code.

The first step in the Business Cost Calculator process was to identify the compliance costs that could arise from introducing a NCC. The costs that were identified were:

- transition costs for practitioners
- costs of technical change, where the NCC would set a different technical standard to existing standards
- costs of purchasing the NCC.

The Allen Consulting Group used ABS data to identify the number of practitioners (builders, plumbers, building surveyors and architects) that would incur the costs in each state and territory. The breakdown by state and territory was necessary because the transition costs were expected to differ by jurisdiction. Specifically, some jurisdictions already had performance-based plumbing codes, and plumbers in these jurisdictions would require less time to adjust to the (performance-based) NCC than plumbers in other jurisdictions (two hours compared to five).

The Allen Consulting Group assumed that not all professionals and trades people would incur the costs (60 per cent of builders and 80 per cent of architects and building surveyors). This assumption was based on responses to a survey about the proportion of professionals and trades people that used the existing building code.

To estimate the total transitional costs, the Allen Consulting group multiplied:

- the number of professionals and trades people in each jurisdiction by
- the proportion that would need to become familiar with the NCC by
- the estimated number of hours required to become familiar with the NCC in each jurisdiction by
- by the average hourly wage in Australia ($29.93 per hour — adult full time ordinary private sector earnings).

Based on this, the Allen Consulting Group estimated that moving to the NCC would cost around $13 million in additional compliance costs.

Source: Allen Consulting Group (2009).

6 Strengthening the framework for regulation reform

Key points

- A suite of evaluation and review approaches is needed across the regulatory cycle, to ensure that regulations remain appropriate, effective and efficient.
- How well they are deployed depends on the framework of institutions and processes that constitute the regulatory 'system'.
  - It is important that there is effective coordination and oversight to ensure that there are no 'gaps' in coverage and that the right tools are used at the right time.
- Australia's regulatory system has evolved over time and is now rated well by the Organisation of Economic Cooperation and Development (OECD).
- However, there would appear to be scope to improve its performance, from the perspective of enhancing the performance of the regulatory stock, in five areas:
  - identifying and flagging ex post review needs when new regulation is being developed
  - the prioritisation and sequencing of reform efforts
  - public consultation on review priorities, processes and outcomes
  - incentive systems for regulators to focus on compliance cost reduction strategies
  - evaluation capabilities and resourcing within government.

It emerges that several approaches to reviewing and evaluating regulations have made — and should continue to make — a useful contribution to identifying areas for reform and thus to enhancing the regulatory stock. However no approach can be relied on to 'do it all'. Each has its own niche, either in relation to the type of reforms targeted or the point in the regulatory cycle at which the approach comes into play. Such approaches are most effective, therefore, when they complement each other such that there are no 'gaps' in coverage (and, equally, no doubling up), with all regulations reviewed in the most timely and appropriate way.

Given the limited resources available for such activities — particularly skilled analysts — it is also important that these resources are allocated such that the overall returns from the various approaches can be maximised. This depends in turn on the effectiveness of the wider system or framework in which the individual approaches are designed and managed.

6.1 The regulatory system

A regulatory system comprises the set of institutions and processes that determine how and when regulations are made, administered and reviewed. In terms of ensuring that the current stock of regulation is performing well, and that poorly performing regulations are identified and remedied in a timely way, there are certain requirements that any system would need to discharge.

Managing over the 'cycle'

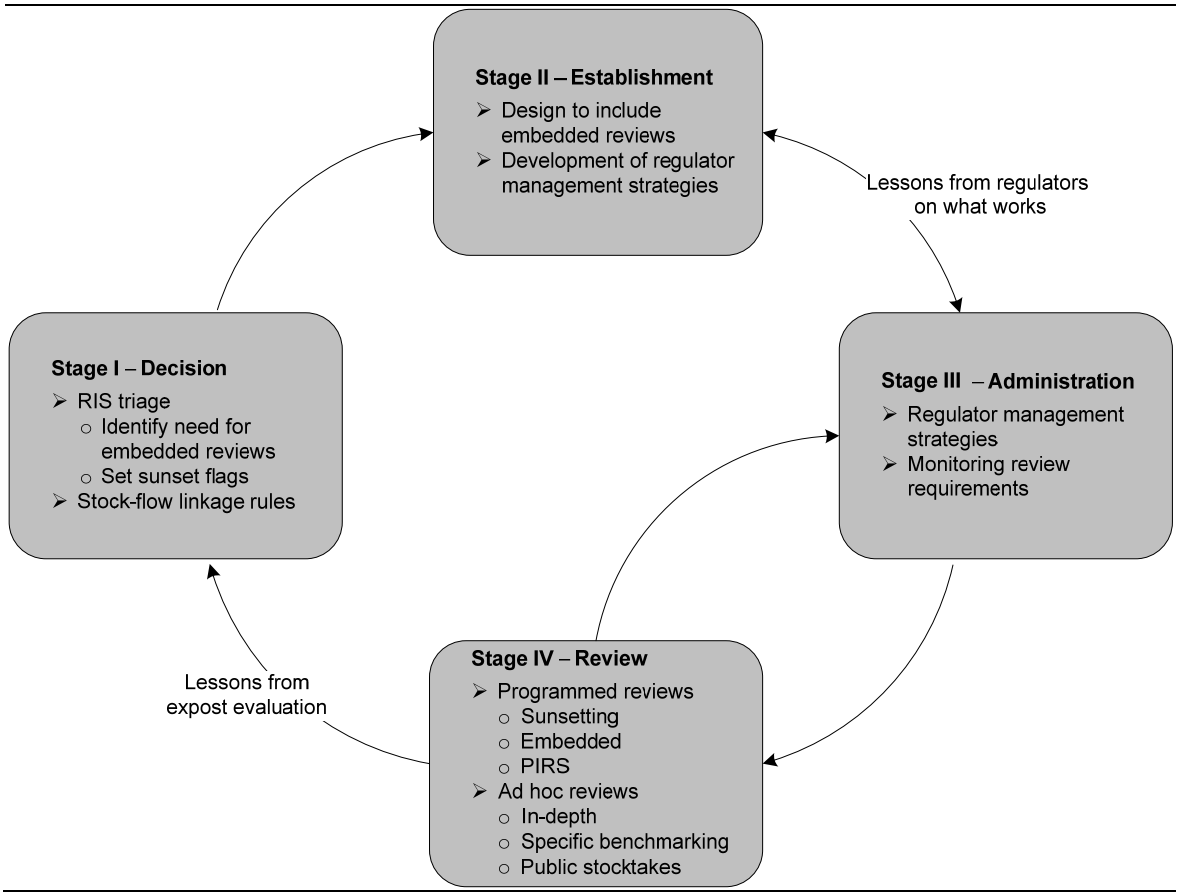
These are usefully considered in relation to the four stages of the regulatory 'cycle' that regulations commonly pass through. These involve: the initial problem identification and decision to employ a regulatory solution; the design of the regulations concerned and their implementation; the administration and enforcement of those regulations by the 'regulator'; and, finally, evaluation and review. Following this last stage, a regulation may lapse, be retained, modified or replaced, in which case the cycle recommences (figure 6.1).

Each of these stages in the regulatory cycle requires tools and strategies for 'quality control'.

- At the first *decision* stage, regulatory proposals need to be assessed for their appropriateness and cost-effectiveness. Some discipline and transparency is brought to this by a requirement to prepare a regulation impact statement (RIS) for regulation with potentially significant impacts. At this point, before new regulations are added, an assessment of the adequacy of existing regulations also needs to be made. The scope to apply more light-handed or 'market friendly' options needs to be considered. Finally, the need for the selected regulatory option to be reviewed sometime after it has been implemented should also be considered at this point.
- The second *establishment* stage involves the detailed design and making of regulation, including assignment of responsibilities and accountabilities. Object clauses and guidelines for regulators need to encourage cost-effective and risk based approaches to administration and enforcement. Where embedded legislative reviews are to be provided for, their scope and governance need to be specified.
- At the *administration* stage, regulator strategies for managing regulation and reducing any unnecessary compliance costs come into play. Review requirements need to be monitored, data collected and preparations made for scheduled reviews.

- The *review* stage itself will occur at different intervals for different regulations, depending on their significance and the circumstances of their initial formulation. Reviews also need to be proportionate to the nature and significance of the regulations concerned, and be able to address the issues that are germane to their performance.

Figure 6.1 **Review approaches through the regulatory cycle**



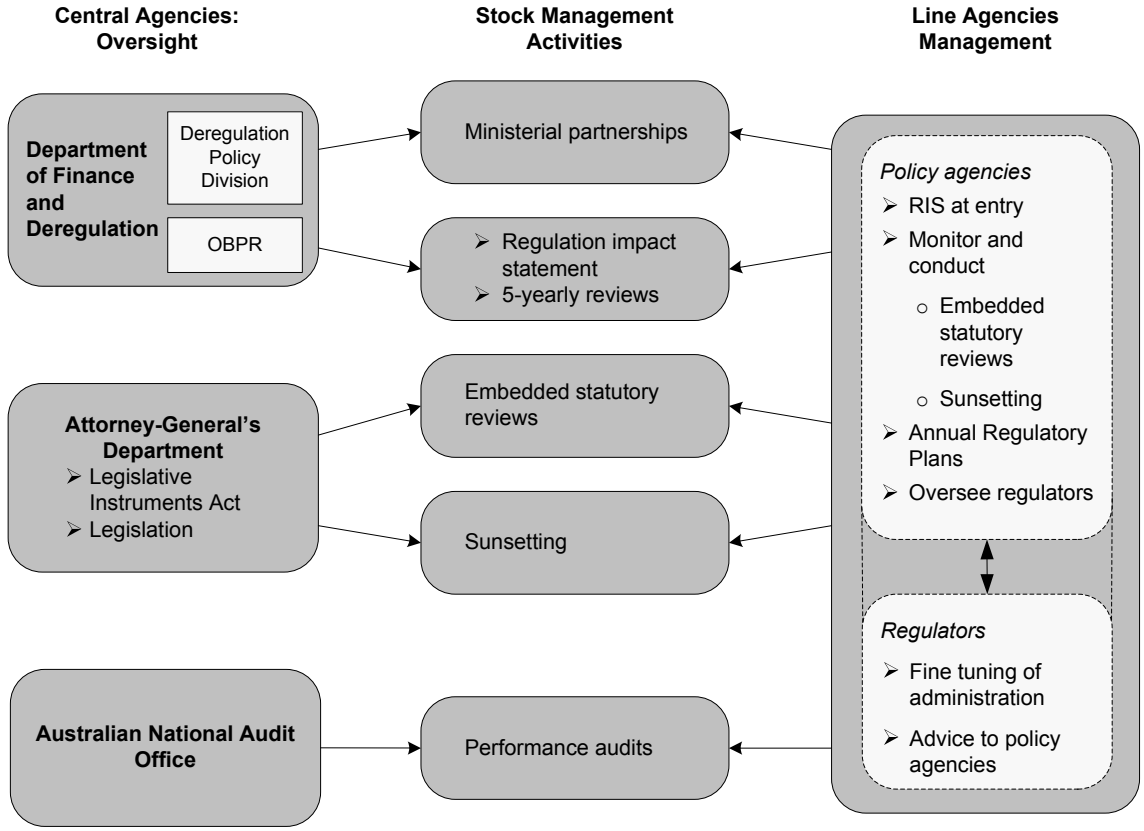
Institutional arrangements

How well these decisions at each stage of the regulatory cycle are made and implemented will depend on the institutional arrangements — organisations and processes — that assign responsibilities, provide incentives, and ensure adequate capabilities. The OECD has emphasised the importance of regulatory governance to regulatory performance (OECD 2010f). While it has acknowledged that different institutional structures can work for different countries, it has stressed the importance of having a 'joined up' system that contains clear roles, responsibilities and accountability. Such a system requires strong leadership and oversight arrangements, as well as effective 'gatekeeping' and evaluation capabilities.

A number of changes have been made to Australia's regulatory system over time, with the aim of strengthening its capacities at each stage of the regulatory cycle, as well as enabling better coordination. Among the more important of these at the Commonwealth level (figure 6.2) are:

- assignment of responsibility for good regulatory practice to a Cabinet-level Minister (the Minister for Finance and Deregulation) (appendix J)
- the strengthening of procedures and analytical requirements for making regulation, and the expansion of Office of Best Practice Regulation (OBPR) responsibilities to provide advice to agencies as well as to vet and report on compliance (OECD 2010d)
- the institution of automatic review mechanisms for subordinate regulation (notably though sunsetting) (appendix E)
- the initiation of a range of in-depth reviews in key areas of regulation (appendix C).

Figure 6.2 **The Commonwealth's regulatory system**



Within Council of Australian Governments (COAG), the establishment of the Business Regulation and Competition Working Group has for the first time provided an on-going national forum for the consideration of reforms encompassing all jurisdictions — including to improve processes (for example, regulatory assessment) and particular areas of regulation (for example the 27 'seamless national economy' items) (appendix D).

6.2 Can the operation of Australia's system be enhanced?

The OECD, in its recent review of regulation in Australia (OECD 2010d), endorsed these arrangements, a number of which had responded to earlier recommendations of the Regulation Taskforce (2006). Recommendations by the OECD that accountability be strengthened were also accepted, including through 'sign-off' provisions in relation to regulation assessments (Australian Government 2010a). The various elements required for a good regulatory system can now be said to be largely in place. However, in considering from the perspective of this study how effectively the framework is operating in practice, there would appear to be scope for further improvements in a number of areas.

Identifying and flagging review needs in new regulation

The development and establishment phases of the regulatory cycle present a good opportunity to assess whether certain regulations deserve special reviews, beyond sunsetting or other broad-brush provisions. At this point there is the ability to draw on the knowledge of those involved in developing the regulation, who are best placed to understand its potential strengths and weaknesses.

Under the Australian Government's *Best Practice Regulation Handbook*, RISs need to:

> … outline how the regulation will be reviewed. This part should set out when the review is to be carried out, and information on how the review will be conducted; for example, if special data is required to be collected (Australian Government 2010a, p. 45).

The logic behind the requirement is sound — namely that any regulation with impacts sufficient to warrant a regulation impact statement (RIS) (typically only around 2-3 per cent of all regulations made) should also be reviewed again at some point after implementation. However, in many cases responses have been

perfunctory, with little detail on the type or timing of any review. Moreover, there appears to be no systematic monitoring or follow-up.

In the Commission's view, it would be beneficial if these provisions could be strengthened. This could be achieved by:

- requiring that a review must be specified ('embedded') in the relevant statute where significant uncertainties are apparent about a regulation's impact, with the timing and focus of the review designed to address these uncertainties
- requiring that all regulations found to require a RIS be reviewed within five years (which could replace the current broader five year 'default' rule).

Where regulations have been exempted from RIS requirements under the 'exceptional circumstances' provisions, the required post-implementation reviews should also be subject to these requirements. (As noted in chapter 4, such post-implementation reviews should be broad in scope and, for areas of regulation with more pervasive impacts, ideally undertaken at arms length from the agency concerned.)

The OBPR would seem best placed to supervise these requirements, which essentially represent an extension of its current activities.

Prioritisation and sequencing

The terms of reference place emphasis on the need to identify regulatory reform priorities. There are obviously limits to the ability of any government to pursue multiple reforms simultaneously. Screening for reform needs and then prioritising and sequencing reforms — reflecting their resource requirements and interdependencies — are important to a successful reform process.

Most of the major reform approaches discussed in previous chapters have involved prioritisation at some level. For example, the Commonwealth applied a tiered screening process in the Legislative Review Program under the National Competition Policy (NCP) (appendix D) with a Council representing different community groups appointed for the purpose of determining those regulations needing detailed review. Similarly, COAG evaluated potential reform areas under its Seamless National Economy (SNE) program according to criteria related to their likely impact (box 6.1).

Box 6.1 Selecting candidates for COAG's 'Seamless National Economy' reform agenda

The Business Regulation and Competition Working Group (BRCWG) was tasked with identifying the first tranche of regulatory reform initiatives for the COAG regulatory reform agenda and the Seamless National Economy.

The BRCWG considered the potential benefits to growth, productivity and workforce mobility from over 35 possible reform areas. These were drawn from a number of sources. They included issues with multi-jurisdictional implications that were suitable for reform, but had nonetheless proved resistant to reform in the past and were evaluated according to the following considerations:

- how *wide* is the reach of the regulation?
- how *deep* is the reach of the regulation? Does it have a significant effect on industries generating a large amount of GDP?
- how *large* are the costs to business and taxpayers of complying with the regulation?
- how *damaging* is the regulation to incentives for effort, risk-taking, entrepreneurship and innovation?
- how *large* are the impediments created by the regulation to workforce mobility and participation?

Each area was then categorised according to the desired level of regulatory change: mutual recognition, harmonisation or a national system.

While the 'selection criteria' used in these and other exercises have been appropriate in the broad, there appears to have been insufficient consideration given to the best sequencing of reform efforts, or to the number and combination of reforms pursued at any one time. And, partly because of this 'congestion', review efforts have not always been proportionate to the relative significance of the different reform areas (PC 2005a). Moreover, in cases like the Seamless National Economy reforms, similar time and effort by government officials and other stakeholders are required whether the regulatory area is large and important (occupational health and safety) or comparatively minor (wine labelling).

This suggests a need for realistic prior assessment of the 'capacity constraints' in developing reform programs. In the case of the NCP, the original five year time frame for reviewing some 1800 regulations had to be extended by five years, and even then proved logistically difficult, with the quality of some reviews suffering as a result. The SNE reform stream — expanded from the half dozen original 'hot spots' to ultimately comprise 27 items — has understandably required more time and effort than originally envisaged. It further illustrates the need to complete reviews and reforms in train before embarking on new ones. This can also be

complete reviews and reforms in train before embarking on new ones. This can also be important to the credibility of an ongoing reform process, and the willingness of business people and other community groups to provide input.

Effective filtering, prioritisation and sequencing will be essential if the large wave of sunsetting regulation that looms ahead is to be effectively dealt with. This new mechanism provides a valuable opportunity both to remove redundant regulation and to improve the performance of what remains. But without careful preparation, the potential benefits may not be realised.

Transparency can assist such 'triage' processes, both by providing a discipline on decision-making and enabling the views and experience of those affected to be taken into account. It is particularly important in developing major programs of reforms to ensure that the areas with the highest potential payoff are being addressed.

Communication and consultation

There appears to be scope to improve communication and consultation within the regulatory system more generally. The OECD has identified these as two of 'four C's' in an effective system (together with coordination and cooperation) (OECD 2010f). They are important across all four stages of the regulatory cycle.

Consultation with business and other stakeholders is of fundamental importance when developing regulations, both in relation to the options being considered and at the detailed design and implementation stage. Once regulations are in place, effective two-way communication can be crucial to the effective administration of regulations and to identifying ongoing refinements. At the review stage, such communication is essential to enhance the performance of the regulators, particularly with respect to compliance costs.

As noted, public consultation on review programs can help agencies determine priorities. And advance notice of reviews can alert stakeholders to matters of importance to them and enable them to contribute in a more proactive way. The publication by departments of Annual Regulatory Plans has been required for some time. They are a potentially valuable communication tool. However, they have been of variable quality, and generally just provide a long list of regulations intended for review. There would appear to be scope to improve these plans. Although the plans are posted on the Department of Finance and Deregulation's website, there is also potential to consolidate information on upcoming regulation and review initiatives in a more user-friendly format.

The Commission understands that the AusLaw site administered by the Attorney-General's Department is to perform this role for sunsetting regulation. Advertising this facility and improving its 'user-friendliness' could enhance the contribution it will make. The Department of Innovation, Industry, Science and Research hosts a business consultation website that is searchable by keyword and agency. However, as an 'opt-in' service for agencies, the information available remains incomplete.

Incentives for regulators

How regulations are administered is an important determinant of the overall regulatory burden. Excessive costs can arise from overly stringent requirements or prescriptive supervision. These can emanate from attempts to minimise rather than optimise risk, or simply from lack of attention to compliance costs relative to the principal objectives of a regulation. The submissions by business groups in this and other reviews conducted by the Commission would suggest that there is significant scope for regulators to do more to reduce compliance costs.

These behaviours are partly 'cultural' and can really only be remedied by governments modifying some of the incentives facing regulators. Regulation Taskforce (2006) proposals for the Australian Government to pursue this though clearer guidance in legislation and 'Statements of Expectation and Intent', together with the development of cost-related key performance indicators (KPIs) and requirements for better consultation and appeal mechanisms, were all accepted (Australian Government 2006). But the extent of their implementation is unclear and could usefully be reviewed.

Evaluation skills and capacity for reviews

The reviews necessary to identify and implement regulatory reforms require analysts at least as skilled as those responsible for developing the regulations in the first place. While the initial development of regulation is generally undertaken within government, evaluation tasks — both ex ante and ex post — are increasingly being contracted out to consultants. Drawing on external expertise makes sense, particularly where more advanced evaluation methods are called for, but it should not occur to the detriment of analytical capabilities within departments or agencies. Such skills are also needed to monitor and evaluate external analysis and to formulate appropriate regulatory adjustments.

The limited availability of the right people (and their opportunity costs) are important reasons for prioritising and sequencing their efforts. However, given the relatively large gains to be had from well-targeted reforms, there may be a case for

devoting additional resources to the reform task, and to regulatory reviews in particular. This applies both to the institutions overseeing and vetting new regulations, and to those monitoring and evaluating existing regulations. The specification of review needs when regulation is being developed should also make provision for resourcing where this is likely to be necessary to ensure an adequate evaluation.

A Submissions and Consultations

This appendix outlines the study process and lists the organisations and individuals that have participated. Following receipt of the terms of reference on 24 May 2011. It released an issues paper in June to assist study participants in preparing their submissions. The Commission received 9 submissions before releasing the draft report. Those who made submissions are listed in table A.1

The Commission held informal discussions with organisations and government departments and agencies. It conducted a total of 17 meetings (table A.2)

Table A.1 **Submissions received**

Individual or Organisation	*Submission no.*
WSP Group	1
Australian National Retailers Association	2
CropLife Australia	3
Australian Chamber of Commerce and Industry	4
National Transport Commission	5
Department of Innovation, Industry, Science and Research	6
Property Council of Australia	7
Accord Australasia Ltd	8
Australian Services Roundtable	9

Table A.2 **Consultations and meetings**

Interested Parties

New South Wales

Better Regulation Office, NSW Department of Premier & Cabinet
COAG Reform Council
Equal Opportunity for Women in the Workplace
IPART
NSW Treasury

Canberra

Attorney General's Department
Australian Chamber of Commerce and Industry
Australian National Audit Office
Department of Broadband, Communications and the Digital Economy
Department of Finance and Deregulation
Department of Sustainability, Environment, Water, Population and Communities
Indigenous Corporation, Department of Families, Housing, Community Services and Indigenous Affairs
Office of Best Practice Regulation
The Treasury

Tasmania

Tasmanian Treasury

Western Australia

Western Australian Treasury

Queensland

Queensland Office for Regulatory Efficiency, Queensland Treasury

International

OECD

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