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# Tackling the underlying causes of over-regulation: an update\*

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- On August 15, the Treasurer announced the Government's final response to the report of the Taskforce, which I chaired, on Reducing Regulatory Burdens on Business. In all, the Government accepted either fully or in part 158 of our 178 recommendations.
- I am often asked what I think of the Government's response. The short answer is that in my experience a 90 per cent strike rate ain't bad!
- A longer answer, which you will no doubt be expecting from the assigned title of my presentation today, needs to be more nuanced and qualified. (I should note at the outset that my comments today are made on my own account, and do not implicate my fellow Taskforce members.)
- For a start, of the 158 'acceptances' only a minority (some 15 per cent) involved concrete, 'immediate' actions. However, as I've previously observed that was to be expected, as most of our recommended reforms will require time to flesh out and implement. Indeed in about 50 cases, the recommended action was a further more detailed review. We took this course where the area was important, but its complexity or interjurisdictional character made it too difficult for us to 'solve' in a 3 month review traversing the whole gamut of regulation.
- Seen another way, of the recommendations to reform specific regulations that the Government broadly accepted and that were *capable* of early action, nearly all were acted on.
  - They included the simplification of superannuation taxation (including abolition of the tax on end benefits), raising the thresholds for coverage of firms under the Corporations Act and Taxation Acts, reducing the costs of

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\* Speaking notes for a presentation to the Conference, *Australian Regulatory Reform Evolution*, 24-25 October, Canberra.

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business incorporation, allowing annual reports to be electronically available as the default option, allowing choice in accreditation bodies for medical devices, and a range of other matters.

- Of the rest, however, a substantial number received in principle agreement or involved a need to build on previous initiatives. Again this was to be expected, but it also means that the impact of the report at a more detailed level will only become fully evident over time as further initiatives are actually put into effect. It also underlines the importance of the Taskforce's recommendation that the implementation phase be developed around agreed timelines.
- Stepping back again to the bigger picture, the 'headline' acceptance rate was high across most of the regulatory areas we addressed.
- The two exceptions were health/aged care (one-third rejected) and taxation/superannuation (one-half rejected). The main reason given for their rejection was fiscal, either because of the potential increases in expenditure or reductions in tax revenue. The Taskforce anticipated the latter, but was of the view that it should be possible to find better ways of raising such revenue.

## From symptoms to causes

- Perhaps the most promising aspect of the Government's response for the longer term, has been its endorsement of the need for systemic changes within Government to address the underlying *causes* of excessive, badly designed or poorly administered regulation. In this area, the Government accepted 26 of the Taskforce's 29 recommendations, and it is here that I concentrate my remarks today.
- In its inquiry, the Taskforce became convinced that the problems we observed and that were brought to our attention, were not *aberrations*, but the inevitable outcome of how regulations were being made and administered.
- They included regulations that were (among other things) overly prescriptive, poorly targeted, duplicative, mutually inconsistent, excessive in their coverage of firms and unduly onerous in the reporting and other obligations on the firms affected.
- Such regulatory outcomes are testimony to systemic failures in how governments have been responding to the rising demands and needs of our increasingly affluent, knowledgeable and risk-averse society.
- Rather than repeat the detailed reasoning and evidence laid out in the Regulation Taskforce's report (and in a speech that I gave following the Government's interim response) let me take some licence today by characterising the problems through a hypothetical example.

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## A hypothetical regulation in the ‘making’

- A child is critically injured following a mishap with a skipping rope. On a slow news day, the story gets a run in one of the tabloids. A caller to the local radio talk show expresses alarm that these potentially lethal products are still being sold. The compere, a high profile figure, expresses concern: “Government inaction is putting our kids at risk!!” The Minister is commanded to appear on his show. In the face of some torrid questioning and innuendo, she promises that her government will take firm action to eliminate the threat posed by skipping ropes.
- Next day, the talk-back king pursues a new story (about bad language in public places). The Minister, however, feels obliged to instruct her department to take steps to put the government’s new skipping rope policy into effect.
- The department gets to it. Following a couple of conversations with the Minister’s office, a proposal is drafted, for Cabinet consideration, to ban skipping ropes. However, a few days before Cabinet is due to meet, someone recalls that any new regulations that may impose costs on business must have a Regulation Impact Statement, demonstrating the superiority of the preferred course of action. Panic stations!!
- A RIS justifying the ban is hurriedly put together by a junior officer and submitted to the Government’s Regulation Unit, whose job it is to assist agencies and monitor their compliance with the Government’s RIS requirements. The Unit naturally finds that the draft is inadequate on the key matters of demonstrating that any new government action is warranted and that a ban in any case would be the best available action. (Consternation!!)
- A second draft, responding to some of the Unit’s concerns, is quickly assembled and re-submitted. On a less significant matter, or with a less extreme regulatory option (and perhaps with more time) the revised RIS may have been helped over the line. As it is, the Unit is obliged to fail it a second time.
- Time is now up, however, and the submission proceeds to Cabinet. A Coordination Comment from the Regulation Unit in the Cabinet Submission appendix notes that the RIS was not adequate. The Minister (who has not read the RIS) concludes that the Unit is being obstructionist. Cabinet, aware of the origins of the new skipping rope policy – the little girl, the public outcry – agrees to the Minister’s proposed ban. (The Treasurer/Finance Minister has been briefed by his department about the adverse efficiency implications, but takes comfort from the fact that there are at least no *budgetary* implications. The Minister responsible for Industry knows that there are no local manufacturers of skipping ropes left – the last turned to importing when the tariff dropped below 15 per cent – so she too is comfortable.)

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- I could conclude the hypothetical there, as I think you get my drift. But this would omit the *implementation* phase, which as business groups told the Taskforce, can be as problematic as regulation-making itself in contributing to bad outcomes. So I'll go further. In this contrived example, Cabinet could have decided that a 'black letter' ban on skipping ropes was going a tad too far. (Maybe there *was* a small local manufacturer after all, perhaps in a country electorate, or maybe the already precarious relations with the main exporting country were seen as an issue). So, instead, the power to decide which skipping ropes are too dangerous for sale is delegated under a legislative amendment to the regulator.
  - The regulator is now obliged to make the call on this politically tricky issue. Not being super-human, he (or she) is inclined to be cautious. He knows from painful experience that his agency will be lambasted publicly if any further mishaps occur, but receive no credit at all if skipping ropes are able to be used more liberally without mishap. So to be on the safe side, he issues a new subordinate regulation (which would again fail a cost-benefit test) placing a range of conditions on the marketing and sale of not only children's skipping ropes, but *all* devices that could conceivably be used by children "for the purpose, inter alia, of skipping or related activities".
  - Things now start to get politically interesting again, because the regulator has inadvertently affected some key Australian enterprises producing a variety of products, as well as many firms (and adult consumers) who use them. Moreover, firms producing related goods are obliged to incur labelling and other costs to stop their products from being used for skipping, as well as in convincing the regulator about their compliance. Complaints are made to government at different levels by the firms' industry associations.
  - Years go by. Eventually a review of the regulations is conducted – possibly as part of a wider review of business redtape – and the regulatory constraints are greatly eased and their product coverage reduced.

### **Poor outcomes reflect poor processes**

- This was clearly a somewhat fanciful case study. But the reality is that a close variant of this little story could have been told based on any one of many actual examples at all levels of government, including some major regulatory initiatives.
- It therefore illustrates a number of failings in the way the legislative and other regulatory instruments of public policy have been developed in the past, which explain the poor regulatory outcomes about which business groups have understandably been so critical.

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- Again, I commend the Taskforce’s report to you for a more detailed account, but for present purposes the key words are knee-jerk political responses, lack of analysis of costs and benefits, haphazard or limited consultation, and, above all, a ‘regulate first ask questions later’ culture within parts of government; a culture that is reinforced by a perception within the wider community itself that government action equals regulation.
  - This is notwithstanding the fact that all governments have processes in place that require them to analyse the case for intervention and assess the impacts of alternative options – with this all being set out transparently for decision makers, as well as for those directly affected and the wider community, in a Regulation Impact Statement. Business groups were supportive of those processes, but critical of the failure of government to properly implement them.
  - The Taskforce’s recommendations were designed to build on and strengthen existing requirements at the Commonwealth level in four key areas:
    - improving regulation-making processes through stricter obligations on policy departments and regulatory agencies to undertake better analysis and effective consultation;
    - improving the performance of those administering regulation by clarifying policy intent, sharpening accountability and achieving better communication and interaction with those being regulated;
    - ensuring that regulations are coherent and consistent across jurisdictions; and
    - ensuring that they remain appropriate over time, through the use of tighter sunset provisions and periodic reviews.
  - It is not my intention to go through all our specific recommendations in these areas. They can be readily found in our report. What I can more usefully do, in light of the Australian Government’s acceptance of most of those recommendations, together with some additional initiatives, is set out my understanding of how regulatory processes are intended to operate in the future. I will then discuss a number of ongoing issues and challenges in getting the best out of this system.

## **Some key features of the Australian Government’s new regime**

The new regime differs from the old in several crucial respects –

- Firstly, the bar has been raised in terms of the procedural and analytical requirements in making regulation, including a need to estimate likely compliance costs using an IT-based tool, the Business Cost Calculator, to undertake consultations consistent with principles established by Government

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and to explain why existing regulation is inadequate – all of this being documented in a regulation impact statement where there are significant impacts on business.

- Secondly, where a regulatory proposal fails to satisfy these (and other) requirements, the proposal will be precluded from going any further, unless exceptional circumstances demonstrably warrant such a breach. In that case, however, the regulation will need to undergo a post-implementation review within 1-2 years.
- Thirdly, the assessment of compliance will continue to be independently made by a successor body to the ORR, within the Productivity Commission, named the Office of Best Practice Regulation. Relative to its predecessor, this body will have additional functions relating to oversight of the BCC, annual regulatory plans and post-implementation reviews and an increased role in assisting agencies improve their regulatory assessments, including through cost-benefit and risk analysis. To discharge these functions, additional resources have been allocated to it.
- Fourthly, in addition to the increased disciplines on regulation-making, regulatory bodies will face some significant changes to their ‘incentives environments’ facilitating an approach to their regulatory responsibilities that balances competing objectives and is proportionate to the risks involved. The key changes include Ministerial Statements of Expectations, enhanced performance reporting, consultation protocols and stakeholder forums, codes of conduct, and timely review processes.
- Fifthly, the Government has agreed to pursue action within CoAG in areas of regulation where lack of consistency was identified as a major problem. Ten ‘hot spots’ for reform have been agreed under the CoAG’s National Reform Agenda. Also the Productivity Commission has been asked to develop a framework of indicators to benchmark regulatory performance across jurisdictions over time.
- Finally, the stock of regulation will be *systematically* reviewed over time, rather than through ad hoc initiatives. Henceforth, any legislation not already subject to in-built review, or regulatory sunseting, will be screened for a review after five years. In the meantime, over the next five years, the Productivity Commission will conduct annual targeted reviews and establish further reform agendas spanning all areas of regulation across the economy.
- The only recommendations in this stream which the Government rejected outright, related to proposed amendments to the Legislative Instruments Act to embed agreed best practice requirements and to shorten sunset periods for subordinate regulation. Also, rather than assign responsibility for overseeing

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good regulatory practice to a single Ministerial ‘champion’ in Cabinet, the Government underlined the need for *all* Ministers to ensure that best practice is achieved, with the Treasurer’s portfolio having lead responsibility for regulation reform matters.

- All of this represents a considerable advance over previous arrangements in addressing the underlying causes of over-regulation. However, even the most promising chickens should not be counted before they hatch. A number of implementation issues and challenges still need to be successfully handled for the reforms to have their intended effects.

## Issues and challenges

- The most fundamental and formidable challenge is to bring about *cultural* change within the institutions of government responsible for regulation. While the new regime *is* a significant improvement over the previous one, a number of changes are more a matter of degree. Most elements were at least implicitly present in the previous regime: it’s just that they were often not properly implemented.
- So why should we expect better performance against higher standards? The answer depends on the extent to which the incentives facing regulatory bodies change, and their capability is improved, under the new arrangements.

### *Stronger gate-keeping*

- Looking at incentives first, for reasons already given, the forces behind a ‘regulate first, ask questions later’ approach within government are strong. Formal requirements to undertake a RIS etc. have to date not been an adequate counterweight. Exposure of the poor compliance records of particular agencies, after the event, in the Productivity Commission’s annual publication *Regulation and its Review*, may have produced some individual conversions, but arguably they have not been deeply held. There has been no real trend improvement in more recent years (as the forthcoming report covering the most recent year demonstrates).
- What has been most lacking is enduring tops-down support for good regulatory practice within government, including effective sanctions where there is a failure to achieve minimum standards.
- The latter is particularly important, since history tells us that while governments (at all levels) have occasionally taken significant steps to improve regulatory practices, the impact of such reforms on actual regulatory behaviour tends to be

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temporary. Over time, the initial political interest wanes, standards lapse and old ways eventually reassert themselves.

- Achieving a *sustained* improvement requires institutional or procedural reforms that can entrench good process in the day-to-day workings of government. Australia has arguably secured this in a number of key policy areas in the past couple of decades, including monetary policy and elements of National Competition Policy, and our economic performance has reaped the benefits. However, while we have also made significant progress in establishing the elements of good regulatory *process* – indeed, the Commonwealth’s Best Practice Principles were originally adopted by the OECD – we have not succeeded in embedding them in regulatory *practice*.
- Thus in my view the Government’s commitment to strengthening the ‘gate keeping’ arrangements – such that a failure to meet the new requirements will prevent a regulatory proposal from proceeding – is potentially the most crucial feature of the regime. If effectively implemented, the stricter gatekeeping arrangements could transform the incentives on government departments and regulatory agencies to take the best practice principles seriously. For example, a common deficiency in regulation-making, which generally becomes apparent when a RIS is finally put together, is a failure to adequately define ‘the problem’ in the first place and to explain why government intervention could help. (As in my skipping rope story, a bit of thought at this initial stage may be sufficient to show why action would be futile or costly.) Under the new regime, lack of attention to these important threshold considerations could bring unstuck the whole policy initiative. Accordingly, the incentive to address these matters right at the beginning of the policy-development (or regulation-making) process should be heightened.
- The Government has recognised the significance of gatekeeping discipline to the success of the new regime by making the Prime Minister the arbiter of whether there may be exceptional circumstances warranting a leave pass from the best practice requirements. Early decisions on such petitions will be instrumental in conditioning expectations throughout government about required standards.

#### *Post-implementation reviews as a fail safe*

- For those few cases where there may be legitimate reasons for by-passing the requirements, the Government has agreed that a post-implementation review should be held within 1-2 years. This is an important safeguard against any unintentional consequences of such regulation persisting. Keeping track of those cases will fall to the new OBPR, which should also advise/determine the nature of the review, to ensure that compliance costs or any other emerging issues can be properly addressed.

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- Unlike the separate stream of five-yearly reviews, which in the interests of cost-effectiveness should only be conducted where preliminary screening reveals significant problems, post-implementation reviews will need to be mandatory, since the regulations were introduced without the benefit of the usual assessment process.

### *Establishing the Office of Best Practice Regulation*

- The Government's preparedness to introduce sanctions on non-compliance has effectively given the new Office more power than its predecessor. Judgements made by the OBPR will essentially determine whether regulatory proposals can proceed. This could be expected to increase the external pressures on that body and underlines the importance of its continuing independence from the executive arms of government.
- Importantly, the OBPR will be more than a watchdog on compliance; it will also play a greater role than its predecessor in providing training and technical assistance to officials, and has been granted additional resources for this purpose. In other words, it will assist in capacity building within departments and agencies, to help them meet the higher standards of analysis that are now required.
- This dual role – as referee and coach – poses some obvious challenges. In particular, to discharge the refereeing role appropriately, its coaching needs to be focussed more on generic capability than on the development of options in specific cases. That said, from my observations on what can sometimes pass for policy analysis, there is much that can be done by the new Office to educate officials in the rudiments of good regulatory practice, short of it crossing the line into policy development territory.
- At a more practical level, there is much to do to build up the OBPR's own capacity and capabilities, in order for it to perform the additional tasks assigned to it and handle the extra volume of activity. For example, as noted, the Office will shortly take over responsibility for developing and overseeing use of the Business Cost Calculator, annual regulatory plans, etc., which have previously been with the Office of Small Business (in DITR). A special Cost-Benefit Unit is being established, to provide a centre of expertise and advice to agencies in the use of such a framework. The skill shortages confronting other parts of our buoyant economy are also evident here. Recruiting capable people with good analytical and communication skills is not easy and will take time. Meanwhile, we have been seeking secondments from among departments to help establish critical mass more quickly, while maintaining necessary standards.

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### *Building capacity within departments/agencies*

- Perhaps related to such capacity issues, I am conscious of disquiet within the senior ranks of the Public Service about the potential additional burdens on the bureaucracy resulting from the new requirements. It is important that the new requirements be well integrated and streamlined, to avoid unnecessary complexity, duplication etc., and this is currently receiving much attention from those overseeing implementation of the new regime. Beyond that, however, I must confess that I find it hard to be *too* sympathetic, especially considering the wider costs and benefits at stake for the community as a whole.
- True, the Cabinet's decision that all regulatory proposals involving potentially non-trivial compliance costs must have those costs quantified using the Business Cost Calculator, is a significant additional commitment, especially if done well. Even so, the majority of regulations proposed in any year have negligible business impacts and would be quickly screened out of the need to do a full BCC analysis (a 'Quicksan' module has been developed for such assessments). Of those that do proceed, because compliance burdens are an issue, a BCC report will in many cases yield useful information about the most cost-effective approach. (I understand that there have already been cases of regulatory proposals being substantially revised in light of costs revealed by the BCC.)
- As for the RIS process (to which the BCC is one important input) while there have been complaints about the burdens imposed, the facts are that in 2005-06:
  - only 96 regulatory proposals out of around 2600 (4 per cent) were assessed as needing to prepare a RIS;
  - and the average salary cost of RISs prepared was \$5000.
- At face value this does not look onerous. Indeed the average cost of preparing a RIS is a tiny fraction of the average consultancy contract these days, and may well be lower than it should be if done properly.
- The real source of the burden on government in many cases, is more likely to come from RISs being done at the last minute, or the need to do *new* work for the RIS, when it should have already been done in the normal course of policy/regulation development. The RIS is merely a written account of elements that are essential to good public policy: namely, establishing a case for government intervention and determining which option would be most appropriate. This should only be burdensome when decision-making has taken a short cut – and perhaps in that situation it *deserves* to be!

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### *Improved consultation*

- The Government agreed with the Taskforce about the overall inadequacy of consultation by many departments and agencies when making regulatory decisions. It endorsed as a key principle of good regulatory process that “there needs to be effective consultation with regulated parties at all stages of the regulatory cycle.” And it accepted the Taskforce’s recommendations for a whole-of-government policy on consultation requirements, setting out best-practice principles relating to when and how consultation should take place, and a website portal enabling any business to find out what is happening and register an interest.
- While this policy will undoubtedly require some additional effort on the part of departments/agencies, the Taskforce was in no doubt that this was justified and could potentially yield significant improvements in regulatory outcomes.
- Given that the Government’s new policy principles on consultation will need to be pitched at a relatively high level to be generally applicable, assessing whether performance is adequate in practice will be another important duty of the OBPR. As in the past, the standards expected will vary according to the significance and potential impacts of the regulation in question. At one extreme, for example, a regulation with only moderate impacts on a specific section of business, may need only relatively low key and targeted consultation; at the other extreme, a major piece of legislation, significantly affecting a cross-section of business and the community, may require a policy ‘green paper’ and formal submissions. In all cases, though, it is fundamental that those being consulted have an early opportunity to comment on options being considered and, at a later stage, to give feedback on the detail (which, as the saying goes, is where the ‘devil’ often is).

### *A combined effort is needed*

- In this, as in other aspects of the new requirements, change is likely to be more substantial and enduring if it is evolutionary rather than revolutionary. The Office of Best Practice Regulation will be playing its part in assisting officials to understand what good regulatory practice involves, and will progressively raise the compliance bar as familiarity and experience with the new regime grows. For their part, policy departments and regulatory agencies will need to ensure that the training of relevant officials in the new processes, and in good regulatory practices generally, is given priority, and that there are the resources and systems in place to ensure that it is put to good use. The appointment of a Senior Executive in each organisation to be the key coordinator and point of contact with the OBPR will facilitate this.

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- The requirements for regulatory analysis will be laid out in a new publication, the *Best Practice Regulation Handbook*, which will be released in draft form shortly. It will explain the new regulatory assessment requirements, when they need to be followed and what type and level of analysis is appropriate in different circumstances – including consultation, compliance cost assessment and risk analysis. The Handbook will be accompanied by a brief ‘User’s Guide’ and check-lists, to facilitate take-up. There will be an opportunity to provide feedback on this material and other operational aspects during a six month trial period.
  - That opportunity extends also to business groups and the wider community. While business has been rightly critical of the growth in regulation, it has also often been an advocate for more government regulatory intervention and support. Moreover, when regulatory changes have been in the offing, even major ones, business has not always been active in offering advice and information that could help avert higher cost options. If government is to do a better job in evaluating compliance burdens and other impacts as a normal part of regulation-making, business will need to play its part in helping government identify and measure such impacts.
  - In concluding, lest you mistake my message today, I should make clear that the need for regulation is not at issue. Regulation is essential to a well-functioning society and economy. The challenge is to ensure that regulation evolves to meet society’s needs in the most appropriate and cost-effective way. That will only occur if there are good processes and institutions in place to test the need for regulation and to determine its most beneficial form. If effectively implemented, the Government’s response to the Regulation Taskforce’s report provides a promising basis for achieving this at the Commonwealth level, and a positive model for the States and Territories.