Office of Regulation Review

A Guide to Regulation

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Inquiries:
Office of Regulation Review
PO Box 80
Belconnen ACT 2616
Australia

Tel: (02) 6240 3290
Fax: (02) 6240 3355
Email: ORR@pc.gov.au

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FOREWORD

This document, *A Guide to Regulation (Second Edition)*, has been prepared by the Office of Regulation Review (ORR), which is part of the Productivity Commission, for use by policy and regulatory personnel in all Commonwealth Government departments, agencies, statutory authorities and boards. The document can be made available to the public.

In March 1997, the Government announced its responses to the recommendations made by the Small Business Deregulation Task Force.[1] Several of those responses indicated that the ORR would produce a publication to be named *A Guide to Regulation*. Those responses set down some specific matters to be addressed in this document, which was endorsed by the Government in September 1997. Subsequently, a Commonwealth interdepartmental committee was established to inquire into quasi-regulation.[2] The Government accepted the recommendations of the committee to strengthen the scrutiny and assessment of quasi-regulation and to make such regulation more effective and accessible.

This second edition of the Guide incorporates Government decisions about regulatory best practice and quasi-regulation. It is designed to assist officials working on the review and reform of existing, new or amended regulation. It explains how best practice processes — such as the use of Regulation Impact Statements (RISs) to consider alternative ways of attaining the goals of regulation — can lead to better regulations.

The Guide consists of five separate parts, each part providing progressively more detail. It is designed so that those requiring a broad overview of the Commonwealth regulatory review requirements need read only the first one or two parts. Those who must prepare RISs may need to draw on the detail of the latter parts.

Part A describes in broad terms best practice processes and requirements for developing and amending legislation and regulation.

Part B sets down the seven major elements of a RIS which are designed to formalise and record the steps that should be taken in the formulation of policy. Modified RIS guidelines designed specifically for the assessment of taxation measures are included.

Part C consists of a simple and brief checklist for use by officials in preparing a RIS.

Part D provides more detailed guidance for use in preparing a RIS.

Part E sets out some explanatory material about issues addressed in a RIS.

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1 *More Time for Business*, Statement by the Prime Minister, the Hon John Howard MP, 24 March 1997.

2 Quasi-regulation refers to a wide range of rules or arrangements — such as codes of conduct or advisory notes — by which governments influence businesses to comply, but which do not form part of explicit government regulation (ie. legislation/ black letter law).

No examples of specific RISs have been included in this Guide, in part because such examples cannot satisfactorily cover the wide range of regulatory matters covered by Commonwealth departments, agencies, statutory authorities and boards. However, specific examples of RISs that assess a range of regulatory issues can be found in the explanatory material tabled in Parliament with the:

- Privacy Amendment Bill 1998;
- Corporate Law Economic Reform Bill 1998; and
- Education Services for Overseas Students (Registration of Providers and Financial Regulation) Amendment Bill 1998.

An example of a RIS for subordinate regulation is the Telecommunications Numbering Plan 1997, developed by the Australian Communications Authority.

Further examples of RISs can be found in the explanatory material tabled in Parliament, after June 1997, for those legislative changes which have an impact on business.

Comments and suggestions about the content of this Guide are welcome and should be directed to the ORR. Users of this document may contact the ORR at any stage for more information or for assistance in preparing a RIS.

Contact details:

Office of Regulation Review
Productivity Commission
PO Box 80
Belconnen ACT 2616
or

Level 3, Nature Conservation House
cnr Emu Bank and Benjamin Way
Belconnen ACT 2617

Phone: (02) 6240 3290

Fax: (02) 6240 3355

e-mail: ORR@pc.gov.au

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A: BEST PRACTICE PROCESSES FOR REGULATION

A.1 Introduction

Regulation includes any laws or other government 'rules' which influence the way people behave. It is not limited to primary or delegated legislation; it also includes 'quasi-regulation' (such as codes of conduct, advisory instruments or notes etc) where there is a reasonable expectation by governments of compliance.

While some regulation is necessary and beneficial, there are some cases where it may not be so or where it could be better designed. Regulation should not only be effective, but should also be the most efficient means for achieving relevant policy objectives. In this context, there is a public perception that rule makers too often concern themselves with the issue of effectiveness, ignoring efficiency issues (that is, existing regulation may be effective, but it may not necessarily be the 'best' means for achieving the particular policy goal).

Determining whether regulation meets the dual goals of 'effectiveness' and 'efficiency' requires a structured cost-benefit approach to policy development. The relevant problem to be addressed and subsequent policy objective should be identified as a first step in the policy development process, followed by consideration of a range of options (including no action) for achieving the objective. The benefits of any regulation to the community should outweigh the costs.

Preparation of a Regulation Impact Statement (RIS) is a critical feature of the regulation making process, primarily because doing so formalises and evidences the steps that should be taken in policy formulation. It helps to ensure that options to address a perceived policy problem are canvassed in a systematic, objective and transparent manner, with options ranked according to their net economic and social benefits. The RIS embodies this analytical process.

Improving the regulation making culture will require some fundamental changes to the way regulation is made, requiring departments, agencies, statutory authorities and boards to re-orient their policy and regulatory focus, including their regulation making processes.

A Guide to Regulation has been endorsed by the Commonwealth Government, and compliance with the outlined procedures and processes is *mandatory* for all Commonwealth departments, agencies, statutory authorities and boards making, reviewing and reforming regulations.

There are related requirements of the Council of Australian Governments (COAG) that RISs should be prepared for new regulations proposed, or existing regulations which

are reviewed and/or reformed, by Ministerial Councils and national standard setting bodies. These requirements are set down in the COAG-endorsed publication *Principles and Guidelines for National Standard Setting and Regulatory Action by Ministerial Councils and Standard-Setting Bodies*. Officials making new regulation or reviewing and reforming existing regulations for these decision-making forums should consult that publication rather than *A Guide to Regulation*.

A.2 What is a Regulation Impact Statement (RIS)?

The RIS is a document prepared by the department, agency, statutory authority or board responsible for a regulatory proposal following consultation with affected parties, formalising and evidencing some of the steps that must be taken in good policy formulation. It requires an assessment of the costs and benefits of each option, followed by a recommendation supporting the most effective and efficient option. It must be incorporated into the assessment process used by all areas of government responsible for reviewing and reforming regulations.

Preparation of a RIS ensures that all relevant information is documented and that the decision-making processes are made explicit and transparent.

RISs are widely used by state and territory governments, and by member nations of the Organisation for Economic Co-operation and Development (OECD).

A RIS has seven key elements which set out:

- the problem or issues which give rise to the need for action;
- the desired objective(s);
- the options (regulatory and/or non-regulatory) that may constitute viable means for achieving the desired objective(s);
- an assessment of the impact (costs and benefits) on consumers, business, government and the community of each option;
- a consultation statement;
- a recommended option; and
- a strategy to implement and review the preferred option.

For further information about RISs, see section B of this guide, ‘Guidelines for Commonwealth Regulation Impact Statements (RIS)’.

A.3 Should a RIS be prepared for all regulation?

Subject to limited exceptions — outlined below — the Government has decided by administrative decision that preparation of a RIS is mandatory for all reviews of existing regulation, proposed new or amended regulation and proposed treaties

involving regulation which will directly affect business, have a significant indirect effect on business, or restrict competition.

The term 'regulation' includes primary legislation and subordinate legislation, such as statutory rules approved by the Governor-General in Federal Executive Council and legislative instruments — either disallowable or non-disallowable — made by boards, agencies or departments. Regulation includes international treaties. It also includes quasi-regulation, which refers to a wide range of rules or arrangements where governments influence businesses to comply, but which do not form part of explicit government regulation. Some examples of quasi-regulation include industry codes of practice, guidance notes, industry-government agreements and accreditation schemes.

'Business' includes any private organisation which aims to make a profit, the commercial activities/transactions of not-for-profit organisations, and any government business enterprise.

RIS requirements apply to *all* government departments, agencies, statutory authorities and boards that review or make regulations which have an impact on business, including agencies or boards with administrative or statutory independence.

Regulation affects business when it imposes a cost or confers a benefit on business. The terms 'cost' and 'benefit' should be interpreted broadly, covering items which can be immediately quantified in monetary terms (eg service charges, subsidies, compliance costs), as well as items which cannot be immediately quantified in monetary terms (eg restrictions on competition, environmental damage etc).

Restrictions on competition can impose substantial costs through higher prices, reduced choice and impediments to innovation and efficiency. Reflecting these costs — and to meet the requirements of the *Competition Principles Agreement* (CPA) — restrictions on competition have been singled out for special attention in RISs.

The Commonwealth Government has asked the Office of Regulation Review (ORR) to provide advice to departments, agencies, statutory authorities, boards and other decision-making forums about whether a RIS should be prepared, on a case-by-case basis.

Preparation of a RIS will *not* be mandatory for regulation that:

- is not likely to have a direct, or a substantial indirect, effect on business and is not likely to restrict competition; or
- is of a minor or machinery nature and does not substantially alter existing arrangements; or
- involves consideration of specific Government purchases;[1] or

[1] This exception applies to procurement of specific goods — such as motor vehicles — and public sector competitive tendering and contracting (CTC). However, a RIS may need to be prepared for procurement and CTC guidelines.

- is required in the interest of national security; or
- is primary or delegated legislation which merely meets an obligation of the Commonwealth under an international agreement by repeating or adopting the terms of all or part of an instrument for which the agreement provides; or
- is excluded from consultation in the Legislative Instruments Bill 1998. Exclusions are provided for legislative instruments that give effect to specific Budget decisions, application order proposals made under section 111A of the Corporations Law of the Australian Capital Territory, and those that provide solely for commencement of all or part of enabling legislation; or
- is a regulation of a state or self-governing territory that applies in a non-self governing territory.

The full RIS process is inappropriate for taxation measures, particularly where prior public consultation will provide an opportunity for tax avoidance. However, the RIS required for tax proposals will examine the administrative options for ensuring compliance with tax proposals and the costs and benefits of each alternative, to ensure that compliance cost considerations are fully taken into account and with a view to selecting the most appropriate method of compliance.

For further information about the modified RIS for tax legislation, including legislation resulting from the Budget, see section B (page B9) of this guide, 'B(Tax) Guidelines for Commonwealth Regulation Impact Statements (RISs) for Taxation Measures'. In addition, the Australian Taxation Office (ATO) issued in September 1998 *ATO Guidelines for the Preparation of Regulation Impact Statements (RIS).*

While it is important to ensure compliance with these best practice processes, it is also necessary to retain flexibility for emergency situations — such as public health and safety emergencies etc — where there is an urgent need for government action. These situations are, however, likely to be rare and a RIS still needs to be prepared *after* regulatory action has been taken.

It is noted that preparation of a RIS may be unnecessary where regulation reflects a *specific* election commitment and there is no scope to consider alternative ways to meet that commitment.

If there are any doubts as to whether or not a regulatory review or proposed regulation qualifies for an exemption/exception from RIS requirements, the matter should be referred at the earliest opportunity to the ORR (see section A.6 for more information). It is important to note that it is the ORR — not individual departments, agencies, statutory authorities or boards — that decides whether a RIS should be prepared.

A.4 At what stage should a RIS be prepared?

In order to obtain the maximum benefit from the RIS process, for new regulation (including amendments to existing regulation) the RIS should be prepared by officials once an administrative decision is made that regulation may be necessary, *but* before a policy decision is made by the Government or its delegated officials that regulation is necessary. Where consultation is not possible before regulation is made, consultation should occur afterwards.

The analytical framework underpinning a RIS should be used throughout the policy development process. It is important to note that for reviews of existing regulation, the terms of reference should reflect the key elements of the RIS, with any reports, studies, reviews or discussion papers using a RIS framework. This requirement ensures that the RIS framework is incorporated at an early stage in regulation reviews and is used until a final RIS is prepared, prior to a policy decision being made.

In the case of treaties that involve regulation, a RIS should be prepared before the formal policy decision to pursue treaty negotiations, again prior to Australia signing a treaty and, finally, when the treaty is tabled in the Parliament with the National Interest Analysis (see page A6 for more information about RISs and treaties).

A.5 Key governmental processes to consider when preparing a RIS

RIS requirements are mandatory for any regulatory proposal affecting business, not just those considered by Cabinet. Other means by which regulation affecting business is proposed include by Ministerial correspondence and agreement, press releases, interviews, independent boards, other policy changes not dependent on legislative change, in meetings of Ministerial Councils and as subordinate regulation.

The ORR is responsible for examining and advising on the adequacy of all RISs (see section A.6 for more information). RISs should be developed in consultation with the ORR. Departments, agencies, statutory authorities and boards must consult with the ORR as early as possible in the policy development process. (See the Foreword of this Guide for ORR contact details.)

Primary legislation, subordinate legislation, other regulation and treaties

For primary legislation, other regulation and treaties requiring a RIS, the draft RIS must be circulated with the draft submission/proposal for the information of departments/agencies. The RIS must also accompany the relevant Cabinet submission or letter to the Prime Minister seeking approval for the legislation/treaty. Where legislative or regulatory action does not require policy approval external to the portfolio — for example, quasi-regulation agreed by a Minister — and where such regulation impacts on business and requires a RIS, the relevant Minister should advise

the Prime Minister of his/her intention to implement the proposal, attaching a draft RIS to his/her letter.

A consultation statement explaining the consultation processes undertaken and the views elicited from the main affected parties must be included in the RIS.

In the case of Cabinet submissions, the draft RIS will take the form of an attachment lodged separately with the Cabinet Secretariat, in accordance with the procedures for Cabinet submissions and memorandums.

A RIS should also be prepared for subordinate legislation (whether new or amended) that affects business or restricts competition. In its current form, the Legislative Instruments Bill 1998 specifies that a Legislative Instrument Proposal (LIP) — effectively equivalent to a RIS in all but name — must be submitted with all subordinate legislation which impacts on business, and be certified by the ORR. (RISs for legislative instruments will be called LIPs six months after commencement of the legislation.)

A RIS for new primary legislation and subordinate legislation (including amendments) will be included in the explanatory memorandum (for primary legislation) and explanatory statement (for tabled subordinate legislation). Modified RISs for taxation legislation (including amendments) will be included in the explanatory memorandum. RISs for treaties will be tabled along with the National Interest Analysis.

RISs must be of a standard suitable for publication in explanatory material. RISs for non-disallowable subordinate legislation and new or amended quasi-regulation should be available to affected groups and individuals and, ideally, be published on the internet.

There is scope for draft RISs to be modified after Cabinet consideration where, for example, Cabinet considers that the level of analysis is inadequate or where a draft RIS refers to confidential information. However, such changes must be made in consultation with the ORR. Revised final RISs must be circulated to all coordinating departments.

The final RIS to be tabled with explanatory material should be called the ‘RIS’, to distinguish it from earlier *drafts* of the RIS.

Treaties

Treaties which are likely to involve domestic regulations affecting business or restricting competition are subject to RIS requirements. A draft RIS should accompany the Cabinet submission or letter to the Prime Minister when policy approval is sought to enter treaty negotiations. At this early stage, a draft RIS should focus on the nature of the problem being addressed and the objectives of the proposed treaty. At a later stage, when endorsement is sought to sign the final text of a treaty, the draft RIS would

need to include analysis of the likely impacts on different groups within the Australian community.

When the treaty is tabled in the Parliament, a RIS should accompany the National Interest Analysis. Furthermore, when domestic legislative changes are made in order to implement the treaty, a RIS is also required except where the domestic legislation repeats or adopts the terms of all or part of an instrument for which the treaty provides.

On occasion, authority to enter treaty negotiations may be based only on the agreement of a Minister or group of Ministers, without policy approval from Cabinet or the Prime Minister being sought. In these instances, departments — in consultation with the ORR — must assess whether the proposed treaty could involve regulation that will affect business or restrict competition. If such effects are likely, the department should write to the Prime Minister seeking policy approval to enter negotiations and attaching a preliminary RIS. Further policy approval should be sought from the Prime Minister to finalise a treaty at the end of the negotiation process and an updated draft RIS provided.

In the case of template treaties in the areas of Comprehensive Taxation, Investment Promotion and Protection, Bilateral Aviation and International Film Co-production, the ORR should be consulted prior to entering into negotiations in order to determine whether the particular circumstances warrant a RIS. This requirement reflects the fact that the nature of the impact of these types of template treaties can vary significantly, depending on the other party. Treaties based on other existing template agreements are unlikely to affect business and so would not normally require a RIS.

The objective of the RIS is to aid decision-making processes and is in addition to NIA requirements. Details about RISs and treaties are also included in the Department of Foreign Affairs and Trade (DFAT) document *Negotiation, Conclusion and Implementation of Treaties*. Further information can also be obtained from the ORR.

Trade Impact Assessment (TIA)

The Government has decided that a Trade Impact Assessment (TIA) should be included in RISs for all proposals that have a *direct* bearing on export performance. The TIA should summarise the impact of regulatory options and proposals on exporters and assess the overall impact on Australia's international trade. Please contact the Assistant Secretary, Trade and Economic Analysis Branch, Department of Foreign Affairs and Trade with queries as to when a TIA is required.

Ministerial Councils and national standard setting bodies

The Council of Australian Governments (COAG) has agreed that a RIS must be prepared for any regulations that are to be considered by Ministerial Councils or national standard setting bodies. The RIS requirements for Ministerial Councils and national standard setting bodies — including the role of the ORR — are included in the

COAG endorsed publication *Principles and Guidelines for National Standard Setting and Regulatory Action by Ministerial Councils and Standard-Setting Bodies* available on the website of the Department of Prime Minister and Cabinet.

This COAG requirement does not negate the need for a RIS to be prepared by Commonwealth departments, agencies and statutory authorities in accordance with RIS guidelines, prior to development of a Commonwealth negotiating position for a Ministerial Council or national standard setting body. However, this should not result in duplication because, in the majority of cases, a RIS which meets the Commonwealth RIS requirements outlined in this guide will also meet the COAG RIS requirements.

Under the COAG RIS guidelines, the ORR has a role in assisting Ministerial Councils and national standard setting bodies in the preparation of RISs. The ORR must be given forward notice that a RIS will be drafted. The draft RIS must be provided to the ORR for comment prior to a policy decision being made.

The ORR is required to report annually to the Committee on Regulatory Reform (CRR) — an officials' group that reports directly to COAG — about the compliance of Ministerial Councils and national standard setting bodies with the COAG RIS guidelines. Further information and clarification about the relationship between the COAG and Commonwealth RIS processes can be obtained from the ORR.

Consultation statement

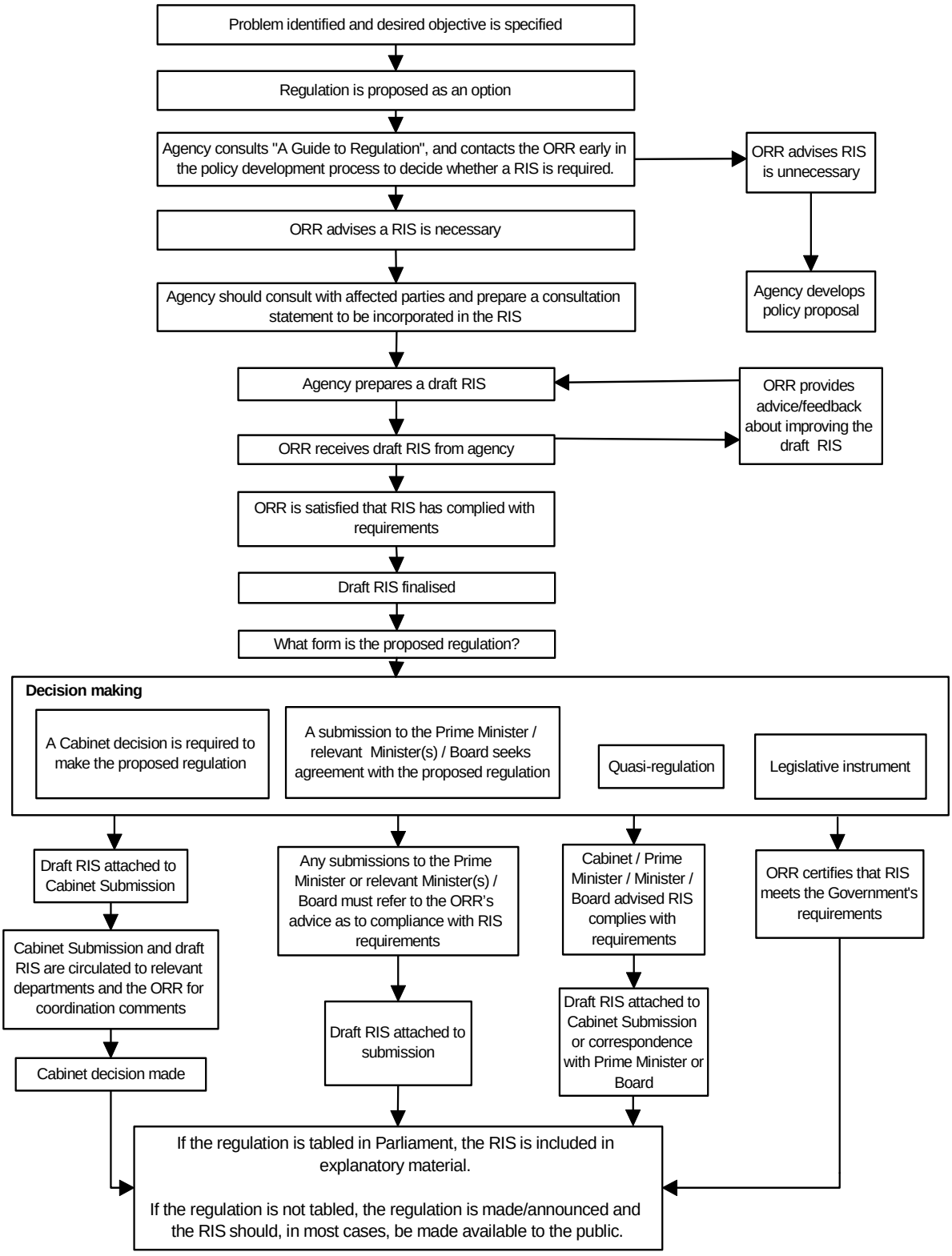
To ensure that relevant issues are examined, departments, agencies, statutory authorities and boards should identify the groups which may be affected by the options considered in a RIS. The cost-benefit analysis should document the likely impact of each option on each group, followed by an overall assessment of the impact of each option on the community.

Government policy is to ensure that those affected by proposed regulation are consulted at an early stage of the development of the regulation, with comments received in response to consultation to be taken into account in determining the most appropriate regulatory option.

Accordingly, in preparing the RIS for regulation which affects business, there must be consultation with groups likely to be affected by the options, unless full consultation is inappropriate (eg in the context of Budget measures or proposals going to Cabinet).

The purpose of consultation is to examine the costs, benefits and appropriateness of each option. Consultation on the draft regulation using a draft RIS may also be

Integrating 'best practice processes for regulation' with the policy making process



desirable. The level of consultation will depend on the significance and impact of the relevant regulation. A consultation statement will be included in the RIS, detailing the consultation undertaken, or reasons why consultation was inappropriate.

The flow chart above identifies key processes to consider when developing a regulatory proposal.

Small business impact

The Government has asked the ORR to ensure that particular effects on small businesses of proposed new and amended legislation and any other regulation are made explicit in the RIS. The RIS should also give full consideration to the Government's objective — outlined by the Prime Minister in *More Time for Business* — of minimising the paperwork and regulatory burden on small business.

A.6 Role of the Office of Regulation Review (ORR)

When RISs are required, the Government has decided that they must be examined by the ORR, which is part of the Productivity Commission. In the case of primary legislation, treaties, subordinate legislation and other regulation, the ORR provides advice to the relevant decision maker such as Cabinet, the Prime Minister/Minister(s) or board — and, as necessary, the Assistant Treasurer — on the adequacy of the RIS. Box D.3 (see page D19) provides information about the criteria used by the ORR to determine whether the analysis contained in a RIS is adequate.

In the case of minor policy proposals and quasi-regulation (which may be agreed between the responsible Minister and/or the Prime Minister or Board), the relevant department or agency will need to consult with the ORR as to whether a RIS is required.

The ORR's role in relation to regulation review and reform by Ministerial Councils and national standard setting bodies is set out in the COAG endorsed publication *Principles and Guidelines for National Standard Setting and Regulatory Action by Ministerial Councils and Standard-Setting Bodies*.

Departments, agencies and statutory authorities considering regulation that may impact on business are required to consult the ORR *at an early stage* in the policy development process. All RISs should be developed in consultation with the ORR. Draft RISs should be sent to the ORR for comment and advice. The ORR will advise departments and agencies when a draft RIS complies with the Government's requirements and contains an adequate level of analysis (see page D19).

The ORR will receive all Cabinet submissions proposing regulation or treaties. It is required to report to Cabinet, in its coordination comments, on compliance with the RIS requirements and on whether the level of analysis is adequate.

CHARTER FOR THE OFFICE OF REGULATION REVIEW (ORR)[2]

The role of the Office of Regulation Review (ORR) is to promote the Commonwealth Government's objective of effective and efficient legislation and regulations, and to do so from an economy-wide perspective. Its functions are to:

- advise the Government, Commonwealth departments, regulatory agencies and statutory authorities on appropriate quality control mechanisms for the development of regulatory proposals and for the review of existing regulations;
- examine Regulation Impact Statements (RISs) prepared by departments and agencies and advise on whether they meet the Government's requirements and whether they provide an adequate level of analysis;
- provide training and guidance to officials to assist them in meeting the requirements to justify regulatory proposals;
- report annually on compliance with the Government's Regulation Impact Statement guidelines, and on regulatory reform developments more generally;
- provide advice to Ministerial Councils and national standard setting bodies on COAG guidelines which apply when such bodies make regulations;
- lodge submissions and publish reports on regulatory issues having significant economic implications; and
- monitor regulatory reform developments in the states and territories, and in other countries, in order to assess their relevance to the Commonwealth.

These functions are ranked in order of the Government's priorities, and the ORR must concentrate its limited resources where they will have most effect.

Whilst maintaining an economy-wide perspective, the ORR is to focus its efforts on regulations which restrict competition or which affect (directly or indirectly) businesses. The ORR is to ensure that particular effects on small businesses of proposed new and amended legislation and regulations are made explicit, and that full consideration is given to the Government's objective of minimising the paperwork and regulatory burden on small business.

The ORR (together with the Treasury) is to advise the Assistant Treasurer in his role as the Minister responsible for regulatory best practice.

[2] In March 1997, the Government announced (in the Prime Minister's statement *More Time for Business*) that the ORR should have a charter outlining its role and functions.

In all other cases, the advice of the ORR on compliance with RIS requirements and (where applicable) the adequacy of analysis, will be included in the correspondence to the Prime Minister or in a submission to a Minister or other decision maker, such as a board or an official.

Recognising the importance of these best practice processes and the Government's commitment to improving regulatory culture, the Assistant Treasurer has the specific role of promoting regulatory best practice by ensuring that these regulation review and reform initiatives are implemented.

Departments and agencies should also consult with the ORR when developing terms of reference for reviews of existing legislation or regulations that impact on business.

The ORR conducts training programs to assist departments and agencies prepare RISs and fulfil other regulatory review and reform obligations. The ORR also reports publicly on compliance with the Government's regulation review and reform requirements. Departments and agencies are required to assist the ORR by providing relevant information. The reporting of compliance with RISs will also form part of the benchmarking strategy to enable the Government to measure its performance in regulation review and reform.

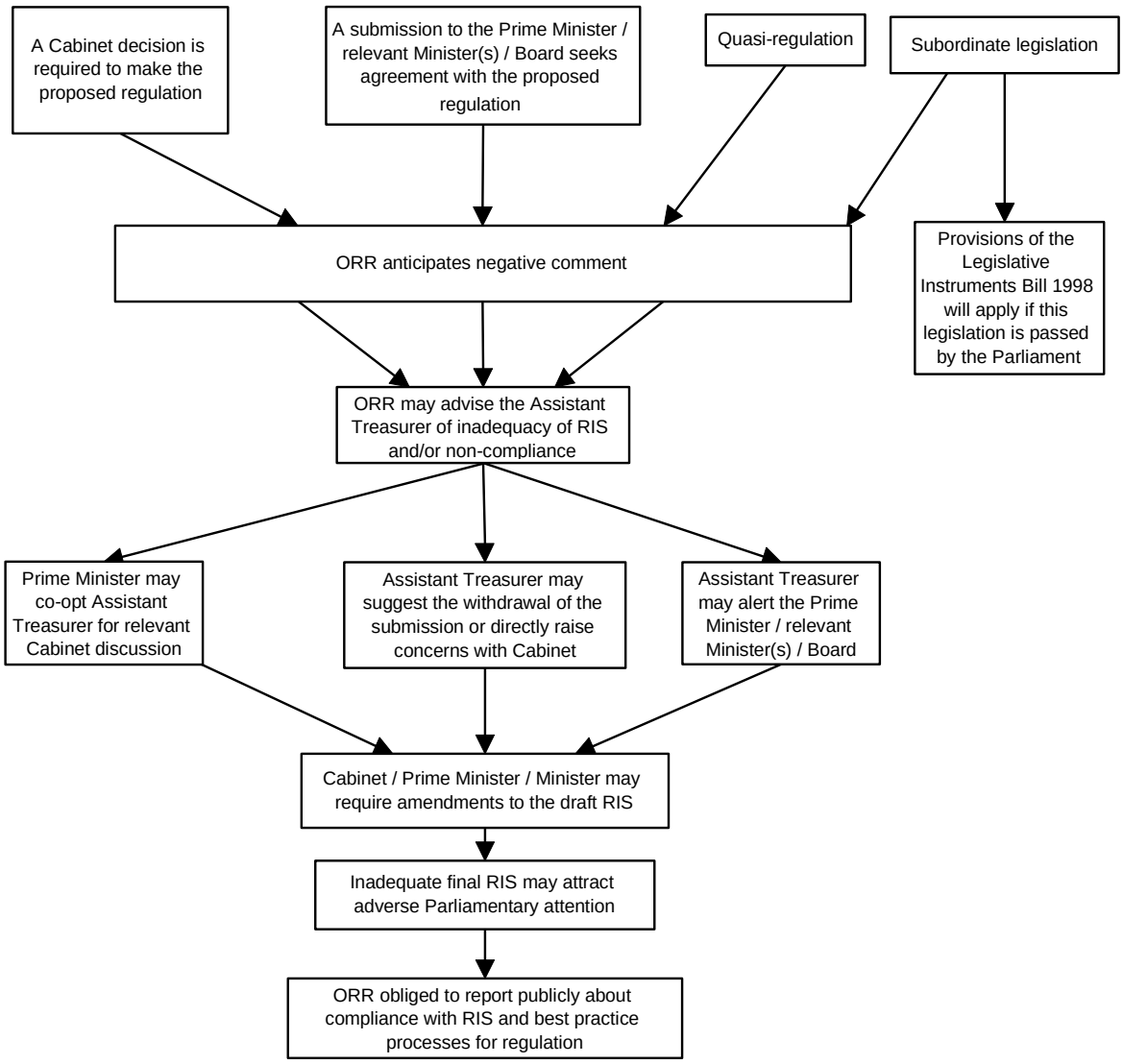
A.7 Consequences of non-compliance

The absence or inadequacy of a RIS does not affect the validity of regulation. Where a RIS is required but has not been prepared or is inadequate, it is up to the Cabinet/Government to determine whether to dispense with the RIS requirements, postpone policy approval until a RIS is done or require the subsequent preparation of a RIS.

If the ORR anticipates preparing a negative comment about a RIS, or has identified a policy proposal that has not been developed in accordance with the requirements of best practice processes for regulation, the Assistant Treasurer could draw the matter to the attention of the responsible Minister. In extreme cases where there are no overriding considerations — such as urgency — the Assistant Treasurer may suggest the withdrawal of the submission. In less extreme cases, the Prime Minister could co-opt the Assistant Treasurer for the relevant Cabinet discussion.

The ORR also reports publicly about compliance with the Government's regulation review and reform requirements in the Productivity Commission's annual report. In particular, the ORR will report on the number of Bills introduced into Parliament, the number of treaties, quasi-regulation and subordinate legislation made during the relevant financial year for which a RIS was required, noting the number and type of instances in which a RIS was prepared.

Consequences of non-compliance with best practices for regulation (including preparation of a RIS)



The flow chart identifies some of the likely consequences of non-compliance with best practice processes for regulation.

The Office of Small Business (OSB) — which is part of the Department of Employment, Workplace Relations and Small Business — has developed a range of Regulatory Performance Indicators (RPI) designed to monitor progress in improving the quality of Commonwealth regulation. The RPIs provide information on the extent to which departments and agencies are implementing measures to improve the regulatory environment. The RPIs also allow benchmarking of departmental and agency performance. The RPIs used by the OSB include measures of compliance with the Government's regulatory best practice and RIS policy. The first RPI report will relate to the 1998-99 financial year and will be published in late 1999.

In addition, the National Competition Council (NCC) monitors compliance of all jurisdictions — including the Commonwealth — with the *Competition Principles Agreement* (CPA). The NCC focuses on whether regulation restricts competition, whether the restriction on competition is the only way of achieving an objective and, if so, whether the restriction can be justified as being in the public interest. The NCC reports publicly each year on regulation review and reform processes and outcomes of each jurisdiction.

B: GUIDELINES FOR COMMONWEALTH REGULATION IMPACT STATEMENTS (RISs)

The following guidelines set out the information requirements for a Commonwealth Regulation Impact Statement (RIS), including the seven major elements of a RIS.

The RIS process is part of the Commonwealth Government's regulation review and reform policy, announced by the Prime Minister in *More Time for Business* (24 March 1997). The guidelines were endorsed by the Government in September 1997. They were subsequently revised (in this second edition of *A Guide to Regulation)* to include recent Government decisions on the application of regulatory best practice to quasi-regulation.

Commonwealth departments, agencies, statutory authorities and boards should consult with the Office of Regulation Review (ORR) for advice about how and when to use these RIS guidelines. Further information is readily available in Parts A, C, D and E. On the specific question of what criteria are used by the ORR to determine whether the analysis contained in a particular RIS is adequate, see Box D.3 on page D19 of this guide.

For taxation measures, a modified RIS is required— see page B9.

B.1 Problem or issue identification

This section of a RIS should specify the social, environmental or equity goal, or identify an economic or market failure problem. Information should be provided on the nature and magnitude of the problem — for example, on the likelihood of a detrimental event occurring and the consequences. Where an underlying market failure (such as lack of consumer information or social costs) is causing the problem, this should also be identified.

B.2 Specification of the desired objective(s)

The objective of the regulatory initiative should be specified. The objective should not be specified so as to align with (and thus pre-justify) the particular effects of the proposed regulation. Rather, it should be specified in relation to the underlying problem.

This section should also identify the pre-existing policy authority (if any) for a possible regulatory initiative: for example, a relevant Government decision or policy announcement.

B.3 Identification of options

This section should set out the alternative regulatory forms, options and instruments (including the proposed option) which could wholly or partly achieve the objective(s) specified in section B.2. Alternative regulatory forms include self-regulation, quasi-regulation, co-regulation and explicit government regulation (ie. "black letter law").

To provide guidance regarding the most appropriate regulatory form, the Government has endorsed a checklist which should be used by all Commonwealth officials considering proposals for new or amended regulation. This checklist is provided on pages D4–5 of this guide.

Self-regulation

Self-regulation is generally characterised by industry formulating rules and codes of conduct, with industry solely responsible for enforcement. In some cases governments may also be involved, by providing advisory information etc. Self-regulation should be one of the first options considered within the RIS framework. For further information about self-regulation, refer to section E.2 of this guide.

Quasi-regulation

Quasi-regulation refers to a wide range of rules or arrangements by which governments influence businesses to comply, but which do not form part of explicit government regulation, such as legislation/black letter law. Some examples of quasi-regulation include industry codes of practice, guidance notes, industry-government agreements and accreditation schemes. All government departments, agencies, statutory authorities and boards reviewing or proposing quasi-regulations that affect business should prepare a RIS. For further information about quasi-regulation, refer to section E.2 of this guide.

Co-regulation

Co-regulation typically refers to the situation where industry develops and administers its own arrangements, but government provides legislative backing to enable the arrangements to be enforced. This is known as 'underpinning' of codes, standards etc. Sometimes legislation sets out mandatory government standards, but provides that an industry code can override those standards. Legislation may also provide for government imposed arrangements in the event that industry does not develop arrangements of its own.

In 1997, the *Trade Practices Act 1974* (TPA) was amended to allow prescription of an industry or consumer code, or relevant provisions of such codes, as either mandatory or voluntary. The Government has decided that a number of prerequisites must be met before prescription of codes under the TPA can proceed. These are discussed in section E.2 of this guide.

Explicit government regulation (black letter law)

Explicit government regulation — which is sometimes referred to as "black letter law" — refers to primary or subordinate legislation. Explicit government regulation is the most commonly used form of regulation. While it can have a number of advantages when compared to other forms of regulation, there are also several important disadvantages associated with its use. For further information about the strengths and weaknesses of explicit government regulation, refer to section E.2 of this guide.

Alternative instruments

Within each form of regulation a number of alternative instruments can often be used. Alternative instruments (only some of which will be relevant for a particular type of regulatory form) may include:

- no specific action (ie rely on the market in conjunction with existing general liability laws (negligence or no fault) and insurance laws);
- information and education campaigns (including product labelling or media campaigns);
- market-based instruments (including taxes, subsidies, tradeable permits, and performance bonds);
- tradeable property rights;
- pre-market assessment schemes (such as listing, certification and licensing);
- post-market exclusion measures (such as bans, recalls, licence revocation provisions and 'negative' licensing);
- service charters;
- standards (including voluntary and regulatory, performance-based or prescriptive); and
- other mechanisms, such as public information registers, mandatory audits and quality assurance schemes.

For further information about alternative instruments, see section E.2.

Where voluntary standards are developed by Standards Australia and other third parties and are used for regulatory purposes, the Government has decided that it must be demonstrated in a RIS that standards are the most effective means of achieving the relevant policy objective. The RIS should also address the ramifications of industry forming the view that the standards will need to be complied with. For further information about standards see section E.2, page E19.

Alternative compliance mechanisms or enforcement regimes

As well as regulatory options and instruments, in some cases alternative compliance and enforcement strategies should be identified. These can include:

- administrative versus civil versus criminal sanctions;
- corporate versus director liability;
- the desirability of risk-based enforcement strategies; and
- the desirability of enforcement pyramids (ie warnings for initial or low-level breaches, fines for subsequent and/or high level breaches, leading to licence suspension or revocation as ultimate sanctions).

For further information about compliance and enforcement mechanisms see section E.2.

B.4 Assessment of impacts (costs and benefits) of each option

This section should analyse the benefits and costs of the options, including any restrictions on competition identified in section B.3, both for different groups within the community and for the community as a whole. Where possible, quantitative measures — such as financial and economic costs and benefits — should be identified and compared.

However, the analysis should not be restricted to tangible or monetary items and, where applicable, should also include possible changes in environmental amenity, health and safety outcomes, and other non-monetary outcomes.

Where government action seeks to reduce the risk of a detrimental event occurring, this section should outline the associated costs and benefits.

Impact group identification

The groups likely to be significantly affected by the regulatory initiative should be separately identified. These groups should be broken down into sub-groups where the initiative will have different effects on those sub-groups. Group and sub-group distinctions may include:

- government, business and consumers;
- within the government category, Commonwealth, state/territory, or local governments;
- within the business category, big, medium and small businesses, and importers, exporters and/or firms supplying the local market;
- within the consumer category, groups with different levels of information and/or abilities to process information;
- groups in different geographical areas (eg urban/rural) or different states/territories; and

- groups with different age, language, physical, cultural, gender, family or income/wealth characteristics.

Assessment of costs

Estimates of the cost to *government* of introducing the new regulatory process or amendment, and the other options, should be given, including where relevant:

- numbers and levels of staffing;
- salary costs (including on-costs);
- costs of other relevant items such as any special advertising, accommodation, travel; and
- enforcement costs.

The sources of revenue against which the costs will be charged should be included: for example, general Budget appropriation or fees. Estimates of revenue from any licences, fees or related charges in the regulation process should be given. Where possible, a net cost to government should be indicated.

Estimates of costs to *businesses* — including small business — affected by the regulatory initiative should also be given. These costs might derive from:

- 'paper burden' or administrative costs to businesses associated with complying with and/or reporting on particular regulatory requirements;
- standards — including voluntary standards — being incorporated into regulation, thus becoming regulatory standards which could be complicated and/or unnecessarily high;
- licence fees or other charges levied by government;
- changes likely to be required in production, transportation and marketing procedures;
- shifts to alternative sources of supply; and
- delays in the introduction of goods to the marketplace and/or restrictions in product availability.

Estimates of costs to *consumers* are also required. These may derive from:

- higher prices for goods and services;
- reduced utility (quality, choice etc) of goods and services;
- delays in the introduction of goods to the marketplace and/or restrictions in product availability; and
- more difficult or more expensive options for seeking redress.

An assessment of the likely costs to the *community* as a whole should be provided.

Where possible, the various costs should be quantified. Where quantitative data about costs are unavailable, there are various estimation techniques that can be used. Where it is not possible to prepare a quantitative estimate, a qualitative assessment of costs and benefits should be undertaken.

When assessing aggregate costs, it is important to avoid double-counting. For example, if a regulation is likely to increase business costs and it is expected that businesses will pass these costs on to consumers in the form of higher prices, this cost item should be noted as impacting on business and consumers, but counted only once in an assessment of aggregate costs.

Assessment of benefits

Information on the benefits of the options to governments, consumers, business, other affected groups and to the community at large should be identified. Examples of such benefits, some of which may not be quantifiable, could derive from:

- firms being able to take greater advantage of economies of scale;
- reductions in compliance costs for business and administrative costs for government;
- reductions in costs or prices resulting from removal of restrictions on competition;
- improvements in product and service quality;
- availability of a wider range of products and services;
- reductions in workplace accidents and improvements in public health (and Medicare cost savings consequent upon them);
- improvements in environmental amenity; and
- improvements in the information available to business, the workforce, consumers or the government.

Restrictions on competition

Where a particular option restricts competition, the RIS must address additional issues in the context of the cost-benefit assessment in order to meet the Commonwealth's commitments under the inter-governmental *Competition Principles Agreement* (CPA), agreed by COAG in April 1995. In particular, the RIS must examine whether the option restricts competition and whether it is the only way of achieving the desired objective.

The RIS should not recommend an option which restricts competition unless it is demonstrated that the benefits of the restriction to the community as a whole outweigh the costs; and the desired objective can be achieved only by restricting competition.

Other issues to consider

Effects on small business

The RIS should include a sub-section that assesses the impact of each option on small business compliance costs and paperwork burden.

Effects on trade

Where a proposed regulation has a direct bearing on export performance, a Trade Impact Assessment (TIA) should be incorporated into the RIS. The TIA should summarise the impact of regulatory options and proposals on exporters and assess the overall impact on Australia's international trade. Please contact the Assistant Secretary, Trade and Economic Analysis Branch, Department of Foreign Affairs and Trade with queries as to when a TIA is required.

B.5 Consultation

A consultation statement will be incorporated into the RIS detailing the consultation undertaken and a summary of the views elicited from the main affected parties, or specify reasons why consultation was inappropriate (eg in the context of Budget measures or proposals going to Cabinet). Relevant individuals and groups may include:

- Commonwealth Ministers, departments, agencies, statutory authorities or boards;
- state, territory and local governments, particularly where the regulatory process arises from negotiations between different levels of government and/or involves overlapping responsibilities;
- business, consumers, unions, environmental groups and other interest groups which will be affected by the regulatory process; and
- other groups or sub-groups identified above in section B.4.

B.6 Conclusion and recommended option

This section should state what the preferred option is and why this option was accepted and other options rejected.

B.7 Implementation and review

This section should state how the regulation should be administered, implemented and enforced. It should also state how the recommended option will be monitored, with a view to its amendment or removal should the circumstances which led to its

introduction change. The information should include an assessment of the feasibility of:

- a ‘sunset’ clause;
- on-going arrangements for consulting with the interest groups affected;
- provision for regular review; and
- provision for regular reporting to the public, such as in an agency’s annual report.

This section should also discuss the administrative simplicity of the proposal, including:

- a specific sub-section that assesses the impact on small business and ways to minimise compliance costs and paperwork burden associated with regulation;
- the feasibility of ‘one stop’ facilities for the regulation. This may in some cases involve consideration of the practicability of joint facilities or offices with another Commonwealth agency, with an appropriate state or local government agency, or even with a related private agency;
- the feasibility of the administrative procedure being carried out by existing teams of staff in other departments or agencies; and
- whether it is appropriate to have an in-built authority to waive or modify the regulation in certain circumstances, and provide for an adequate appeal process.

B(TAX): GUIDELINES FOR COMMONWEALTH REGULATION IMPACT STATEMENTS (RISs) FOR TAXATION MEASURES

The RIS process is part of the Commonwealth Government's regulation review and reform policy announced by the Prime Minister in *More Time for Business* (24 March 1997). These guidelines were endorsed by the Government in September 1997.

The following guidelines set out the information requirements for a Commonwealth Regulation Impact Statement (RIS) for taxation measures. They apply only to taxation measures. Departments and agencies considering taxation measures should contact the Office of Regulation Review (ORR) for information about how and when to use the RIS guidelines. Reference should also be made to the Australian Taxation Office (ATO) document (published in September 1998) *ATO Guidelines for the Preparation of Regulation Impact Statements (RIS)* which provides further information and advice about tax RISs.

The full RIS process is not suitable for taxation measures because:

- prior public consultation on taxation measures could release sensitive information which could be used by taxpayers to engage in tax avoidance or minimisation schemes. This could compromise revenue collection and the Government policy responses to tax matters which seek to close off such schemes;
- many taxation measures are announced in the Budget or by way of special Ministerial statements. Prior public consultation on taxation measures is likely to compromise the Budget process or inhibit the usefulness of such Ministerial statements;
- there can be difficulties in identifying the ultimate bearer of a tax, and that can place constraints on the public consultation process; and
- review processes for taxation measures are already in place. A key role of the Treasury and the Australian Taxation Office (ATO) is to keep the tax system as a whole under continuous review. Taxation measures are difficult to review in isolation, because it is the interaction of all taxation measures in the taxation system that is important.

The Small Business Deregulation Task Force noted that it is not the need to pay tax to which small business objects, but rather the burden imposed by taxation compliance. Recognising these concerns, the RIS required for taxation proposals will examine the options for ensuring compliance with taxation proposals designed to meet Government policy objectives, and the costs and benefits of each alternative implementation option where more than one is available. This will ensure that compliance cost and other considerations are fully taken into account by the Government.

A RIS for taxation measures — which does not include sensitive information which may compromise the Government's policy responses to taxation matters or reveal the content of Cabinet consideration of policy options — will be included in the explanatory memorandum tabled in the Parliament with the relevant tax legislation. The four main elements of such RISs are described below.

The Office of Regulation Review (ORR) will be responsible for examining and advising on the adequacy of RISs for taxation measures.

1 Specification of the policy objective(s)

The objective of the taxation measure outlined by the Government should be specified. Any authority to implement the taxation measure (eg a Government policy statement) should also be identified. (Though this obviously excludes references to Cabinet documents or related sensitive information).

2 Identification of implementation options

This section should set out the options for implementing the Government's policy decision.

In identifying options for implementing the taxation measure, consideration should be given to:

- whether the design of the tax measure should include transitional arrangements;
- whether the design of the tax measure incorporates tiered thresholds;
- alternative administrative arrangements within the ATO;
- options for ensuring taxpayer compliance;
- the need to provide taxpayers with detailed information or other supporting material; and
- collecting additional information from taxpayers so as to, for example, improve the ATO's capacity to estimate the impact of a particular measure on taxpayers, assist in revenue estimates and/or monitor tax compliance.

Sometimes there will be only one implementation option which partially or fully achieves the policy intent of the taxation measure. In such cases, this option should be discussed, along with any associated changes in compliance and ATO administration costs.

3 Assessment of impacts (costs and benefits) of each implementation option

This section should analyse the costs and benefits of the implementation options identified in section 2, both for the Government and different groups within the community. Financial and economic costs and benefits should be considered.

Impact group identification

The groups likely to be significantly affected by the regulatory initiative should be separately identified. These groups should be broken down into sub-groups where the initiative will have different effects on those sub-groups. Group and sub-group distinctions may include:

- government, business and consumers;
- within the government category, Commonwealth, state/territory, and local governments;
- within the business category, big, medium and small businesses, and importers, exporters and/or firms supplying the local market;
- within the consumer category, groups with different levels of information and/or abilities to process information;
- groups in different geographical areas (eg urban/rural) or different states/territories; and
- groups with different age, gender, family or income/wealth characteristics etc.

Section 16 of the *Income Tax Assessment Act 1936* prohibits releasing information on individual taxpayers. Therefore, for the purposes of the RIS included in the explanatory memorandum, there can be only broad categorisation of affected parties.

Assessment of costs

Estimates of the **administration cost to government** of each implementation option should be given, including where relevant:

- numbers and levels of staffing;
- salary costs (including on-costs);
- costs of other relevant items such as any special advertising, accommodation, travel; and
- enforcement costs.

The sources of revenue against which the costs will be charged should be included, for example, general Budget appropriation or fees. Estimates of revenue from any cost recovery process should be given. Where possible, a net administration cost to government should be indicated.

Estimates of **compliance costs** to businesses/taxpayers affected by the implementation option should also be given. This should include an assessment of the impact of each option on small business compliance costs and paperwork burden.

These costs might derive from 'paper burden' or administrative costs to businesses associated with complying with and/or reporting on particular regulatory requirements.

Where appropriate, **other impacts on business/taxpayers** of the implementation options, but not extending to those associated with the underlying policy measure, would be identified. Such impacts might include, for example:

- resource allocation (eg changes likely to be required in production, transportation and marketing procedures, or shifts to alternative sources of supply);
- impacts on international trade; and
- delays in the introduction of goods to the marketplace and/or restrictions in product availability.

Where possible, the various costs should be quantified. Where quantitative data are unavailable, a qualitative assessment of costs should be undertaken. When assessing aggregate costs, it is important to avoid double-counting.

Assessment of benefits

Information on the benefits of the alternatives to affected groups and/or to the community at large should be identified for each option. Such benefits could derive from:

- government revenues;
- enhancing the integrity of the taxation system; and
- administrative simplicity.

Where possible, the various benefits should be quantified. Where quantitative data are unavailable, an assessment of qualitative benefits should be undertaken. When assessing aggregate benefits, it is important to avoid double-counting.

Other issues to consider

Consultation

As noted in the introduction, prior consultation on taxation measures may not be appropriate in many cases. However, consultation may have occurred during the drafting of tax legislation required to give effect to the Government's decision.

Where consultation has occurred, general details of the consultation process should be included in the RIS, including a summary of the main affected parties and their views. Individual taxpayers should not be identified.

4 Conclusion and recommended option

This section should state the preferred option for implementing the Government's policy decision. If there are alternative options, the reason(s) why the preferred option was accepted and others rejected should be explained.

This section should note that the Treasury and ATO will monitor this taxation measure, as part of the whole taxation system, on an ongoing basis. In addition the ATO has consultative arrangements in place to obtain feedback from professional and small business associations and through other taxpayer consultation forums.

C: RIS CHECKLIST

This 'RIS checklist' presents a simple and brief picture of the issues that should be addressed in a RIS. In some cases not all items will be relevant, while in others a more detailed analysis of some items will be required. For example, the RIS Guidelines for taxation measures draw on only some of the items referred to here.

Where proposed regulations restrict competition, departments and agencies must ensure that the requirements of the *Competition Principles Agreement* (CPA) are embodied in the RIS. Furthermore, where a proposed regulation might have a direct bearing on international trade or export performance, departments/agencies should consult with the Department of Foreign Affairs and Trade (telephone 02 6261 3521) to ensure that the RIS analysis meets the information requirements of a Trade Impact Assessment (TIA).

A detailed explanation and discussion of each checklist item is provided in the following section (eg Section D) of this Guide.

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C.1 Problem D1

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C.2 Objectives D3

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C.4 Impact analysis (costs and benefits) of each option D6

Item 1	Who is affected by the problem and who is likely to be affected by its proposed solutions?	D7
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Item 3	Identify and categorise the expected impacts of the proposed options as likely benefits or likely costs.	D9
Item 4	Determine which groups are likely to experience these benefits and costs and what the extent of their impacts are likely to be. Quantify these effects where possible.	D9
Item 5	Identify distributional effects and attribute these to the groups affected.	D11
Item 6	Identify the data sources and assumptions used in making these assessments.	D12
Item 7	Summarise outcomes for each option examined.	D11

C.5 Consultation D13

Item 1	Who are the main affected parties?	D13
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C.6 Conclusion and recommended option D15

Item 1	Provide a brief summary of the assessment of each option.	D15
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C.7 Implementation & review D15

Item 1	How will the preferred option be implemented?	D15
Item 2	Is the preferred option clear, consistent, comprehensible and accessible to users?	D16
	Is it sufficiently flexible to adapt to various situations and circumstances?	D16
Item 3	What is the impact on business, including small business, and how will compliance and paper burden costs be minimised?	D17
Item 4	How will the effectiveness of the preferred option be assessed? How frequently?	D19
Item 5	If the preferred option takes the form of regulation, is there a built-in provision to review or revoke the regulation after it has been in place for a certain length of time?	D19

C.8 Adequacy criteria for RISs D18

Box D.3	Adequacy criteria for RISs	D19

D: PREPARING A RIS

This section follows the same structure as the 'RIS checklist' (Section C). It provides details and some examples of issues that should be considered when addressing each item contained in the 'RIS checklist'.

In some cases, two or more items are grouped together, with the subsequent discussion addressing those items together.

D.1 Problem

Item 1 What is the problem being addressed?

Item 2 Why is government action needed to correct the problem?

To design appropriate solutions to a problem, the problem must be clearly specified. If it is not clearly identified, over-regulation may result or the problem may not be solved. Specification of the problem should include detailing its nature and size.

It is at this first stage of the regulatory development process that consultation should begin (see section D.5).

The impact (major, moderate, minor or insignificant) of the problem should also be estimated. If the problem has an insignificant or minor impact, then it is likely that there will be no case for government action or regulation. If the impact is larger, preparation of the RIS will help indicate whether government action is necessary and beneficial.

When identifying the nature and size of the problem, reference should be made to empirical evidence as well as perceptions of the problem. This includes assessing the worst outcome that could occur if a 'do nothing' approach were taken. If the problem involves risk to the public, workers or the environment, the extent of hazard and the risk that it will occur should be identified (see section E.3 of this guide for an introduction to risk analysis).

As government action is not costless, there should be an onus on the department/agency proposing action to describe why Government involvement is required to deal with the particular problem identified.

Government action has often been justified in cases of 'market failure'. Market failure refers to situations of inadequate information; public goods or externalities etc. (see section E.1 of this guide).

The precise nature of the market failure should be identified. For instance, the problem may be the failure of irrigators and other water users to take account of environmental costs of water use, such as salinity, in their decision making.

Box D.1: Checklist for the identification of problems and risks

STEP 1 - Identify the problem

Clearly define the problem, for example:

- lack of competition;
- human health and safety risks;
- damage to the physical environment;
- unacceptable industry behaviour/unfair trading practices;
- insufficient or misleading market information; or
- unacceptable transactions costs for consumers.

Are there deficiencies in the existing regulatory system which, if corrected, might fix the problem?

Is the problem one for government or of purely private interest?

STEP 2 - Assess the risk

What is the risk of the problem occurring?

How widespread is it - local, state, national, international?

Is it recurring?

Is it significant?

STEP 3 - Assess the consequences of no action

List the consequences of no action.

Can relying on the market in conjunction with the general application of existing laws solve the problem? If not, why not?

Will the market self correct within a reasonable timeframe?

Can a regulatory scheme improve the situation?

The existence of market failure indicates that there may be a role for government action to make the community better-off.

To provide guidance regarding the clear identification of problems, risks and consequences of no action, the Government has endorsed a checklist which should be used by all Commonwealth officials considering proposals for new or amended regulation. This checklist is provided in Box D.1.

D.2 Objectives

Item 1 What are the objectives of government action?

This step should identify what outcomes, goals or targets are sought in relation to the identified problem. A common error is to confuse the desired final outcome of the proposal with the means of obtaining it.

Example: ***Do not confuse 'ends' with 'means' when setting an objective***

An objective of government health policy may be 'to reduce the health care costs associated with smoking'. This objective differs to an objective of 'banning smoking in certain venues' which may be only one means of attaining the first, broader objective.

The objective should also not pre-justify a preferred solution, but rather, should allow for an examination of alternative solutions to the underlying problem.

The objective should be clear, concise and as specific as possible. It should be specified broadly enough to allow consideration of all relevant alternative solutions, but should not be so broad or general that the range of alternatives becomes too large to assess, or the extent to which the objective has been met becomes too hard to establish.

If applicable, a distinction should be made between the primary and subsidiary objectives of the proposal.

If outcomes are subject to constraints, such as that they must be achieved within a certain time frame, then these should also be clearly specified within the statement of objectives.

Item 2 Is there a regulation/policy currently in place? Who administers it?

The characteristics of existing regulations and the responsible regulatory organisation(s) should be identified, along with relevant government policy.

If there is an authoritative basis for the proposal to review or amend regulations, for example, a relevant Cabinet Minute or governmental policy announcement, it should be identified.

D.3 Options

The RIS should test the effectiveness and appropriateness of alternative non-regulatory and regulatory measures for achieving the stated objectives and should help departments and governments select the most effective and efficient approach. The measure adopted should be carefully targeted at the identified problem so that it does not impact unduly on areas that it was not designed to address.

As it is unreasonable and too costly to assess every possible alternative solution to a problem, it is necessary to consider in detail only the most feasible options. However, the reasons for rejecting options without detailed analysis should be clearly stated. Section D.4 discusses how to apply a cost/benefit analysis to options.

To provide guidance regarding the most appropriate regulatory form the Government has endorsed a checklist. This checklist is provided (below) in Box D.2. The Government has decided that this checklist should be used by all Commonwealth officials considering proposals for new or amended regulation.

Box D.2: Checklist for the assessment of regulatory forms for their suitability

(1) Self-regulation should be considered where:

- there is no strong public interest concern, in particular, no major public health and safety concern;
- the problem is a low risk event, of low impact/significance; and
- the problem can be fixed by the market itself. For example, there may be an incentive for individuals and groups to develop and comply with self-regulatory arrangements (industry survival, market advantage).

The likelihood of self-regulatory industry schemes being successful is increased if there is:

- adequate coverage of industry concerned;
- a viable industry association;
- a cohesive industry with like minded/motivated participants committed to achieve the goals;
- evidence that voluntary participation can work – effective sanctions and incentives can be applied, with low scope for the benefits being shared by non-participants; and

- a cost advantage from tailor-made solutions and less formal mechanisms such as access to quick complaints handling and redress mechanisms.

(2) Quasi-regulation should be considered where:

- there is a public interest in some government involvement in regulatory arrangements and the issue is unlikely to be addressed by self-regulation;
- there is a need for an urgent, interim response to a problem in the short term, while a long-term regulatory solution is being developed;
- government is not convinced of the need to develop or mandate a code for the whole industry;
- there are cost advantages from flexible, tailor made solutions and less formal mechanisms such as access to a speedy, low cost complaints handling and redress mechanisms; and
- there are advantages in the government engaging in a collaborative approach with industry, with industry having substantial ownership of the scheme. For this to be successful, there needs to be:
  - a specific industry solution rather than regulation of general application;
  - a cohesive industry with like minded participants, motivated to achieve the goals;
  - a viable industry association with the resources necessary to develop and/or enforce the scheme;
  - effective sanctions or incentives to achieve the required level of compliance, with low scope for benefits being shared by non-participants; and
  - effective external pressure from industry itself (survival factors), or threat of consumer or government action.

(3) Explicit government regulation should be considered where:

- the problem is high risk, of high impact/significance, for example a major public health and safety issue;
- the government requires the certainty provided by legal sanctions;
- universal application is required (or at least where the coverage of an entire industry sector or more than one industry sector is judged as necessary);
- there is a systemic compliance problem with a history of intractable disputes and repeated or flagrant breaches of fair trading principles and no possibility of effective sanctions being applied; and
- existing industry bodies lack adequate coverage of industry participants, are inadequately resourced or do not have a strong regulatory commitment.

The checklist is intended to supplement the RIS process by providing additional information to help determine which regulatory forms are worth considering, prior to the more formal testing of the effectiveness and likely costs and benefits of different regulatory options which is undertaken in a RIS.

D.4 Impact analysis

The previous section (D.3) discussed identification of feasible options. In this section, the advantages (labelled 'benefits') and disadvantages (labelled 'costs') of each of the most feasible options proposed should be considered carefully.

The main requirement of this section is that a comprehensive assessment of each option's expected impact is prepared. The objective should be to choose the most appropriate and cost-effective option and also to provide readily accessible evidence to support a decision. Ideally, objectives should be pursued only if the benefits of doing so exceed the costs.

The level of detail required for the impact analysis will depend on the problem identified, the information available, the expected net impact of the option proposed and the costs of preparing the impact analysis.

Qualitative, quantitative and scientific evidence all have a role to play in the impact analysis of a particular option.

As a minimum requirement, a qualitative assessment of all the expected effects of a proposed option is expected. In addition, quantification of effects can provide useful information and help demonstrate the need for regulatory action. This type of information is required wherever possible.

In some cases, a comprehensive and detailed qualitative analysis, supported by scientific and quantitative evidence where it is available or readily obtained, would suffice. This is particularly so if it is clear, on an initial examination of expected impacts, that the option is expected to result in a significant net benefit. In these cases, more detailed quantitative analysis may only confirm initial results and may not warrant the additional time and expense. This is particularly so if the costs of preparing a comprehensive impact analysis are large.

However, a more detailed and comprehensive quantitative analysis would be useful if, on initial examination:

- options appear to result in similar levels of benefits and costs, so that no one proposed solution is clearly superior to other alternatives;
- there is a possibility that an option could impose a net cost on the community; or
- the proposed solution is expected to have a large or far-reaching impact on the economy.

In these cases, a more careful consideration of the option's effects would be required. The ORR may be consulted for advice on cases where additional quantitative analysis of a particular option appears to be necessary.

In addressing the following items of an impact analysis, consultation with other departments, business and the community will provide useful information on the options' effects and their magnitudes.

Item 1 Who is affected by the problem and who is likely to be affected by its proposed solutions?

An impact analysis will be most useful if it is comprehensive. To ensure this, **an economy-wide perspective must be taken**. This means that all groups affected by the problem and its proposed solution must be identified, including those directly affected by the options and those indirectly affected. In addition, the effects on the community as a whole must be assessed.

In the past, some departments/agencies have perceived regulation impact statements as 'business impact statements'. While an impact on business is the trigger for preparing a RIS, the impact of an option on all affected groups needs to be considered and compared when an impact analysis is prepared.

Groups may initially be distinguished as: consumers, business and government. These groups may then need to be further sub-divided, for instance:

- within the consumer group according to geographical location, age, cultural background or levels of information held;
- within business along industry or sectoral lines; according to size or whether the business imports or exports; and
- within government as to Commonwealth, state/territory or local government level, or according to department or agency.

The extent and type of sub-groups of relevance will vary according to the problem and option being assessed.

Item 2 How will each proposed option affect existing regulations and the roles of existing regulatory authorities?

This item recognises that new proposals must co-exist with the existing stock of regulations and requirements. Responses to this item will help ensure that proposals do not conflict with or duplicate existing regulations and requirements, indicate whether the application of existing requirements could solve the identified problem or whether amendment or repeal of other regulations and requirements will be necessary.

This is particularly applicable to those in Commonwealth regulatory bodies because the proposed solution may conflict with, or duplicate, existing regulations and requirements imposed by state/territory and/or local governments. Similarly, it may highlight areas where national consistency of requirements would be most suitable.

It is important, also, to recognise that the impact of a proposal on government is likely to extend beyond the proposing department or agency, in most cases, to other levels of government or other agencies. This may result, for example, if another department or another level of government is responsible for collecting information or for enforcing the proposal. As a proposal should aim to achieve its objectives at least cost to

government overall (just as it should aim to minimise the burden on the community as a whole), all impacts on government should be assessed.

Consideration must be given to the contribution that the proposed option would make to the **overall** burden of regulation on the community. When a new requirement is added to the existing stock of regulations, the effectiveness of other regulations may be reduced. This may occur simply due to the volume of regulations and requirements that exist — there is a limit to the number of regulations that business can comply with fully, just as there is a limit to the number of regulations that departments/agencies can enforce fully or effectively.

If a similar proposal, or problem, has been experienced interstate or overseas, it is useful to consider its impact on regulatory authorities in these cases. Others' experience may indicate approaches to the problem which have not yet been considered or may highlight advantages and shortcomings of options that are being considered.

Item 3 Identify and categorise the expected impacts of the proposed options as likely benefits or likely costs.

Item 4 Determine which groups are likely to experience these benefits and costs and what the extent of their impacts are likely to be. Quantify these effects where possible.

The responses to these items will form the most lengthy and detailed part of the RIS. The amount of detail that this section involves depends on factors such as: the significance of the proposal's effects; and time, resource and data constraints.

Benefits and costs are terms used to describe the positive and negative effects of a proposal. A benefit will include any item that makes any person better off, regardless of whether it can be easily measured or quantified.

A cost is any item that makes someone worse off or that reduces a person's sense of wellbeing. Cost items should include 'opportunities forgone' because a particular proposal has been adopted in place of another proposal.

EXAMPLE: ***Benefits of possible solutions****.*

Benefits to consumers may include: a reduction in pain and suffering; increased access to information; lower prices; improved safety of products, workplaces, services etc.

Benefits to business may include: a reduction in plant or property damage; a reduction in lost production time; reduced compliance costs; less anti-competitive behaviour in the market or greater regulatory transparency, certainty and predicability.

Benefits to government may include: streamlined regulatory processes and requirements; reduced monitoring and enforcement costs; higher levels of compliance.

Benefits to the community may include: improved environmental outcomes; safer workplaces; greater access to services or opportunities; more economical use of resources and higher economic growth; and an increase in the standard of living and quality of life.

Benefits and costs can be further classified as: allocative or distributional/transfer effects; direct or indirect effects and tangible or 'intangible' effects (see sections E.1 and E.2 for further information).

An impact analysis should be comprehensive and include all benefits and costs, not just those of a financial nature. Also included should be benefits and costs that are economic; those relating to resource allocation; those resulting from any reduction in risk; and administration or compliance costs.

EXAMPLE: ***Costs imposed by possible solutions****.*

Costs to consumers include: an increase in prices; a reduction in the variety of goods and services available or a reduced range of quality/price combinations; and a lower level of workplace safety.

Costs to business include: uncertainty for investment; restricted access to markets; higher input prices; the costs of establishing and maintaining administrative processes that enable the firm to comply with new requirements; purchasing or modifying existing machinery to comply with requirements; and increased complexity of regulations and accompanying uncertainty about how to adhere to regulations (see Section D7, Item 3 for detailed discussion of how to measure business compliance costs).

Costs to government may include: the one-off costs of establishing the infrastructure required to implement the proposal; and the on-going costs of collecting and processing information, inspecting premises and imposing sanctions.

Costs to the community might involve: an undesirable redistribution of income and wealth; reduced innovation; lower employment levels; and lower economic growth (which implies a lower standard of living).

To ensure that all impacts of a proposal are identified, it is useful to consider how the proposal is expected to impact on each group identified in Item 1.

A table, such as that below, may be useful for presenting this information.

Ideally the impact analysis in a RIS would quantify all the benefits and costs identified and a net benefit for each proposal would be calculated. This would allow for an easy comparison of options and easy identification of the option that yields the greatest net benefit or the least net cost to the community.

OPTION A

	BENEFITS		COSTS	
	Description	**Estimate**	**Description**	**Estimate**
Consumers				
Business				
Government				

In practice, such quantification is not always possible, nor is it always necessary. For instance, some items may be too difficult to quantify (this is particularly so for 'intangibles' such as enjoyment), or the availability of time or other resources may limit the amount of quantification that is possible. At times, quantification of all items may be superfluous as it is clear that a proposal will result in a significant net benefit for the community. In other cases, attempts to put values on all benefits and costs could involve false precision, be costly and reduce the RIS to a mechanistic process. That said, however, the onus of proof lies with the proponent of a regulation; some form of evidence must be produced to justify why a particular proposal has been recommended.

Some existing or proposed regulations and requirements restrict competition. For instance, licensing requirements will limit the number of people engaged in an occupation. This restriction in supply may allow existing practitioners to raise their prices. A similar situation might arise if only some producers of goods are entitled to use certain terms on their labels.

Where a particular option restricts competition, the RIS must address additional issues in the context of the cost-benefit assessment in order to meet the Commonwealth's commitments under the inter-governmental *Competition Principles Agreement* (CPA), agreed by COAG in April 1995. In particular, the RIS must examine whether the recommended/preferred option is the only way of achieving the desired objective. This is because the RIS should not recommend an option which restricts competition unless it is demonstrated that the benefits of the restriction to the community as a whole outweigh the costs; and the desired objective can be achieved only by restricting competition.

Item 5 Identify distributional effects and attribute these to the groups affected.

The distributional effects of a proposal are very important for determining whether the proposal is desirable. A proposal may result in a net benefit to the community, but

when its distributional effects are examined it may be deemed undesirable as significant benefits may go to a small number of people, while the costs may be borne by a large number or may be disproportionately borne by those who do not benefit at all.

EXAMPLE: ***The distributional effects of taxing leaded petrol***

Cars are an important source of lead emissions. Leaded petrol is taxed at a higher rate than unleaded petrol to hasten the switch away from cars using leaded petrol, and thereby reduce the levels of lead emissions. However, this policy has a distributional dimension. Older cars use leaded petrol and these are often owned by people on lower incomes. Additional taxes on lead may adversely affect some lower income groups.

In this case a balance needed to be struck between encouraging the switch to newer unleaded cars while not imposing significant costs on those least able to afford them. The Government's decision was to impose a two cent a litre additional tax on leaded fuel, rather than a tax of up to five cents a litre as had been advocated in some quarters.

Attention should be given to determining who 'wins' and who 'loses' if a particular option is adopted. Information on distributional effects can assist governments choose among options.

Item 6 Identify the data sources and assumptions used in making these assessments.

Data sources and assumptions made when conducting the impact analysis should be recorded so that they can be referred to at a later date when the proposal's effects are being assessed. This information should also be available so that assumptions can be altered to gauge how changing them might affect the desirability of the proposal.

Item 7 Summarise outcomes for each option examined.

This information could be presented in a table (see example of RIS summary) listing each alternative proposal examined and the main results.

An outline of the main assumptions underlying the assessments, and key variables that affect results should be repeated here.

EXAMPLE: ***RIS summary***

Objective: To reduce the level of household waste entering landfills

Alternative	**IMPACT ON**	**Likely benefit/ comment**

	Households	Business	Government	
Education/ persuasion	Low cost.	Minimum cost if education provided by government. Could benefit recycling industries.	Continuing education strategy costing around *$a* p.a.	Uncertain amount of waste reduced. Effective in some cases. Could use in concert with other measure.
Charges for landfill	Additional charges estimated at *$b* p.a.	Additional charges estimated at *$c* p.a. Industries most affected are	Increased revenue of *$d* p.a. Funds could be used to finance other waste reduction initiatives.	Reasonable certainty of reduced waste, but could lead to illegal dumping. May have to monitor this.
Reduced collection of rubbish or mandatory use of smaller bins	Could force households to reduce waste, ie pursue recycling options or buy less packaging. Does not account for different household sizes and therefore different disposal requirements.	This option difficult to apply to business.	Reduced collection costs, however may be higher enforcement costs against illegal dumping.	In addition to landfill charges, is likely to reduce waste by forcing households to be creative. But, larger households may be disadvantaged. Some level of illegal dumping likely.
Subsidise recycling collections	Significant benefit to environmentally conscious consumers. Likely waste reduction of *e%.*	Will benefit industries that provide recycling services. A larger number of firms may shift resources into providing recycling services.	Cost of additional collections *$f* p.a.	Estimated reduction in landfill waste of g%. Need to determine what level of subsidy to apply.
Provide composting equipment	Significant benefit to some consumers provided that the equipment is used.	Minimal impact on business. Firms supplying the equipment will benefit from increased revenue.	Cost of providing equipment *$h* p.a.	Some uncertainty over whether equipment will be used, however, estimated reduction in organic waste of *i%.*

D.5 Consultation

Item 1 Who are the main affected parties?

Item 2 What are the views of those parties?

Item 3 Where consultation was limited or not undertaken, why was full consultation inappropriate?

Consultation with affected parties is a key requirement of the entire RIS process. Consultation should occur when objectives and options are being identified as well as

when impact analysis is undertaken. This is necessary as government efforts to solve a public problem should be developed and adopted in an open and transparent manner. Consultation with affected parties, other departments and the general community is essential for achieving this. In addition, consultative processes can improve the quality of the RIS and ultimately of the solution adopted.

Consultation on regulatory options can improve the quality of the solution adopted by:

- providing perspectives and suggestions on alternative solutions from those parties that will be affected by the government action;
- helping regulators balance competing interests;
- providing a check on the regulator's assessment of costs and benefits and whether/how the proposed option will work in practice, thus reducing the risk of unforeseen circumstances if the option is adopted;
- identifying interactions between different sets and types of regulations; and
- possibly enhancing voluntary compliance through greater understanding and acceptance of a proposal, thereby reducing reliance on enforcement and sanctions.

Consultation may be promoted through techniques such as: holding meetings; producing consultative/discussion papers; publicising an intention to deal with a particular problem and inviting comment; or setting up working groups. To help ensure that the process does not become unwieldy and too lengthy, participants could be given clear instructions on the problem of concern and what constraints apply.

It is important to note that the Government has decided that where reviews of regulation are undertaken, the terms of reference and any reports of such reviews *must* use a RIS framework.

A consultation statement should be incorporated into a RIS. It should contain a statement identifying those consulted and outlining the main views expressed. Areas and the extent of agreement, as well as areas of difference, should be noted. The RIS should also include information on intergovernmental consultation, if this is relevant, and indicate whether consensus has been achieved.

Where consultation was not undertaken or where consultation was limited, clear reasons why full consultation was not undertaken should be given.

D.6 Conclusion and recommended option

Item 1 Provide a brief summary of the assessment of each option.

Item 2 What is the preferred option(s)?

Item 3 Briefly outline the main assumptions that the conclusion rests upon.

Item 4 Why is this option preferred and others rejected?

This section should not introduce new information but should present the key outcomes of the RIS. The analysis, and particularly its results, should be carefully communicated to others so that the essential points are easily understood.

It should include a brief summary of each option. The reasons for deciding to proceed with a particular option, how the community is expected to obtain a net benefit, and why the preferred option is the best option, should be explicitly stated, as should the reasons for rejecting other options.

As adoption of most options will involve making difficult trade-offs among valued attributes, it is important to indicate the main assumptions that support adoption of the preferred option. These should be briefly stated, particularly if they may have a significant impact on expected outcomes. This allows for checking and refining of the analysis. The effect of varying critical assumptions should also be included.

D.7 Implementation & review

Having established which option is most likely to effectively and efficiently meet the objectives stated at the beginning of the RIS, it is necessary to consider how the option will be implemented and enforced, and to establish a review strategy that will allow the option to be evaluated, after it has been in place for some time.

This section should indicate how the preferred option will be implemented and reviewed and what the review process will involve. It may also include criteria for abandoning or modifying the proposal if it does not adequately achieve its objectives.

Item 1 How will the preferred option be implemented?

It is important to consider some practical implementation issues (if they have not yet been considered) before the option is adopted:

- administrative issues, such as which authority will administer the option proposed and how it will function;
- actions regulated parties are required to take such as maintaining extra information, completing forms, or proving experience, expertise or educational achievements;

- all the departments and agencies that will have a role in implementing or enforcing the proposal — resource requirements and costs should be estimated;
- information required to administer the preferred option and whether they duplicate existing requirements — opportunities for rationalisation (for example, by establishing 'one stop shops' to collect, or dispense, information for several departments/agencies) should be examined; and
- how compliance would be checked or ensured; that is, how the option would be enforced.

Item 2 Is the preferred option clear, consistent, comprehensible and accessible to users?

This principle simply ensures that the mechanism will be understood by those who are affected by it. In the case of legislation, clear expression may also help highlight areas of inconsistency or duplication with existing regulations. Clarity can also aid compliance as complex requirements are difficult to comply with and difficult to enforce. It may be useful to consider whether every possible detail and circumstance needs to be set out in the requirements. Some level of discretion for those enforcing the requirements, coupled with clear guidance on what will be regarded as complying behaviour and what will not, should go some way to improving the clarity of regulation and requirements.

Is it sufficiently flexible to adapt to various situations and circumstances?

If legislation is adopted, it should be drafted in a way that makes it sufficiently flexible to take into account the different impact it will have on those being regulated. Performance-based regulation may be used to achieve this end. (For example, see the sub-section 'Standards (including voluntary and regulatory standards)' in section E.2). At the same time, the regulation should be applied fairly and equitably. For instance, importers should be subject to the same, rather than more or less onerous, labelling requirements as domestic producers. Consideration may be given, where appropriate, to have an in-built authority to waive or modify the regulation in certain circumstances and provide for an adequate review/appeal process of decisions made.

Item 3 What is the impact on business, including small business, and how will compliance and paper burden costs be minimised?

The impact of a regulation on business — including different types of business such as small business — should be identified. Ways to minimise compliance and paper burden costs of business should be discussed.

Compliance and paper burden costs are the additional (incremental) costs incurred by businesses when satisfying regulations. Compliance costs can usually be divided into two broad categories:

- one-off costs, such as acquiring sufficient knowledge to meet their regulatory obligations, purchasing/leasing additional equipment and buildings, legal/consultancy fees and training expenses; and
- recurring and ongoing costs, such as staff costs or time, consumable materials, inspection fees/licences and enforcement costs (ie costs arising from need to devote additional time and resources to satisfying regulatory requirements).

RISs should include estimates of both one-off and ongoing compliance costs. Where detailed information about compliance costs is not available, such costs should be estimated by developing plausible assumptions and using available data on business costs and on the number of businesses likely to be affected by a regulatory proposal.

To estimate the incremental change in compliance costs resulting from a proposed regulatory change, it may be appropriate to consider how the change impacts on particular types of business (for example, small, medium and large, rural or urban business etc). For each type of business considered, estimate the incremental change in compliance costs for a typical business in each type or class of business; then multiply this estimate by the number of businesses of that type/class. This will provide an estimate of total additional compliance costs incurred by business in complying with a new or amended regulation.

For example, a (hypothetical) regulatory option could require all clothing manufacturers to use a prescribed form to report on the number and type of people they employed as at 1 July each year. Most businesses would already have such information as part of their normal record keeping requirements. Therefore, the compliance cost for each business would include the additional staff time needed to collect this information and complete the form on 1 July each year.

Consultation with business might indicate the additional compliance costs each type of business might incur. Alternatively, an estimate could be made of these costs. For example, this industry might have 30,000 small businesses, 3,000 medium sized businesses and 500 large businesses. One-off costs could include training of staff to complete the form. If an average of 15 minutes training was required to competently complete the form for all types of businesses, and average clerical wages and on-costs in this sector were $12 per hour, the cost would be $3 per business. This figure should be multiplied by the number of businesses to derive a total one-off compliance cost (see the box below).

In addition, ongoing costs could include the time taken to acquire the relevant information, complete the prescribed form and transmit it to the regulator. It could be assumed that it would take an average of 10 minutes for a small business to acquire the relevant information and complete the form, an average of 15 minutes for a medium sized business and 20 minutes for a large business. These cost estimates could be multiplied by the number of businesses in each class to estimate total ongoing compliance costs.

The results of this hypothetical example are provided in the following Box, showing that this proposal is estimated to increase total compliance costs of the clothing manufacturing sector by $171 500. This comprises $100 500 one-off compliance costs and $71 000 ongoing annual compliance costs.

Example: **Estimating the compliance cost of regulation ($)**

Type of compliance costs	Small Business	Medium Business	Large Business	Total
One-off (non recurring) costs	90 000	9000	1500	**100 500**
Ongoing (recurring) costs	60 000	9000	2000	**71 000**
Total	**150 000**	**18 000**	**3500**	**171 500**

This example shows that even small increases in compliance costs for individual businesses can result in significant economy-wide increases in business costs.

The consideration of compliance costs in a RIS is very important because such costs can:

- distort economic decision making away from the most efficient and effective use of resources;
- divert resources into non-productive uses;
- diminish the viability of business; and
- be passed on to consumers through higher prices, with possible distributional and equity consequences.

Where possible, ways to reduce or minimise such compliance costs should be discussed. In addition, any trade-offs between compliance costs and administrative costs of government, such as the costs of implementing and monitoring regulations, should also be explicitly identified.

Item 4 How will the effectiveness of the preferred option be assessed? How frequently?

Item 5 If the preferred option takes the form of regulation, is there a built-in provision to review or revoke the regulation after it has been in place for a certain length of time?

This section should state how the preferred option will be monitored to assess its progress in achieving its objectives, and how it can be amended or removed when the circumstances which led to its introduction change.

When the option has been in place for some time and is being reviewed, the department/agency should consider key issues such as:

- is there still a problem?

- are the objectives being met?
- were the impacts as expected? Have unforeseen problems occurred? Are there indirect effects that were not anticipated?
- is action still required? Is this still the appropriate action to take or would another measure be more appropriate? Does experience with the measure suggest ways that it can be improved to meet the objectives?

In addition to conducting a full review of a regulatory system after it has been in place for some time, measures for on-going review might include:

- establishing a complaints/feedback mechanism and/or a point of contact for queries;
- establishing arrangements for ongoing consultation with groups affected;
- provision for regular reporting to the public such as through an agency's annual report; and/or
- inserting a review or sunset clause in the legislation.

A sunset clause in legislation is a 'use-by-date' for the legislation. It results in the legislation expiring after a certain time, for example five years. Prior to expiry, the regulation can be reviewed and re-enacted if it is still required. Sunset clauses can be an effective means of keeping the overall burden of regulation on the community at an acceptable level and of reducing the number of outdated regulations still in force.

A sunset clause is particularly suitable for regulation that has been established to deal with an unexpected emergency or with temporary problems, such as measures aimed at providing drought relief.

D.8 Adequacy criteria for RISs

The ORR is responsible for examining and advising on the adequacy of RISs prepared by departments, agencies, statutory authorities and boards. The ORR also provides advice to Cabinet, the Prime Minister/Minister(s) — and, as necessary, the Assistant Treasurer — on the adequacy of RISs. Box D.3 provides information about the criteria used by the ORR to determine whether the analysis contained in a RIS is adequate.

Box D.3: Adequacy criteria for RISs

1. Is it clearly stated in the RIS what is the fundamental problem being addressed? – and is a case made for why government action is needed?
2. Is there a clear articulation of the objectives, outcomes, goals or targets sought by government action?
3. Is a range of viable options assessed including, as appropriate, non-regulatory options?

4. Are the groups in the community likely to be affected identified, and the impacts on them specified? There must be explicit assessment of the impact on small businesses, where appropriate. Both costs and benefits for each viable option must be set out, making use of quantitative information where possible.
5. What was the form of consultation? Have the views of those consulted been articulated, including substantial disagreements. If no consultation was undertaken, why not?
6. Is there a clear statement as to which is the preferred option and why?
7. Is information provided on how the preferred option would be implemented, and on the review arrangements after it has been in place for some time?

Relevant to all seven criteria (which correspond to the seven sections of a RIS) is an overriding requirement that the degree of detail and depth of analysis must be commensurate with the magnitude of the problem and with the size of the potential impact of the proposals.

Finally, for proposals which maintain or establish restrictions on competition (such as barriers to entry for new businesses or restrictions on the quality of goods and services available), it must be established that:

– the benefits to the community outweigh the costs; and

– the Government's objective can be achieved only by restricting competition;

both of which are requirements under the Competition Principles Agreement.

E: EXPLANATORY MATERIAL

This section provides explanatory material which focuses on key conceptual and analytical issues raised in sections A to D of this guide. It provides a brief summary of these issues to assist officials not familiar with key terms and concepts included in a RIS. A list of publications is also provided which elaborate and expand upon this summary information.

This section comprises three parts, a discussion of the main reasons why regulation may be necessary (section E.1), forms of regulation and alternative instruments (section E.2), and information on some cost-benefit techniques (section E.3).

E.1 When may regulation be necessary?

Regulatory intervention by government is often employed to:

- deal with 'market failure'; and
- attain social goals, involving issues such as worker safety, environmental degradation, consumer protection and equity goals.

This following discussion explains in simple terms a number of economic concepts that can be used to justify regulation.

Market failure

Where competitive markets are working properly, they allocate the economy's available resources to their most valued uses. Markets allocate resources to individuals according to the values they place on them. However, in some cases, markets fail to produce economically efficient outcomes. In these situations, a case might be made for government action. The main types of 'market failure' occur in the following situations:

- when there is a monopoly and abuse of market power;
- if there is insufficient or inadequate information available;
- when goods or services are 'public goods'; or
- when there are external costs or benefits (externalities or spillovers) resulting from a transaction in a market.

These types of market failure are discussed below.

Monopoly and abuse of market power

Problems of market power arise from uncompetitive market structures or from anti-competitive conduct. In these conditions, prices are usually higher than they should be and not enough resources are allocated to production of particular goods or services. Such inefficiencies impose costs on the entire community.

'Monopoly power' is said to exist when producers can use market power to restrict output and set prices higher than at competitive levels, and there is no threat that another producer will enter the market and drive prices down. A single firm that produces a good or service that does not have any close substitutes, and does not over time face the threat of another firm entering the market, may possess monopoly power. A monopoly can result from regulatory restrictions on competition. However, care must be taken not to presume that markets with few participants are characterised by monopoly power. If other firms can potentially supply the same market, this should move prices closer to competitive levels.

Restrictions on competition can create monopoly power and are generally addressed by competition laws that make markets more contestable and by reviews of legislation under the *Competition Principles Agreement* (CPA). Where a particular regulatory option under consideration restricts competition, the RIS must address additional issues in the context of the cost-benefit assessment in order to meet the Commonwealth's commitments under the inter-governmental CPA. In particular, the RIS must examine whether the option is the only way of achieving the desired objective, and whether a restriction on competition generates a net public benefit. The compliance of all jurisdictions — including the Commonwealth — to these requirements is monitored by the National Competition Council (NCC).

A 'natural monopoly' can arise where a single firm can produce the total output of a market more efficiently than two or more firms. However, a natural monopoly may also use its market power to restrict output and increase prices.

Governments can prevent the abuse of market power by a natural monopoly by imposing price controls, profit controls or creating third party access rights to natural monopoly facilities, where such access creates competition in upstream or downstream markets.

A small number of firms in a market might also have some market power if they 'cooperate' effectively to restrict output and raise prices to their benefit, at the expense of consumers. Such conduct is usually addressed by general competition laws prohibiting anti-competitive conduct. Indeed, firms maintaining cooperative arrangements to control a market would, in most cases, be in breach of the *Trade Practices Act 1974*.

Insufficient or inadequate information

Lack of information can result in market failure if consumers cannot obtain adequate information on which to base their decisions to buy and consume. This may lead consumers to make decisions that are not in their best interests. Consumers need information on aspects of products such as price and quality (including the hazards associated with each product).

Consumers can sometimes have difficulty collecting information. The cost of collecting information will be different for different consumers. Old age, a disability or high transportation costs may mean that some consumers have less information than others. The benefit of holding information will also differ for different consumers. Furthermore, information may not be provided for several reasons:

- there may not be adequate investment in providing information because once it is available, information is difficult to charge for, so that firms and others may wait for someone else to incur the costs of providing it;
- information may not be provided by a firm because it is not in its best interests for consumers to have more complete information. That is, the self-interest of the firm may result in relevant information being withheld from consumers in some cases;
- consumers are only able to determine the quality of a good or service after purchase and consumption (such as restaurant meals etc); and
- it may be difficult or impossible to ascertain the quality of a good or service after consumption (such as the long-term adverse effects on health of prescribed drugs).

Where there is insufficient or inadequate information, or information asymmetries where sellers have access to better information than buyers, markets may sometimes respond by providing more or better information. For example, market solutions such as producer warranties may emerge spontaneously. Secondary markets can also emerge — including certification services, consumer magazines, agents and insurers — which facilitate consumer learning and provide incentives for producers to provide information about product or service quality.

In the absence of such market solutions, adequate information may not be available and there may be a case for government action. Governments can provide information directly or require companies or other organisations to disclose information. They can also restrict the supply of goods and services regarded as dangerous, signal standards by licensing or accreditation etc, impose minimum standards or encourage self regulation.

Public goods

‘Public goods’ are goods or services to which anyone can simultaneously have access once they are provided, and use by one person does not reduce their availability to others. Producers of public goods are unable to exclude consumers from enjoying the

benefits of a good once it is produced, whether each consumer pays for it or not. It may be physically impossible to exclude people, or it may be economically infeasible to do so.

As a consequence, so long as people believe that others also desire the good and that it is likely to be made available, then each individual is unlikely to contribute voluntarily to its provision. Therefore, free markets are unlikely to provide — or may produce insufficient quantities of — public goods and services.

EXAMPLE: ***Why public goods may never be provided***

A dam can be built to prevent regular flooding of several homes. Once built, the dam will not selectively prevent the flooding of some homes and yet allow others to be flooded. That is, the flood prevention 'service' offered by the dam is available to all whether they pay for it or not. In such a scenario, each individual home owner would be aware of this and would prefer to have some other home owners pay for the dam (sometimes called 'free riding'). If all homeowners adopt the same view, it is possible that the dam will not be built, even though it is in the community's interest to build it.

Examples of public goods are the services provided by a lighthouse, national defence and street lighting. Some other items that are sometimes regarded as public goods do not completely satisfy the definition of a public good. Examples include beaches or parks. These items may be accessible by everyone free of financial cost, but at some point a beach or park can become so congested that its availability to other people, and the enjoyment they get from it, is reduced.

In other cases, such as scarce resources that are not owned privately but are potentially available to all, overuse can occur. If there are no restrictions or no price on using the resources, the use of them will be high. Further, no individual has an incentive to conserve the resource for later use as someone else might use it in the meantime. Examples of common resources are stocks of fish in a river or forests that are not privately owned.

Government action may be required to ensure that public goods are provided. The government may itself provide the goods (such as national defence or community parks) or may contract the private sector to do so. Alternatively, governments can create property rights, such as trademarks or copyright, to provide business with commercial incentives to supply a public good or service. Governments may also regulate the use of common resources to ensure that their use is sustainable.

External costs and benefits (externalities)

An externality occurs when a transaction between parties creates benefits (which are not paid for) or imposes costs (which are not compensated) on others not directly involved in the transaction.

The total social or economic costs or benefits to the community of an activity are made up of the private benefits or costs experienced by those directly engaged in the transaction, plus the external social and economic benefits or costs not accounted for by the individuals or firms engaging in the activity.

The implication of externalities is that they are not accounted for in an individual's decision making and therefore result in too much (where external costs occur) or too little (where external benefits accrue) of an activity taking place from the community's point of view.

EXAMPLE: ***External costs***

A firm is discharging effluent into a river which affects fish caught downstream making them unsuitable to eat. The effect that the firm's effluent has on the fish is an external cost to the firm as it does not pay for this damage that it is causing. The firm's analysis of its costs of production would not include the costs of destroying the fish, yet these costs must be incurred by the community as a whole. Therefore, from the community's point of view, the total cost of the firm producing and discharging wastes into the river would include both the firm's costs of discharging the effluent (private costs of the firm) and the damage caused to the river and to fish stocks (external costs).

External benefits

Immunisation is an example of an activity which generates external benefits. The benefit to the community of a person being immunised against a contagious illness is greater than the benefit that the individual alone receives. The individual receives the benefit of a reduced risk of contracting an illness while the community receives this benefit as well as the reduced risk that this person will pass on an infection.

Markets can in certain cases provide socially optimal levels of a good or service that generate externalities, especially where there are a small number of affected parties and those parties reach a voluntary agreement. For example, a factory polluting a river could reach agreement with the local fish industry to reduce pollution to acceptable and safe levels.

However, where there are a larger number of affected parties, voluntary agreement might not be feasible. In such cases, government action may be appropriate.

Where there are negative externalities, governments can prohibit an activity, impose a tax or charge, impose minimum safely requirements or create tradeable property rights.

Where there are positive externalities, governments can subsidise an activity, require that an activity be carried out, or create property rights which enable those who generate positive externalities to be compensated. Property rights can also be regulated to enhance 'law and order' or redistribute income.

Useful references:

Australian Taxation Office (1996); *ATO Guidelines for the Preparation of Compliance Cost Impact Statements (CCIS)*, Revenue Analysis Branch, Canberra.

Australian Taxation Office (1998); *ATO Guidelines for the Preparation of Regulation Impact Statements (RIS)*, Revenue Analysis Branch, Canberra, September.

David D. Friedman (1990); *Price Theory. An Intermediate Text*, 2nd edn, South Western, Cincinnati.

S. Charles Maurice and Owen R. Phillips (1986); *Economic Analysis. Theory and Application*, Irwin, Homewood.

Robert S. Pindyck and Daniel L. Rubinfeld (1989); *Microeconomics.* Macmillan, New York.

E.2 Forms of regulation and alternative instruments

Most regulation produced in the past has tended to follow a prescriptive 'black-letter law' approach. However, many governments are moving away from these approaches to more innovative methods of dealing with identified problems. These alternative methods can be less costly, more flexible, and therefore more effective than prescriptive regulation.

The forms of regulation and alternative instruments are listed in Box E.1.

Box E.1: Forms of regulation and alternative instruments

Forms of regulation

- self-regulation;
- quasi-regulation;
- co-regulation; and
- explicit government regulation.

Alternative instruments

- no specific action;
- information and education campaigns (including labelling requirements);
- market based instruments (including taxes, subsidies and user charges);
- tradeable property rights (marketable rights);
- codes of practice; and
- standards.

In all cases, the methods adopted to deal with a perceived problem should have the following characteristics:

- administrative simplicity;
- flexibility;
- efficiency and equity.

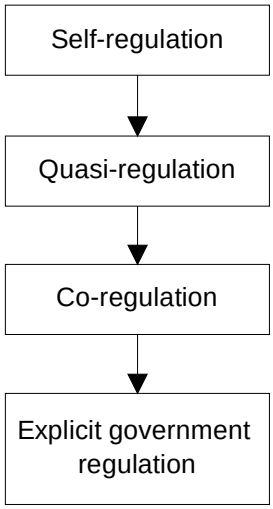
In some cases, a mix of alternatives listed above may be most suitable.

Alternative forms of regulation

The principal forms of regulation may be viewed as part of a continuing spectrum of regulation — from self-regulation to explicit government regulation — as illustrated

below. The principal regulatory forms have various characteristics, advantages and disadvantages — such as their cost-effectiveness, flexibility, responsiveness, accessibility and level of scrutiny — all of which are important in assessing which form might be best for addressing a particular problem.

A simplified spectrum of regulation



Self-regulation

Self-regulation is generally characterised by industry formulating rules and codes of conduct, with industry solely responsible for enforcement. In some cases, governments may also be involved in a limited way, by providing advisory information etc.

The Government requires that self-regulation be one of the first options considered in reviews of regulation and in RISs.

Self-regulation usually implies that firms in an industry or members of a profession have accepted mutual obligations. These obligations are often described in a code of practice or conduct. Self-regulation is common amongst the professions and in the financial sector.

Typically, under these arrangements, an organised group regulates the behaviour of its own members. As the rules are made by people in the industry being regulated, they may be more likely to be observed. They can also be updated more quickly and they can incorporate the expertise of those being regulated.

However, there may be a need to oversee self-regulation to ensure that the community benefits. Sometimes rules are designed to protect or confer commercial advantage on one group over another group, to exclude new entrants to an industry, fix prices or limit competition, or to avoid the need for formal regulation.

By contrast, imposing minimum standards may sometimes reduce the ability of consumers to choose lower cost and/or lower quality products and services.

These issues need to be considered and assessments made of the restrictions on competition and consumer choice that may arise from particular schemes.

Another potential problem is obtaining industry compliance and coverage. Self-regulation may be difficult to enforce due to the lack of legal sanctions. In these circumstances 'free-riders' often benefit from the existence of industry arrangements without themselves complying. However, there may also be greater scope for innovative sanctions to be developed and applied by those closely involved in the industry.

The checklist on page D4 sets out situations where self-regulation is likely to be a suitable and successful approach.

Quasi-regulation

Quasi-regulation refers to the range of rules, instruments and standards whereby government influences business to comply, but which do not form part of explicit government regulation. Some examples of quasi-regulation include government endorsed industry codes of practice or standards, government agency guidance notes, industry-government agreements and national accreditation schemes.[1]

The involvement by government in quasi-regulation, whether through official endorsement, representation on monitoring committees, provision of funding or other help to industry, can enhance industry compliance with the particular code, standard or arrangement.

Quasi-regulation, as with self-regulation, can offer advantages in the form of greater flexibility and responsiveness, less cost to government and greater collaboration with industry, particularly in cases of industry-initiated schemes. Greater compliance is possible if rules are clear and designed in collaboration with industry experts. Quasi-regulation can also make use of innovative compliance mechanisms and quicker, cheaper dispute resolution schemes and — due to greater involvement and ownership — industry may also be more willing to contribute resources to developing, implementing and enforcing this form of regulation.

Three examples of quasi-regulation are provided below.

The checklist on page D4 sets out situations where quasi-regulation is likely to be a suitable and successful.

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[1] For more detail on quasi-regulation, see Productivity Commission 1998, *Regulation and its Review 1997-98,* Canberra.

EXAMPLE 1: **Electronic Funds Transfer (EFT) Code of Conduct**

The EFT Code was introduced in 1986 and applies to financial transactions which are effected through the use of a card and a personal identification number. Industry, consumer and government representatives contributed to the development of the code which was endorsed by Commonwealth and State and Territory Governments.

The code requires EFT providers to issue customers with: clear terms and conditions of use; a transaction receipt each time a service is provided unless the customer specifically elects not to receive one; account statements at least every six months; and the conditions of liability for unauthorised transactions.

The code has been reviewed a number of times, most recently in 1997-98 by a task force drawn from the Treasury and ACCC. The task force concluded that the code was working well and recommended some minor refinements. The code will be monitored by the Australian Securities and Investment Commission. The code will continue to be periodically reviewed to ensure that it remains relevant as the market for EFT services changes over time.

EXAMPLE 2: **The National Code of Practice for the Construction Industry**

This code was written by the Australian Procurement and Construction Council in consultation with the Departments of Labour Advisory Committee and released by the Minister for Workplace Relations and Small Business in August 1997.

The code sets out standards for ethical behaviour, industrial relations and occupational health and safety for participants in the construction industry. Sanctions for breaches include partial or total exclusion from government work, publication of details of the breach or reference of the breach to other relevant authorities.

In endorsing the code, the Commonwealth, state and territory governments indicated that they were using their position as major clients of business to encourage changes in industry production processes so as to raise productivity, and to take other action that will help develop an industry which achieves internationally competitive standards.

EXAMPLE 3: **ANZFA Code of Good Manufacturing Practice for the production of gluten-free and low gluten foods**

Due to the incidence of certain medical conditions relating to gluten intolerance, the Australian Food Standards Code contains definitions of gluten-free and low gluten food. The Food Standards Code also contains conditions for claims and other labelling requirements.

In order to provide guidance on the minimum requirements for the production of foods described as ‘gluten-free’ or ‘low gluten’, a Code of Good Manufacturing Practice was prepared by the Australian and New Zealand food industries, health professionals, consumer organisations and the Australia New Zealand Food Authority in consultation with State and Territory food authorities and the New Zealand Ministry of Health.

The code is not mandatory and is intended for use in industry self-regulation.

Co-regulation

Co-regulation usually refers to the situation where industry develops and administers its own arrangements, but government provides legislative backing to enable the arrangements to be enforced. This is known as 'underpinning' of codes or standards. Sometimes legislation sets out mandatory government standards, but provides that an industry code can override those standards. Legislation may also provide for government imposed arrangements in the event that industry does not develop arrangements of its own.

There are a variety of ways in which government may provide legislative support to industry based codes (or standards) including:[2]

- delegating power to industry to regulate and enforce codes;
- enforcing undertakings to comply with a code;
- setting out standards which can also be overridden by industry;
- incorporating a reserve power to have a code;
- requiring industry to have a code but, in its absence, government may impose a code; and
- prescribing industry codes as voluntary or mandatory.

Although co-regulatory arrangements are usually designed by industry, a RIS is still required in order to demonstrate that the best option has been chosen. The relevant government department, agency, statutory authority or board should prepare the RIS, in consultation with the industry.

EXAMPLE: **Telecommunications consumer protection regime**

The new telecommunications legislation provides that industry may have the responsibility for developing and implementing codes of practice for consumer protection matters such as the internal handling of customer complaints and the timeliness and comprehensibility of bills.

If industry fails to develop adequate codes, the Australian Communications Authority (ACA) has the power to either request that a code be developed by industry in a given time frame, or develop a 'standard' which is binding on industry. Compliance with the codes is voluntary, but the ACA has the power to direct a particular participant to comply.

The legislation also permits codes to confer power on the Telecommunications Industry Ombudsman to handle residential or small business customer complaints about breaches of the code.

[2] For further information see: Minister for Customs and Consumer Affairs (1998); Codes of Conduct: Policy Framework, Industry, Science, Tourism and Consumer Affairs, Canberra, March.

In 1997, the *Trade Practices Act 1974* (TPA) was amended to allow prescription of an industry or consumer code, or relevant provisions of such codes, as either mandatory or voluntary. The Government also decided that a number of prerequisites must be met before prescription of codes under the TPA can proceed, including:

- a market failure has been identified that will, in the absence of government intervention, have a significant detrimental impact on a substantial group in the community. Alternatively, where there is a social policy objective that, if not pursued by government, will lead to a significant detrimental impact on a substantial group in the community;
- a systemic enforcement issue exists, for example, with breaches of voluntary industry codes and lack of agreement on fair trading principles, which has led to the failure of self-regulatory or quasi-regulatory arrangements;
- there are significant deficiencies in any existing regulatory regime which cannot be remedied (for example, inadequate industry coverage); and
- a range of self-regulatory options and 'light-handed' quasi-regulatory options has been examined and demonstrated to be ineffective.

A comprehensive RIS will be required for any code which is under consideration for prescription under the TPA. Draft RISs must be distributed as part of the consultation with affected parties.

EXAMPLE: **Codes of Practice under the *Trade Practices Act 1974***

The TPA allows prescription of an industry or consumer code, or relevant provisions of such codes, as either mandatory or voluntary. A mandatory code can be enforced on all businesses in the specified industry regardless of whether they are signatories to the code. A voluntary code can be enforced only on those businesses which are signatories.

Prescription applies the remedies contained in the TPA to those who contravene such codes. A feature of prescribed codes is that they retain a high degree of industry involvement while providing the enforceability and coverage that can be ensured only through legislative means.

Advantages and disadvantages of self-regulation, quasi-regulation and co-regulation

Overall, there are a number of potential *benefits* associated with self-regulation, quasi-regulation and co-regulation compared with direct government regulation, including:

- lower government administration costs, because such regulations are developed and often administered by business;
- lower compliance costs for business;
- innovative inducements for compliance and sanctions for non-compliance;
- rules which are tailored to specific needs and thus better targeted;

- improved information flows, using clearer terms;
- improved credibility and lower costs of compliance because rules are developed by business, not imposed on them by governments;
- enhanced flexibility, responsiveness and speed of implementation and modification;
- greater responsiveness to consumer demands based on additional information gained from, for example, the complaints mechanism; and
- increased certainty and the opportunity to innovate through 'deemed to comply' codes.

The potential *costs* of self regulation, quasi-regulation and co-regulation can include:

- the creation of restrictions on competition (ie. barriers to entry, restrictions on advertising, prescribed prices etc);
- some 'fringe' businesses not complying with minimum standards;
- ineffective sanctions for non-compliance;
- reductions in consumer choice, by imposing minimum standards that do not allow consumers to choose lower cost/quality products or services;
- the creation of expectations by governments and consumers of compliance, which are not met when some businesses do not comply;
- creation of confusion about regulatory requirements; and
- business may not have the resources and capacity to develop or administer a quasi-regulation scheme.

Potential risks associated with the implementation of quasi-regulation

It is important to note that some of the potential problems and risks associated with quasi-regulation are created by the way governments sometimes formulate or implement quasi-regulations, and therefore can be avoided. Such problems and risks which can be avoided could include:

- governments are often inconsistent in their choice of regulatory forms and there is a often a lack of government justification and risk assessment for quasi-regulation;
- quasi-regulation gives much discretion to regulators and, because of its convenience and lack of scrutiny, is sometimes used as 'backdoor regulation';
- what starts out as self-regulation can gain the imprimatur of government agencies and subsequently be lifted into legislation, depicted by some as 'regulatory creep';
- quasi-regulation may be pitched at best practice standards rather than minimum effective regulation, imposing unnecessarily high compliance burden on business;

- small business often lacks the resources and expertise to operate successfully under performance-based regulation and fears greater litigation from such arrangements, preferring the certainty offered by prescriptive regulation;
- confusion exists about the status and enforceability of many quasi-regulatory arrangements. Quasi-regulation is often less accessible than Acts of Parliament. Some businesses choose to ignore quasi-regulation because they judge that full compliance is impossible or impractical; and
- quasi-regulation can result in a shifting of costs to industry because of the substantial resources involved in developing and administering industry-based schemes.

When reviewing, reforming and implementing quasi-regulations, governments should be aware of these potential problems and risks, and take steps to avoid them.

Explicit government legislation

This type of regulation has three main characteristics: it attempts to change behaviour of groups or individuals by detailing how regulated entities should act; it generally relies on government inspectors and/or monitoring to detect non-compliance; and it imposes punitive sanctions — such as fines — if the regulations are not complied with. This approach establishes clear and standardised rules and can be successful for addressing well-defined and stable problems.

Explicit government regulation is often considered to offer more certainty, including industry-wide coverage, and greater effectiveness compared to other forms of regulation because of the availability of legal sanctions. It is often preferred by regulators, particularly in dealing with high risk, high impact public issues. In some circumstances, compliance costs might be lower for legislation due to greater certainty. This form of regulation is subject to scrutiny from Parliament and from the Government's regulation making and review processes.

However, explicit government regulation can also have several potential drawbacks:

- it may be standardised and inflexible. This means that it may not adequately deal with diverse conditions or with changes over time. This can result in the regulation becoming irrelevant. It may also impede technological progress and innovation;
- it may, over time, generate more and more regulation. For instance, more regulation is created to adapt the original regulation to a new situation or to close the gaps where compliance is not being achieved;
- there are potentially significant time lags inherent in making and amending legislation;
- legislation is not well suited for influencing the quality of complex services such as those provided by many of the professions;

- the perception by some people that legislative drafting is complex and difficult to understand may deter some of them from trying to comply;
- government budgetary costs are often higher with black letter law and there may be less accountability for administrative costs, compared to other regulatory forms which utilise the resources of commerce and industry;
- compliance costs may be high as the law often does not reflect accepted commercial practices; and
- costs and delays associated with the justice system may mean poor access for those without means to pursue their legal rights.

Choosing the best regulatory form

There is a variety of factors relevant to choosing the best regulatory form to address specific problems including: the extent of risk; the severity of the problem; the nature of the industry concerned; the need for flexibility or certainty in regulatory arrangements; and the availability of resources.

A checklist to guide users through the selection of the different regulatory forms — self-regulation, quasi-regulation, co-regulation and explicit government regulation is provided in Box D.2 (page D4).

Alternative instruments

A range of alternative instruments can be used to achieve policy objectives. These alternative instruments are discussed here in detail.

No specific action

Prior to considering the other alternatives, the option of not taking specific action should be considered. This option involves relying on the market in conjunction with existing general liability laws and insurance laws.

There is a possibility that action will not improve upon the problem, or alternatively that the problem may solve itself (as can happen when markets are changing rapidly) or may have been misunderstood. Government action may only shift the problem elsewhere, or the costs of government action may be greater than the costs imposed by the problem it is designed to correct.

In addition, it is useful to consider whether the problem may have been caused by a previous government action — this may point to areas of regulation that need to be removed, simplified or amended in order too remove the problem.

The department/agency proposing action should also consider whether existing regulations and requirements can be altered to achieve the objective sought.

Regulation is often designed to reduce risk, but if people are held responsible for their actions and are required to pay damages, incentives develop for people to take appropriate levels of care. By providing accessible legal remedies, individuals can enforce their rights rather than relying on government action to do so. In practice, however, legal remedy may sometimes be too uncertain, slow or costly to be an efficient method of changing behaviour.

For example, the availability of insurance allows businesses and consumers to assess risks and determine cost-effective ways to reduce them. Governments may establish or merely promote insurance schemes designed to protect certain people (for example, consumers) against specific risks. Governments may also require businesses to carry private insurance for specified risks as a condition of receiving permission to operate or carry out particular activities. In this second case, insurance is really a requirement of the regulatory regime rather than an alternative to it. An example is the requirement in Victoria for registered builders to have insurance. This is designed to protect clients of the builder against any faults which may occur within ten years of the building being completed.

Information and education campaigns

These strategies seek to alleviate the problem by changing the quality of the information available, or by changing its distribution. These measures improve market functioning by allowing people to make better informed decisions.

The main advantage of these strategies over some other approaches is that they allow individuals to choose what is best for themselves given the information available, rather than imposing one solution on all.

This type of approach does not set legally binding rules on behaviour. Instead objectives are reached through education and persuasion. This is most effective if the behaviour which needs to be changed occurs through ignorance. People may voluntarily change their behaviour if they are made aware of a problem or why a particular objective is being sought.

At times, the provision of information or education may be as effective as coercion for obtaining desired results. Appeals for individuals or companies to contribute to the public good, or to maintain a good (business) reputation can be effective for changing behaviour. Similarly, attempting to educate the community of the need for change is another possible strategy.

Information can be disseminated through government action in two ways:

- by requiring companies to disclose information concerning certain features or attributes of the product to consumers; and
- through the government collecting and disclosing information to the public.

EXAMPLE: ***Education and information.***

Many local governments have in place successful recycling schemes. Typically, these require residents to sort through their rubbish to separate plastics, aluminium and papers. This has been achieved largely through a persuasive or educative approach and a change in attitude towards recycling.

Other examples include QUIT campaigns directed at smokers, environmental awareness programs and safe sex campaigns to prevent the spread of HIV and AIDS.

Under these approaches, there often is no attempt to monitor behaviour in order to impose sanctions on those who do not comply. Rather, advertising, training and the provision of advisory services are used to achieve policy objectives. In some cases, monitoring of compliance does takes place. If a party consistently fails to comply there may be an implicit threat that sanctions will be imposed. An example is prices monitoring by the Australian Competition and Consumer Commission.

It should also be noted that the market itself often responds to fill information voids. Examples include product comparisons in magazines such as *Choice* or the independent testing and assessment of cars by the NRMA.

Labelling requirements

Labelling requirements are another way of disseminating information. They often appear on products that pose some risk of harm to users, but can also refer to country of origin etc.

The benefits of labelling are that producers are required to reveal information, for instance on the potentially harmful attributes of their products, to buyers that they might otherwise not reveal. This allows consumers to make more informed choices. Individuals, taking this information into account, will decide whether to consume the product or not. This is often preferable to placing a ban on the product which imposes one solution on all consumers and does not account for different individual circumstances (eg the product may pose less harm to some people).

Labelling requirements may impose costs on businesses. These costs are often passed on to consumers in the form of higher prices for the product. Government also incurs costs in enforcing the labelling requirement.

These costs may not be worthwhile if there are few benefits in labelling. Labelling may result in few benefits if the information that is revealed is: not desired by consumers; is not conveyed meaningfully (so that information is misunderstood); or if consumers do not read or take the information into account when they decide whether to consume the product.

Market based instruments (taxes, subsidies and user charges)

Economic incentives can be used in the design of a regulatory system in order to change behaviour. These instruments can be more efficient than prescriptive regulation because they allow individuals to make their own benefit-cost trade offs in pursuing certain behaviour. Consequently, they may achieve desired regulatory outcomes in least cost ways. However, the outcomes associated with these approaches are less certain than those associated with prescriptive regulation.

Market based instruments work by altering the costs and benefits of certain actions, thereby changing individuals' behaviour. For example, a tax will raise the cost of engaging in a certain activity while a subsidy will lower it. User charges also raise the costs of certain activities.

EXAMPLE: ***Taxes, subsidies and user charges.***

Taxes on emissions of pollution; subsidies to undertake education; and charges for using common resources such as water.

All these instruments are particularly useful in dealing with 'spillovers' from private activities where free markets lead to too little or too much production of a particular good or service.

These approaches achieve desired outcomes by setting the incentives at the right level and by setting charges that reflect the true values of resources so that they are not over or under utilised. In practice, a gradual approach of moving charges in the right direction is often adopted, because it can be difficult to estimate the 'right' level of charges and gradual adjustment gives markets time to adjust.

Tradeable property rights (marketable rights)

These are government issued permits granting property rights (for example to a resource) that may be bought and sold in a market.

Tradeable property rights can be used as an alternative to issuing licences and permits to limit production or consumption activities.

Examples of tradeable permits are water or air pollutant permits. As pollution cannot be reduced to zero because it would be too costly in terms of production and employment lost, a desired total level of a particular pollutant needs to be set as a ceiling. Once this level is defined, permits are issued which allow the holder to produce a certain share of the total.

By allowing trade in permits, those firms that find it easiest or least costly to reduce pollutants can do so and sell their excess permits to other firms that are unable to reduce emissions, except at relatively high costs.

EXAMPLE: ***The Hunter Salinity Control Scheme****.*

A scheme, involving the use of tradeable salt discharge credits to manage saline discharges into the Hunter River, was trialed between 1 January 1995 and 1 January 1996.

The scheme identified three different flow conditions in the river.

In periods of low flow (90% of the time in an average year) the river is most vulnerable to the effect of discharges and no discharges are allowed. During high flow conditions, discharges were allowed provided the level of salinity of the river remained below acceptable levels. Individual discharge sources were allowed a share of this total salt load, depending on the number of 'discharge credits' held.

The total allowable salt load for the river was set at the load that may be discharged by all sources collectively without exceeding the river salinity limits. This was calculated with reference to acceptable salinity levels in the river and the contribution of diffuse sources.

Under flood conditions, licence holders were generally permitted to discharge without limit as the river is least sensitive to the effect of discharge.

As part of the scheme, a formula was developed to determine the initial allocation of credits to those discharging into the Hunter River. A strict monitoring regime was established to ensure that the salinity of the river at any point did not exceed acceptable levels. In addition, trading rules were established and trading in credits was recorded.

The scheme achieved the desired outcomes, including managing water quality, and has subsequently operated successfully since 1 January 1996.

This type of system achieves the desired reduction in overall pollution in a more cost effective way than would a set reduction in pollutants for each firm in the sector.

Codes of conduct/practice

Codes are generally adopted and administered by the industry to which they relate, although they often complement government laws and regulations. Codes may deal with a range of issues such as: membership eligibility; standards for processes, practice or products/services; and complaint handling procedures. The advantages of codes are that they are industry specific, flexible and can be quickly amended. Also, the industry is often best placed to police conduct.

Codes may be either voluntary or mandatory (covering all members). Voluntary codes may be more flexible than mandatory requirements, but outcomes may be more uncertain. If there is some involvement by government in the development, implementation or endorsement of industry codes, then such codes are defined as quasi-regulation.

Standards (including voluntary and regulatory standards)

Voluntary standards are developed by Standards Australia (a non-government body) and other third parties. Voluntary standards — and other standards — are sometimes incorporated into regulations or are used as regulatory standards.

There are three main types of standards:

- principles-based;
- performance-based; and
- prescriptive.

Principles-based standards describe the objective sought in general terms and require interpretation according to the circumstances.

Performance-based standards specify the desired outcome in precise terms, but allow individual organisations to determine how to achieve the outcome.

Prescriptive standards specify the technical means for attaining the specified outcome.

EXAMPLE: ***Prescriptive and performance-based standards.***

The objective of a standard may be to reduce to safe levels the exposure of workers to chemical fumes that are a by-product of a production process.

A prescriptive standard might seek to achieve that objective by requiring companies to install specified ventilation systems to extract the fumes, thereby reducing the exposure of workers.

Under a performance standard, each company would be required to meet the objective of 'reducing workers' exposure to fumes'. Companies could achieve this objective by adopting the approach which best suits their operations. For instance, a company could change the inputs used in the production process, or could modify the production process itself, so that the total amount of fumes produced is reduced to safe levels.

Provided that the objective is specified clearly enough so that companies must attain a minimum level of reduction in exposure before they are deemed to comply with the standard, an alternative approach may provide a more efficient means of obtaining the objective for the company. It may also produce a larger reduction in the exposure of workers to fumes.

Where regulatory options under consideration involve the incorporation of standards, any reports, statements and RISs should examine the costs associated with particular standards, and demonstrate they are the most effective way of achieving the relevant policy objective. In particular, departments and agencies should consider the costs of using standards which were not specifically designed for the problem at hand.

Standards should not be used where they are overly complicated or impose unnecessarily high compliance costs. They should only be used where they are the most effective and efficient way of achieving an objective.

Where a standard is used, the regulation should *not* allow the standard to be modified or changed, unless it can be clearly shown that modification or change is necessary. Any modifications to the standard should *not* be automatically incorporated into regulation. Where regulation refers to a standard, it should explicitly refer to the type, characteristics and date the standard was made. It should *not* refer to a standard that could be changed or modified.

Regulatory reviews may seek to achieve harmonisation of regulatory standards across national jurisdictions (eg for product standards and service sector areas such as accreditation and recognition of professional qualifications etc). This is not to say that Australian regulations need be the same as prevailing international norms. However, where there are differences between the proposed Australian approach and international norms, the ramifications for business and exporters should be examined. For example, where a regulation is more stringent than international norms, this might lead to a cost disadvantage to Australian producers and exporters, or a competitive advantage — based on quality — or possibly both. Where a proposal is less stringent than international norms, this may confer a cost advantage, but it may lead to Australian goods and services being excluded from certain overseas markets.

Useful references:

Commonwealth, State and Territory Consumer Affairs Agencies (1996); *Fair Trading Codes of Conduct: Why have them How to prepare them*, AGPS, Canberra, October.

Government of Canada (1994); *Assessing Regulatory Alternatives*, Regulatory Affairs Guide, May.

Government of Canada (1998); *Voluntary Codes: A Guide for their Development and Use*, Ottawa, March.

Minister for Customs and Consumer Affairs (1998); *Codes of Conduct: Policy Framework*, Industry, Science, Tourism and Consumer Affairs, Canberra, March.

Robert W. Poole (1982); *Instead of Regulation*, Lexington Books, Massachusetts.

E.3 Cost benefit assessment techniques

A major purpose of the RIS is to improve decision making by providing a basis for adopting the most effective regulatory solutions to a policy problem. To help achieve this, the RIS involves an analysis of the likely benefits and costs of each option identified to help ensure that the option adopted is one which results in the largest net benefit to the community.

The impact analysis section of the RIS recognises that there are both positive and negative effects (benefits and costs) experienced by different parties in implementing a proposal and that, unless all of these effects are considered, it is difficult to make sound decisions.

Economists traditionally adopt a tool known as cost-benefit analysis (CBA) to assess the net benefit of a project or proposal. This is a comprehensive form of analysis that involves calculating the total benefit associated with a proposal and comparing this to its total cost. If a net benefit results, the proposal is judged as potentially attractive.

However, CBA is only a guide to decision making as it focuses only on the allocative effects of proposals. It alone cannot provide a definitive answer to which is the best proposal to adopt, as society has a wide range of goals to pursue in addition to allocating resources efficiently. Thus, the CBA is not the sole input to decision making. Issues of equity, cultural and social significance, as well as political considerations, all influence decisions.

The level of quantification required in the impact analysis will vary according to the proposal being analysed and resource constraints. Some departments and agencies already conduct quite sophisticated impact analyses and are encouraged to continue doing so.

The issues that need to be considered when preparing an impact statement are outlined earlier in this guide. This section provides a preliminary discussion of some of these issues and introduces some cost-benefit analysis concepts and techniques. It also discusses 'risk analysis' which is relevant to all proposals, but particularly those that deal with safety concerns.

Classifying benefits and costs

Allocative and distributional or transfer effects

Allocative effects alter what, and how much, society can produce and therefore affect what is available for the community to use. As resources are limited, allocative costs are always incurred when a particular proposal is adopted because resources used in undertaking that proposal cannot be used for other proposals or programs. Therefore,

allocative costs are the community's production and consumption opportunities forgone because of projects undertaken.

EXAMPLE: ***Allocative or distributional effects?***

The difference between allocative and distributional effects can be seen in the example of the government providing subsidies to employers for training workers who would otherwise be entitled to receive social security payments.

If the training received by the workers raises their skills and their productivity in employment, then subsidies may lead to allocative benefits as more goods and services can be produced with the resources the community has.

There are distributional effects in that those formerly reliant on social security payments (which come, ultimately, from the taxpayer) now receive payment for work/training.

Distributive or transfer effects alter the distribution of society's total stock of produced goods and services or income without altering its volume. These effects can be regarded as making some people better off, while others are made correspondingly worse off.

Direct and indirect effects

Direct effects are those that affect the individuals, groups and organisations that are the target of the proposal. Indirect effects are those effects that accrue to any other party. Some of these indirect effects are likely to be unanticipated.

By considering the indirect effects of a proposal, attention is drawn to the need to ensure that a proposal addresses the specific problem at hand and does not generate effects or impacts that go too far beyond the proposal's target.

The unintended or indirect effects of a proposal can be substantial enough to render the proposal less, or no longer, appropriate. Indirect effects may include:

- reducing the effectiveness of existing regulations;
- unacceptably increasing the total regulatory burden on the community; or
- reducing market flexibility.

The distinction between these effects is not always clear. It is often easier to identify indirect effects when existing requirements are being reviewed and these effects have become visible over time.

Tangible and intangible effects

Tangible effects are those that are easily identified and easily quantified and valued. An example is the cost of employing people to collect information from regulated parties.

The term 'intangible' is often applied to those effects to which it is difficult to attribute a dollar value or quantify. Intangible impacts affect peoples' satisfaction, but there is no other economic market for them. Examples include time, health, comfort, environmental amenity and cultural values. When intangible elements cannot be quantified, they should be dealt with in a descriptive or qualitative manner. However, in many cases, some estimation of the value of these effects can be achieved. For example, where regulation of safety is assessed, an indication of the number of injuries or lives expected to be saved could be included.

Some techniques for quantifying benefits and costs

To allow a comparison between alternative proposals, benefits and costs need to be valued in a consistent manner. This requires a standard unit of measurement. Usually benefits and costs are measured in dollar terms. This allows disparate benefits and costs to be added together to arrive at a net figure of the proposal's overall impact on the community.

In competitive markets, prices provide direct measures of benefits and costs which can be observed and used as data for the CBA.

In some cases, competitive markets for benefits and costs (particularly intangibles) do not exist, but it may be possible to derive values of benefits and costs from other data.

EXAMPLE: ***Estimating the value of intangible effects***

Various methods to value intangibles have been used. For instance, with regard to noise, these include: depreciation on property; surveys; and dislocation costs.

An idea of the value that people place on noise could be estimated by the extra amount that people are willing to pay for a quieter car or for a house in a quiet neighbourhood. Similarly, people may be willing to pay more to avoid high noise levels at night than they would pay if the noise occurred during the day.

Other examples include: measuring the effects of pollution by observing distances travelled to swim at clean beaches; or the costs of 'cleaning' water.

An indication of the value drivers place on their time may be inferred by the fact that they are willing to pay a toll to use a freeway rather than use a slower road.

(For additional information see Dept. Environment, Sport & Territories, Dept. of Finance & Resource Assessment Commission (1995);*Techniques to Value Environmental Resources*, AGPS, Canberra).

In some cases, the prices or costs of surrogate goods or services may provide a good estimate. This information can be derived from the prices charged in related markets. In other cases, where there may be no market for similar goods, people could be surveyed to help estimate the value they place on particular goods/services. However, care should be taken in designing these surveys to ensure a wide cross section of

people are surveyed and to make allowances for people over or understating the value that they place on a particular good.

At times, it may be difficult to attribute a dollar value to benefits, whereas cost estimates are more readily available. In these cases, benefits may be expressed in physical units (such as number of lives saved) and costs may be expressed in dollar terms. This form of analysis involves ranking options on the basis of their 'cost per unit of effectiveness' or 'units of effectiveness per dollar spent'. It is applied when the options are equally effective, that is when they produce the same outcome. This technique is known as 'cost effectiveness analysis'. (See Dept. of Finance (1991); *Handbook of Cost-benefit Analysis',* AGPS, Canberra.)

In cases where the benefits and costs cannot be quantified in monetary or numerical terms, a comprehensive and detailed qualitative assessment should be made which will provide a complete tally of the effects of a proposal. This is required to judge whether the effects of a proposal on the community are positive.

In all cases where benefits and costs are estimated, it will be necessary to state the assumptions made and the data sources used.

Discounting future effects

In formal cost-benefit analysis, estimates of all the expected benefits and costs of a proposal, expressed in dollar terms, are added together to arrive at a single figure of the proposal's net expected benefit or cost.

As the benefits and costs associated with a proposal accrue over time, they cannot simply be added together without adjustment. This is because the community is not indifferent between a proposal that yields benefits immediately and a project that yields benefits some years down the track. The latter benefits are less valuable because they are not available to be used immediately and the resources used to acquire these benefits could have been used productively in the meantime.

To compare benefits and costs occurring over different time periods, future effects are discounted using an interest rate. This weighing of effects over time is known as 'discounting'. The interest rate represents the rate of exchange between the value of future effects and present effects and is called 'the discount rate'. Applying a discount rate to future effects allows them to be valued in today's dollars. These amounts are known as the 'present values' of future streams of benefits and costs. By deducting the present value costs of a proposal from its present value benefits, the 'net present value' can be calculated. The discount rate chosen will have a significant impact on the calculated net present value of a proposal and therefore should be selected carefully. (These concepts are discussed in detail in Department of Finance (1991), *Handbook of Cost-benefit Analysis,* AGPS, Canberra.)

For many proposals, discounting will not be possible as not all items would have been quantified. However, the notion that future benefits are less valuable today should be incorporated in the impact assessment.

Allowing for uncertainty

Often there will be a range of reasonable assumptions that could be used in an impact assessment, and individual judgements will vary over what constitutes best estimates.

'Sensitivity analysis' (discussed further in Department of Finance, 1992) can help account for differences in judgement, or uncertainty, and the effects they have on the outcomes of impact assessments. Sensitivity analysis allows a check on how a slight variation in assumptions or future events could affect the values of the benefits and costs of a proposal.

Sensitivity analysis involves altering some critical assumptions and, in formal cost-benefit analysis, re-calculating the estimated net present value with different ('best case', 'most likely' and 'worst case') assumptions in order to gauge the risk or level of uncertainty that is associated with an option's outcomes.

Uncertainty is unavoidable, and methods to deal with it are imperfect. It is best to avoid concealing it, and to indicate its significance for the results obtained wherever possible.

Distributional effects

Formal cost-benefit analysis does not explicitly account for the distribution of benefits and costs across the community. It typically treats the benefits to one group symmetrically with the losses or costs to another. Thus if one group were to lose out by approximately $100 000 but another group gained by $200 000, then the proposal would be judged as potentially attractive. This is because a net benefit would result; the gainers could potentially compensate the losers and the community as a whole would still be better off.

In reality, however, compensation may not be paid. Or in order to compensate those who 'lose out' as a result of implementing a proposal, an explicit analysis of the proposal's distributional impact needs to be made.

Once proposals have been ranked according to their economic or allocative effects, it is important to explicitly assess each proposal's distributional effects.

Reference groups for considering distributional effects will vary according to the problem at hand. For instance reference groups might include: present and future generations; rich and poor; those living near a hazard versus those living a large distance away from it; and small business versus large business.

In some cases, the income levels of gainers and losers can be a relevant consideration, particularly if a less well off group is incurring most of the costs of the regulation. A distributional analysis will help highlight where the burden of the measure is falling and may provide information that is useful for designing compensation arrangements, if they are necessary.

Compensation might be considered if the proposal is likely to cause a significant or sudden change in the business environment or if there will be a large adverse financial impact on some market participants. In most cases an alternative to paying compensation is to spread the effects of the regulation over time.

This explicit analysis of a proposal's distributional effects should provide information to help achieve distributional goals in the most efficient way.

Risk analysis and assessment

Risk refers not to particular *hazards* but rather to the *probability* that the hazards will cause harm, that is, that an undesirable event will occur.

Risk analysis is the process of discovering what risk is associated with a particular hazard. This involves: identifying hazards and the mechanisms that cause them; and estimating the probability that they will occur and their consequences. It may also include assessing the risk of not doing something about the hazard and the risk of following a particular course of action.

Risk analysis is a valuable tool in further addressing the threshold issue of whether or not to regulate, but can also be used for other purposes. These range from assessing the mechanical impact of regulation on risks, to estimating the cost-effectiveness of reducing risks. Furthermore, risk analysis is of use in answering two important questions. First, whether the risks that regulation is intended to address are of significant magnitude compared with other risks. Second, the extent to which regulation reduces the initial risk problem.

EXAMPLE: ***The indirect effects of regulating a risk.***

By imposing strict regulations and standards on new drugs before they can be marketed, their introduction is delayed. This reduces the risk of unintended side-effects. But drugs currently available may not be as effective, or may have more undesirable side effects, than the new drugs. Hence, by delaying the introduction of new drugs, there is a risk that some lives may not be saved or some suffering not alleviated.

There are two main reasons why some analysis of risk should be undertaken.

Firstly, it is necessary to put risks in perspective, as a multitude of risks are faced in everyday life, many of which will remain even if government action is taken to alleviate them.

Secondly, efforts at reducing risk are best directed to cases where gains will be the greatest and where risks are regarded as unacceptable rather than cases where efforts will generate only trivial gains.

Risks can be viewed in several ways. It is possible to look at societal risk or individual risk. The former averages out individual risk and measures the risk to society as a whole or to a large group of people. On the other hand, individual risk varies from person to person. In addition, voluntary risk can be distinguished from involuntary risk. Voluntary risk occurs where an individual can choose to undertake or avoid risk-causing activity and is fully aware and informed of the consequences (for example, playing sport or consuming excessive quantities of alcohol). Conversely, involuntary risk occurs where there is no choice or inadequate information about the consequences.

An analysis should also make a distinction between perceived risks and actual risks. Perceptions of risk may not be reliable guides of actual risks — they may overstate or understate the probability of an adverse event and/or the cost of an adverse event.

An important distinction to make when conducting risk analysis is that between risk and uncertainty. Risk involves a situation where the probabilities of the various outcomes can be predicted and are reasonably well known. Uncertainty involves a situation where the costs and benefits might be known, but the probabilities of the outcome cannot be accurately predicted and are not known.

Risk assessment

Risk assessment enables decisions about regulation to be in proportion to the risks involved. Risk assessment should involve consideration of the wider effects of introducing regulation. Risk analysis should show the importance of the various contributors to the overall risk and show where work is needed to reduce that risk. This analysis should bear in mind that introducing a regulation may have the effect of reducing one risk but may increase another. That is, there may be indirect effects of regulating a risk.

The objective of implementing a proposal to deal with risk should not be to reduce the risk at all costs or to reduce it to a minimum level, but rather to balance the benefits and costs to the community of reducing the risk.

However, one common practice is to overstate the extent of the risk in order to include a safety margin when proposing a regulation. By doing so, policies adopted would be more stringent than would be the case if the 'actual' level of risk were used as a guide.

Another common practice is failing to account for the community's adaptability to a problem. This can also result in excessive measures being taken to deal with a risk.

The overriding reason to consider risks and a proposal's effects on such risks is to ensure that decisions are based on reality, and that society would obtain sufficient benefits from government action in order to justify the costs regulation may impose.

The following issues can be addressed in the risk assessment of regulation:

- an appraisal of the current level of risk to the exposed population/individual from an identifiable problem/source;
- the reduction in risk that will result from the introduction of the proposed measures;
- consideration of whether the proposed measures are the most effective available to deal with the risk; and
- whether there is an alternative use of available resources which will result in greater overall benefit to the community.

Risk analysis and assessment should be as detailed as is appropriate in the circumstances.

Like formal cost-benefit analysis, risk analysis and assessment in itself does not provide a definitive answer to which proposal is the most effective and efficient one. Rather, it provides information which needs to be appraised alongside other relevant factors and issues when deciding between alternative proposals.

Useful references:

Department of Finance 1991, *Handbook of Cost-Benefit Analysis*, AGPS, Canberra.

Department of Finance 1992, *Introduction to Cost-Benefit Analysis for Program Managers*, AGPS, Canberra.

W. Kip Viscusi 1992, *Fatal Tradeoffs*, Oxford University Press, New York.

Department of Environment, Sports and Territories, Department of Finance and Resource Assessment Commission 1995, *Techniques to Value Environmental Resources. An Introductory Handbook*, AGPS, Canberra.