Regulation affects every aspect of our daily lives. The homes we live in, the products we use, the entertainment we enjoy and the work we do are all governed by regulation. Similarly, every aspect of running a business is controlled by regulation. Whether it is a small business or a large corporation, regulations govern how people work, the goods they make, the services they provide and the ways in which those goods and services can be marketed and sold. Regulation is pervasive, yet it is also vital to the running of complex economies and societies and much regulation has laudable policy objectives. But even where regulation has been put in place for apparently sound reasons, there is no guarantee that it is good regulation. Nor should we assume that regulation is the best way to achieve our goals, nor the best response to every problem or potential problem we see. Regulation is in fact a high-cost option. Every regulation imposes a cost: on the Government administering it; on those regulated; and on the economy as a whole. We must be certain, therefore, that whenever regulation is imposed, its benefits clearly outweigh its costs. Regulation can fail in two ways. It can be put in place when it is not needed; and, even where regulation is the right option, it can be poorly designed or badly administered. The costs of such regulation are not outweighed by their benefits and they add a significant deadweight to the economy, sapping the strength of Australian businesses and undermining our competitiveness. To remain competitive, Australia must remove this unnecessary burden on the economy. At its worst, regulation can undermine the very bases of successful liberal democracies. As the amount of regulation blows out and as systems of scrutiny and accountability fail under the weight of regulation, the fundamental principle of the rule of law, including equality before the law and protection of property rights, is eroded in favour of regulatory expediency and micro-management of society and the economy.Similarly, a recent poll by the UK's Centre for the Study of Financial Innovation found that excessive regulation is seen by the world's major banks, insurers and funds managers as the biggest risk facing the financial sector. The Centre's report found that 'regulatory overkill saps bank resources, reduces risk diversification and creates a false sense of security.' Over-regulation and poor regulation are major issues for Australia. By global standards, Australia is far from having the worst regulatory environment. Among OECD countries, Australia is a world leader in some areas, but lags significantly behind in others. The fact that the regulatory environment for business is worse in many countries is no reason for complacency. Our competitors are engaged in reform programs to reduce the quantity and improve the quality of business regulation. This will encourage innovative, entrepreneurial businesses, improving the competitiveness of their economies and increasing their competitive advantage. If Australia is able to implement better

Business Regulation Action Plan

FOR FUTURE PROSPERITY

Business Council of Australia

Contents

Preface

The Business Council of Australia (BCA) represents the Chief Executives of 100 of Australia's leading companies. The BCA's objective is to develop and advocate, on behalf of its Members, public policy reform that positions Australia as a strong and vibrant economy and society. The companies that our Members lead represent a significant share of Australia's domestic and overseas business activity. They therefore have a significant interest in Government policy, the direction and scope of economic reform and Australia's future prosperity.

Australia is experiencing one of its most prosperous periods for several decades. This has delivered economic wellbeing and high living standards to more and more Australians. But behind this comfortable position lie a number of vulnerabilities. Serious constraints and imbalances are emerging within the economy that, in the absence of reform in key areas, will slow growth, limit opportunities and undermine the economy's capacity to deal with longer-term challenges. The challenges of population ageing and ever-increasing competition from global markets are but two examples.

Economic reform by successive Governments over the last two decades has contributed substantially to our current prosperity. The success of these past reforms points to the fact that continual reform, while often difficult to implement, is directly related to a nation's ongoing economic wellbeing. The BCA's central message is therefore this: Australia must act now to make further fundamental reforms to lock in its current prosperity and create the conditions for sustainable growth over the long term. To help achieve this goal, the BCA proposes an integrated action agenda focused on four areas: workplace relations, taxation, regulation and infrastructure development. Each will play a major role in determining the rate of Australia's future growth; however each on its own cannot deliver the answer. Only a combination of these reforms can maximise Australia's economic position and prosperity in the long run.

This *Action Plan* sets out the BCA's proposals for achieving significant reform in the key area of regulation.

Australia must act now to make further fundamental reforms to lock in its current prosperity and create the conditions for sustainable growth over the long term.

About the Action Plan

This BCA *Action Plan* is aimed at achieving significant reform in the key area of business regulation.

Business Regulation Action Plan for Future Prosperity sets out the steps Australia's business leaders and leading companies believe are needed to improve significantly business regulation in Australia. It draws conclusions from both the *Options Paper*, and the *Access Economics Report*, presented as Appendixes to this *Action Plan*.

Appendix 1: *Options for Improving Business Regulation* (referred to here as the *Options Paper*) identifies areas in need of reform and the options available to improve the quality and reduce the quantity of business regulation in Australia.

Appendix 2: *Benefits & Costs of Regulation*, Report by Access Economics Pty Limited for the Business Council of Australia, (referred to here as the *Access Economics Report*) was commissioned to assess the state of business regulation in Australia. It highlights the many regulatory problems faced by businesses in Australia today.

Many other countries have recognised the need to reform business regulation to keep their businesses competitive. If Australia does not match these efforts, we will fall behind and economic growth will slow.

Executive Summary

Australia is enjoying a remarkable period of economic growth, delivering greater prosperity to most Australians. One of the reasons for this growth and prosperity is that we have been prepared to make hard decisions in the past, particularly decisions to free the market from regulation and restrictions. But we cannot afford to be complacent. Even as we enjoy the rewards from past deregulation and regulatory reform, more and more regulation is being imposed on Australian businesses, diverting their resources and undermining their competitiveness. At its worst, this tide of regulation is corroding the fundamental principles that underpin successful liberal democracies; principles such as the rule of law, including equality before the law and protection of property rights.

No one knows exactly how much regulation is in place in Australia, but judging by what we do know, regulation at the Commonwealth and State levels is growing at around 10 per cent per annum, more than twice the rate of Australia's economic growth. Much of this regulation imposes costs on businesses and restricts the ability of businesses to respond quickly to market opportunities and threats. These costs are passed on to customers or shareholders, or have to be offset by cost reductions in other areas, such as employment costs.

Many other countries have recognised the need to reform business regulation to keep their businesses competitive. If Australia does not match these efforts, we will fall behind and economic growth will slow.

If we can surpass the efforts of other countries, Australia's business regulatory environment will be a source of competitive advantage, making Australian businesses more competitive and attracting more foreign investment into Australia.

The BCA has undertaken detailed research into how other countries are meeting the regulatory challenge. *Options for Improving Business Regulation* (Appendix 1: *Options Paper*) examines regulatory reform initiatives being put in place in comparable countries and how they might be adopted in Australia.

Based on the results of this research, the BCA has developed this *Action Plan* to reduce and improve business regulation.

The *Action Plan* sets out the steps Australia's business leaders and leading companies believe are needed to improve significantly business regulation in Australia. The first step is to fix the system that continues to produce poor business regulation. The second step is to clean up the existing stock of regulation, weeding out redundant, inefficient and inconsistent regulation. The third step is to seriously tackle a long-term problem in Australia – the overlapping and inconsistent regulation of the different layers of Government.

Regulation imposes costs on businesses and restricts the ability of businesses to respond to changing market conditions.

The *Action Plan* provides detailed recommendations for achieving Step One, and foreshadows the further reforms needed at Steps Two and Three.

As a starting point, all Governments should adopt eight basic principles in developing, administering and reviewing business regulation:

- Regulation should be the last, not first, response of Government and the benefits of proposed regulation should always be shown to outweigh the costs of administration and compliance.
- Regulation should set a framework, not try to cover the field.
- Regulation has a use-by date, after which it may no longer be necessary or appropriate.
- The current law should always be tested and enforced before more law is added.
- Governments should not impose regulation upon private persons or companies that they are themselves not prepared to adopt.
- All businesses, whether large or small, private or public, should be treated equally.
- Where property rights are affected by regulation, there should be just compensation.
- There must be full transparency and accountability around the processes for making and administering regulation.

These principles should guide Governments when they are considering introducing regulation, when they are choosing the best regulatory response and when they are assessing whether existing regulation is still the best way of achieving desired policy goals. Businesses and others should also use these principles to test and challenge the regulations to which they are subject.

The first practical step towards better business regulation is to fix the systems that continue to produce poor regulation. The initial focus of the BCA's *Action Plan* is on the Commonwealth Government. This does not suggest that the Commonwealth level is where the greatest need for improvement lies. Nevertheless the Commonwealth is well placed to be the leader in terms of improving its regulation-making processes and hence its regulation. For this reason, it is a simpler matter to bring the Commonwealth system into line with world's best practice. The revised Commonwealth system then provides a model for State Governments to adopt. The BCA will be actively encouraging this adoption. State Governments also have a responsibility for improving the coordination of regulation between jurisdictions and for tackling the plethora of poor, redundant and overlapping regulation at the level of Local Government. In terms of increased productivity and better economic outcomes for Australia, most reforms are likely to be needed at the State and Local Government levels and where regulatory responsibility is shared across jurisdictions.

To fix the current system of business regulation, the BCA recommends:

- Creating a Ministerial Task Force, similar to that in the UK and the Netherlands, to act as a 'gatekeeper' to prevent proposals for new business regulation being considered by Government unless the benefits of the proposed regulation clearly outweigh the costs.
- Establishing a Business Regulation Advisory Council to advise the Government on priorities for regulation reform, including Commonwealth, State and Local regulation that should be removed or substantially improved.
- Creating a champion for better business regulation within Government through enhancing the role and powers of the Office of Regulation Review to challenge the need for new regulation affecting business and to oversee the cost-benefit analyses of regulatory proposals.
- Legislating the requirement that all regulatory proposals likely to have a significant impact on business must undergo a detailed regulatory impact assessment to ensure the benefits of the regulation clearly outweigh the costs.
- Requiring the Minister proposing new business regulation to personally certify that the benefits of the regulation will outweigh the costs.
- Introducing a two-stage impact assessment process, with all regulations likely to affect business subject to a preliminary assessment, and all regulations likely to have significant impacts on business subject to full assessment.
- Requiring the release of draft regulatory impact statements for public comment and allowing sufficient time for consultation to make that consultation meaningful.
- Developing a standardised, sophisticated methodology for identifying and measuring the likely costs to business of proposed regulations.

Regulation: a growth industry

- In 2003, there were 1,800 Commonwealth Acts of Parliament in place, 170 of which had been passed in the previous year – a growth rate of 10.4 per cent per annum.
- In the four years from 2000 to 2003, the Commonwealth Parliament passed the same volume of primary legislation as it passed in the sixty-nine years from 1901 to 1969.
- During that same period, the Commonwealth Parliament passed on average 350 pages of new primary legislation each sitting week, or nearly 100 pages each sitting day.
- At the beginning of 2005, there were 1,300 NSW State Acts of Parliament in place, 115 of which had been passed in the previous year – a growth rate of 9.7 per cent per annum.
- During 2000–2003, the NSW Parliament passed 300 pages of Acts, Rules, Regulations and By-laws each sitting week.
- In 2003, the State with the greatest volume of new legislation, Queensland, added another 8,700 pages of laws and rules. South Australia, with the lowest volume, still added another 1,001 pages to its laws.
- In 2004, there were 69 State-based business regulators in Victoria alone, administering 26,000 pages of regulation.
- The OECD estimates that the compliance cost of regulation for small and medium-sized Australian businesses in 1998 was more than $17 billion.
- In 2001–02, the Commonwealth Government spent $4.5 billion on the administrative costs of Commonwealth regulatory bodies.

SECTION

1

Introduction

Regulation affects every aspect of our daily lives. The homes we live in, the products we use, the entertainment we enjoy and the work we do are all governed by regulation. Similarly, every aspect of running a business is controlled by regulation. Whether it is a small business or a large corporation, regulations govern how people work, the goods they make, the services they provide and the ways in which those goods and services can be marketed and sold.

Regulation is pervasive, yet it is also vital to the running of complex economies and societies and much regulation has laudable policy objectives. But even where regulation has been put in place for apparently sound reasons, there is no guarantee that it is good regulation. Nor should we assume that regulation is the best way to achieve our goals, nor the best response to every problem or potential problem we see. Regulation is in fact a high-cost option. Every regulation imposes a cost: on the Government administering it; on those regulated; and on the economy as a whole. We must be certain, therefore, that whenever regulation is imposed, its benefits clearly outweigh its costs.

Regulation can fail in two ways. It can be put in place when it is not needed; and, even where regulation is the right option, it can be poorly designed or badly administered. The costs of such regulation are not outweighed by their benefits and they add a significant deadweight to the economy, sapping the strength of Australian businesses and undermining their competitiveness. To remain competitive, Australia must remove this unnecessary burden on the economy.

At its worst, regulation can undermine the very bases of successful liberal democracies. As the amount of regulation blows out and as systems of scrutiny and accountability fail under the weight of regulation, the fundamental principle of the rule of law, including equality before the law and protection of property rights, is eroded in favour of regulatory expediency and micro-management of society and the economy.

The BCA has developed this *Action Plan* to achieve the lighter touch business regulation needed to ensure Australia continues to improve its international competitiveness. The *Action Plan* draws upon and is complemented by two major reports featured as Appendixes.

The *Options Paper* is a BCA research paper that examines a wide range of options for reforming business regulation, drawing on practical experience overseas and the detailed assessments of the OECD. See Appendix 1.

The *Access Economics Report* examines in detail the current state of business regulation in Australia and how Australia compares with its competitors and nations with similar economies. It also highlights the areas where poor regulation occurs, the mistakes regulators make and the weaknesses in the current regulation-making process. See Appendix 2.

It is clear that there is considerable scope for improving the quantity and quality of business regulation in Australia, reducing costs and removing impediments to innovative, competitive businesses. This *Action Plan* sets out how this can be done.

> Even where regulation has been put in place for apparently sound reasons, there is no guarantee that it is good regulation.

Among OECD countries, Australia is a world leader in some areas, but lags significantly behind in others.

SECTION

2 Australia's Regulatory Environment

Over-regulation is a globally recognised problem. PricewaterhouseCoopers recently surveyed more than 1,300 Chief Executives from around the world to identify some key business growth opportunities and challenges. Overwhelmingly, the CEOs saw the number one threat to business growth as over-regulation, ahead of increased competition, loss of key talent, reputational risk and terrorism.[1]

Similarly, a recent poll by the UK's Centre for the Study of Financial Innovation found that excessive regulation is seen by the world's major banks, insurers and fund managers as the biggest risk facing the financial sector. The Centre's report found that 'regulatory overkill saps bank resources, reduces risk diversification and creates a false sense of security.'[2]

Over-regulation and poor regulation are major issues for Australia. By global standards, Australia is far from having the worst regulatory environment. Among OECD countries, Australia is a world leader in some areas, but lags significantly behind in others (see Exhibit 1). The fact that the regulatory environment for business is worse in many countries is no reason for complacency. Our competitors are engaged in reform programs to reduce the quantity and improve the quality of business regulation. This will encourage innovative, entrepreneurial businesses, improving the competitiveness of their economies and increasing their competitive advantage. If Australia is able to implement better business regulation reform than other countries, this in itself will be a source of competitive advantage.

The fundamental goal of regulatory reform is to improve national economies and enhance their ability to adapt to change.

The OECD has set out the challenge we face very clearly:

'The fundamental goal of regulatory reform is to improve national economies and enhance their ability to adapt to change. Regulatory and structural reforms are complementary to sound fiscal and macroeconomic policies, which alone are not sufficient for growth in an increasingly globalised economy. In times of profound and rapid social, economic and technological change, Governments have to consider the cumulative and inter-related impacts of regulatory regimes to ensure that their regulatory structures and processes are relevant, robust and forward-looking. Countries now understand that regulatory reform is not a one-off effort, accomplished once and for all, but a dynamic, long-term, multi-disciplinary and pro-active policy.'[3]

EXHIBIT 1: AUSTRALIA'S MIXED REPORT CARD

In 2004, the World Bank assessed the regulatory performance of 137 countries. The comparison shows that Australia led the world in some areas, but falls well down the rankings in others. Of particular concern, from the point of view of the competitiveness of Australian business, is that Australia ranks poorly in terms of the cost of doing business.

Where Australia rates highly:	**World ranking**
• Starting a new business – number of procedures and time needed	1st
• Employment – ease of hiring new staff	1st
• Enforcing a contract – number of procedures needed	1st
• Registering property – number of days required	6th
Where Australia rates poorly:	
• Starting a new business – cost	11th
• Employment – rigidity of laws governing hours worked	23rd
• Enforcing a contract – cost	44th
• Registering property – cost	62nd

Source: World Bank (2004), *Doing Business in 2004: Understanding Regulation*.

2.1 | THE REGULATORY 'BLOW OUT'

Lightly regulated advanced economies are more efficient, productive, flexible and better able to withstand economic shocks than those encumbered by inefficient, costly and redundant regulation. Australia already has considerable experience with deregulation and we are currently enjoying the economic benefits of those past reforms (see Exhibit 2). Much of this deregulation focused on removing economic regulation; that is, removing those rules and laws that govern and restrict how the economy works. While few of these regulations now remain, the overall amount or stock of regulation in Australia has continued to grow (see Figures 1–3). This creeping tide of regulation threatens the progress we have made in the past. Its effects are as costly and restrictive as those of the economic regulations that Australia has worked hard to remove (see Exhibit 3).

This problem is pervasive, with the amount of regulation continuing to grow at the Commonwealth, State and Local Government levels. As the *Access Economics Report* shows, there were 1,800 Commonwealth Acts of Parliament in place in 2003, 170 of which had been passed in the previous year. This is a growth rate of 10.4 per cent per annum (in comparison, the national economy grew by 4.3 per cent in 2003).

In the four years from 2000 to 2003, the Commonwealth Parliament passed as many pages of legislation as were passed from 1901 to 1969, even though during this 69-year period, Australia experienced the creation of the Commonwealth, both World Wars, the Depression, post-war reconstruction and the changes of the 1960s.

In NSW, the picture is similar, with over 1,300 State Acts and more than 650 principal statutory instruments in force at 1 January 2005. In 2004 alone, 115 new Acts and 625 new regulations were added. In addition, there were 5,500 Local Government planning instruments in place.

In 2003, the Commonwealth and State Parliaments added another 33,000 pages of legislation to the existing laws of Australia. Not all of these laws, rules and regulations affect business, but many do.

In Victoria, the Victorian Competition and Efficiency Commission has identified 69 State-based business regulators who, as at November 2004, administered a combined total of 170 Acts of Parliament, totalling over 19,600 pages of regulation. There were a further 176 regulations associated with these Acts, adding a further 6,400 pages.

Given that most businesses are affected by regulation imposed at the Commonwealth, State and Local Government levels, this adds up to a complex and costly regulatory environment. The conclusion then is that while overall Australia could be doing a lot worse in terms of business regulation, it could also be doing a lot better.

2.2 | CONSEQUENCES OF THE REGULATORY 'BLOW OUT'

The volume of new laws passed each year by State and Commonwealth Governments has nearly doubled since the 1980s. The sheer volume of legislation means it is inevitable that we will see more and more inappropriate and perverse regulation, as the amount of legislation far outstrips the capacity of the systems designed to ensure its quality. So much legislation is now being produced each year that it overwhelms the ability of Parliaments to consider it properly, the ability of legislative drafters to produce it carefully and the ability of regulators to administer it fairly and effectively. As a result, we continue to see examples of duplicative, poorly drafted and unenforceable regulation, such as those highlighted in Section 4 of this *Action Plan*.

But beneath the examples of perverse and sometimes ludicrous regulation lies a more disturbing trend. As the amount of regulation explodes, straining the capacity of Parliaments and others to maintain scrutiny and control, there is an increasing tendency to put political and bureaucratic expediency ahead of the basic principles than underpin our successful society and economy.

Australia's social and economic success is built on a number of basic principles, common to successful liberal democracies. These well-known principles include the rule of law, the separation of powers, equality for all before law and property rights. While Governments in Australia often proclaim the importance of these principles, there is a growing tendency to disregard them when it comes to making new laws and regulation.

Of particular concern are the serious assaults on the rule of law. The rule of law restrains the ability of Governments to act arbitrarily, assures equality for all before the law and ensures due process in legal proceedings. Increasingly, these concepts are being ignored in favour of regulatory expediency.

For example, Governments are increasingly introducing laws that mean a company director or executive is deemed to be individually liable for an offence when their company is found liable for that offence, effectively reversing the onus of proof and overturning the precept that an individual is innocent until proven guilty.[4] The arguments usually put for such provisions are that it is too hard for regulators to properly investigate and prosecute alleged breaches of the law and that directors and senior executives are capable of looking after themselves when facing such prosecutions. In reality, it means that company directors and executives are having their rights to be treated equally before the law eroded.

Another example of regulatory expediency winning over basic principles is the argument that regulators should have fining powers, rather than have to prosecute cases before the courts. The Australian Securities and Investments Commission (ASIC), for example, has recently been given powers to fine companies for alleged failures to disclose material information to the market. While companies can refuse to pay these fines, there are strong incentives in place for companies to pay, rather than challenge, them. In effect, this means it is the regulator rather than the courts that are determining when laws are being breached.

This attack on the basic principles of our society, in the interests of political and bureaucratic expediency, can only continue while it is shrouded by the sheer volume of laws being pushed through by Governments. This volume of law is also resulting in poorly considered and drafted legislation that results in unintended consequences. When the effects of this regulatory 'blow out' are combined with the cost burden on the economy of poor regulation identified above, the need for fundamental reform of how Governments at all levels develop and administer regulation becomes urgent.

There is an increasing tendency to put political and bureaucratic expediency ahead of the basic principles than underpin our successful society and economy.

EXHIBIT 2: THE BENEFITS OF LESS REGULATION

The past few decades have seen major reforms in the regulatory area.[5] Since those reforms began to take hold, Australia has experienced strong economic growth and prosperity. The Australian economy has outperformed those of the US and Europe. Unemployment has fallen dramatically and the number of long-term unemployed has more than halved. Interest rates and inflation remain at historical lows. Real wages have grown 13 per cent since 1996. Australia has moved from 15th in the OECD in terms of GDP per capita in 1990 to 8th in 2002.

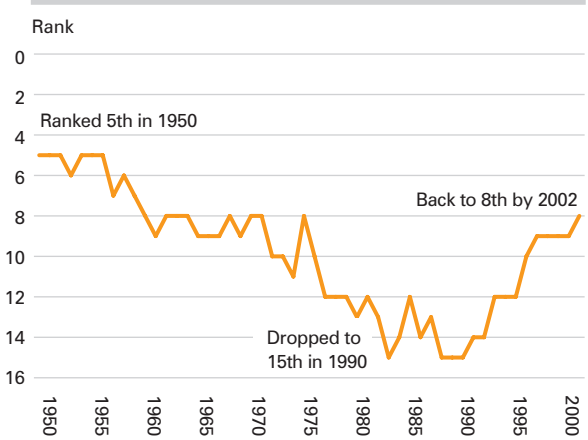
Just as the costs of regulation are hard to quantify precisely (see Exhibit 3), so are the benefits of deregulation. The weight of evidence, however, is that those economies that deregulate and have a light-handed approach to regulatory intervention, strongly outperform economies weighed down with regulation.

The World Bank, for example, has shown that those countries with the highest levels of business regulation also have the lowest levels of labour productivity. Not surprisingly, the greater the amount of regulation, the higher are costs for business and the longer the delays in getting business activity approved. These costs are passed on, to customers or shareholders, or through businesses cutting costs in other areas, including their employment costs.

In Australia, the Productivity Commission has estimated that improvements in productivity flowing from microeconomic reforms, such as the deregulating reforms of National Competition Policy, have benefited the average Australian household by $7,000. Productivity improvements and price changes in infrastructure sectors have created a permanent increase of 2.5 per cent in Australia's GDP, equivalent to around $20 billion.

Reform in particular sectors also leads to improvements. The Productivity Commission estimates, for example, that reform of building codes towards performance-based codes has significantly reduced construction costs. For example, the design cost of Federation Square in Melbourne was estimated to be around $18 million lower due to these changes.

AUSTRALIA'S GDP PER HEAD – RANK WITHIN OECD



Sources: World Bank (2004), *Doing Business in 2004: Understanding Regulation*; Productivity Commission, *Review of National Competition Policy Reforms – Discussion Draft*, October 2004; Business Council of Australia, *Preliminary Submission to the Productivity Commission on the Review of National Competition Policy Arrangements*, June 2004; Productivity Commission Research Report, *Reform of Building Regulation*, 2004.

EXHIBIT 3: THE COST OF MORE REGULATION

Regulation imposes costs on business, particularly the costs of complying with regulation, but also the cost of lost opportunities due to regulatory restrictions or encumbrances (such as time delays from approval processes, which can prevent a company expanding its production capacity to meet new markets). Regulation also imposes costs on Government, notably the costs of administering and enforcing the regulations. Regulation also imposes costs on the economy as a whole, for example, through reducing the competitiveness of business and through higher Government taxes and charges.

While these costs are well known, they are not easily quantified. One of the reasons for this is that regulation is so entwined in everything that businesses do, it becomes impossible to separate out the costs caused by regulation from the normal costs of doing business. The OECD has estimated that the direct compliance costs of regulation for small and medium-sized Australian businesses in 1998 was more than $17 billion. This had grown significantly from a Productivity Commission estimate that the administrative burden of regulation on business in 1994–95 was $11 billion, of which 85 per cent was borne by small to medium-sized enterprises.

The Australian Industry Group's survey of manufacturing firms, *Compliance Costs Time & Money*, estimates that the time taken by manufacturers for regulatory compliance cost them over $680 million a year, with the cost burden falling particularly heavily on small and regional companies. The Housing Institute of Australia has estimated that the costs of regulation add an estimated $60,000 to the cost of a house in western Sydney. The Productivity Commission has found that, in 2001–02, the estimated incremental administrative and compliance costs for general practitioners (GPs) from Commonwealth policies and programs amounted to about $228 million (equivalent to about $13,100 per GP per year).

A survey by the Victorian Automobile Chamber of Commerce of the retail motor trade shows that regulatory compliance is a significant burden. The survey respondents, 90 per cent of whom were small businesses employing 20 or less people, reported that businesses on average were spending over 11.6 hours a week just on regulatory compliance, with the bulk of the burden falling on the owner of the business. The survey also found that in the past five years, the regulatory burden had increased for 86 per cent of businesses. Finally, survey respondents reported that, if business regulation had been reduced by 50 per cent, as promised by Government, there would be more time to run the business, stress levels would be lower and profits and productivity higher.

CONTINUED >

EXHIBIT 3: THE COST OF MORE REGULATION continued

Even one piece of legislation can have significant costs. Westpac estimates, for example, that proposed legislation on anti-money laundering will cost the bank up to $25 million over three years. Even though the legislation has not yet been passed, the bank has already spent over $7 million in anticipation of the new regulation.

The Productivity Commission has identified at least $4.5 billion in administrative costs paid by taxpayers just to run Federal regulatory bodies in 2001–02.

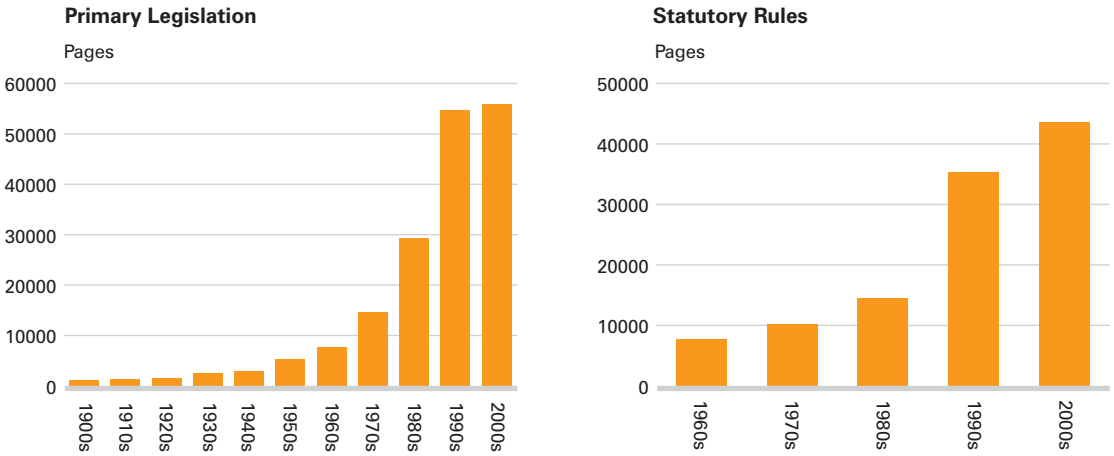
In the US, the Office of Management and Budget has estimated that the cost of federal regulation alone is about 8 per cent of US GDP. Analyses of the costs of regulation in Canada and Mexico give comparable figures and it is reasonable to assume that a similar figure applies in Australia.

Although difficult to measure precisely, the cost of regulation is far from negligible.

Despite the efforts of the past few decades to deregulate much of the Australian economy, the total level of legislation continues to grow unabated at the Commonwealth, State and Local Government levels. The charts below show the number of pages of legislation passed each decade by the Commonwealth and the States. Figures for the current decade are extrapolated from actual figures for 2000–2003.

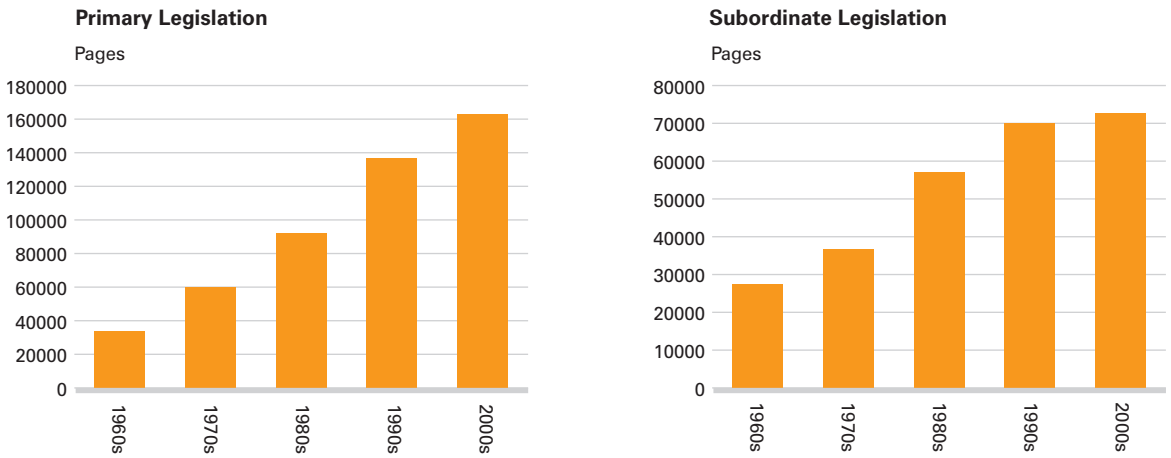
THE REGULATORY 'BLOW OUT'

FIGURE 1 **GROWTH IN COMMONWEALTH LEGISLATION**



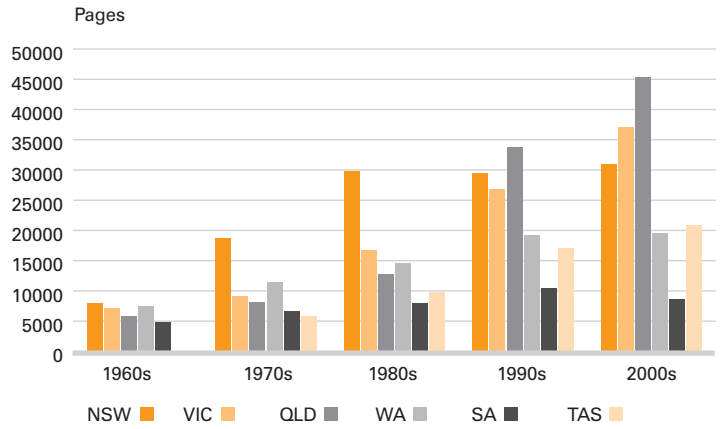
THE REGULATORY 'BLOW OUT'

FIGURE 2 **GROWTH IN TOTAL STATE LEGISLATION***



* not including Territories

FIGURE 3 **GROWTH IN PRIMARY LEGISLATION BY STATE**



Source: Appendix 2: *Access Economics Report*; *Australian Financial Review*, 9 March 2005, p. 54; Productivity Commission Research Report, *General Practice Administrative and Compliance Costs*, 2003; Victorian Automobile Chamber of Commerce, *Survey of Business Compliance Costs*, 2003; analysis of Commonwealth and State Legislation.

SECTION

3 Principles of Better Business Regulation

This *Action Plan* puts forward proposals to reduce the quantity and improve the quality of business regulation in Australia. As a starting point, there are eight principles that should guide the development of new regulation and the review of existing regulation. These principles, set out in the following Sections, provide a firm foundation for improving Australia's competitiveness through improving its business regulation.

3.1 | REGULATION IS A LAST, NOT FIRST, RESPONSE

Markets are not always perfect, but neither are regulations. Too often, Governments and the broader community assume that whenever a market failure can be identified or predicted, regulation is required.

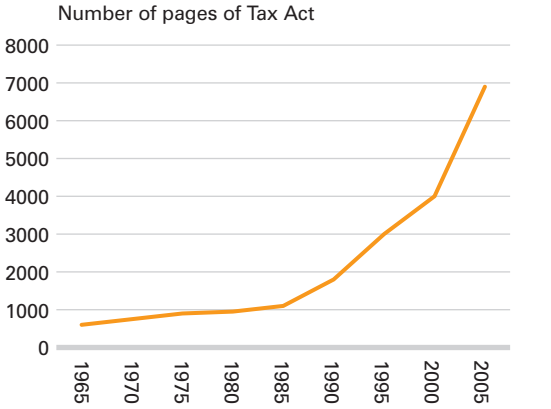
The ultimate test of when to regulate should not be whether the market is operating perfectly, but whether regulation will in fact provide a better outcome. There should be no assumption that a regulatory response is necessary even where a market failure is perceived, particularly where that market failure may only be temporary. The onus should, instead, be on the regulator to demonstrate that the benefits of regulatory intervention outweigh the costs imposed and that the market alone will not provide a solution.

When assessing the costs of regulatory intervention, the costs must include not only the costs to Government of administering and enforcing the regulation, but also the compliance costs to business, the costs to the broader economy and the costs of distortions in the market place caused by the regulation. No regulation should be imposed unless it is clear that the benefits of regulatory intervention outweigh the costs. In assessing the costs and benefits, consideration also needs to be given to how these are distributed. For example, if a few are to bear the costs of regulation for the benefit of the many, how should the few be compensated for these costs?

3.2 | REGULATION SHOULD SET THE FRAMEWORK, NOT COVER THE FIELD

Regulation should be simple, clear, well explained and sensitively enforced. Regulators too often attempt to prescribe rules for all eventualities, leading to complex and confusing regulation, with higher compliance costs and a greater incidence of businesses unknowingly or unwittingly breaching the law. The classic and well-known example is Commonwealth tax legislation, where constant attempts to refine the scope and reach of the law have led to an explosion in the size of the tax laws (see Figure 4).

FIGURE 4 **GROWTH OF TAX LAW IN AUSTRALIA**



Source: Productivity Commission.

Rather than attempting to cover the field, regulations should establish the framework for the performance or conduct that is required of regulated businesses. Businesses should have the flexibility to achieve the objectives of the regulation in the manner most suitable to their circumstances and regulators should have the discretion to accept a range of valid approaches to compliance. The system should also allow for appeals, with cases tested not against whether a business has complied strictly with detailed, black letter law, but whether the business has taken all reasonable steps to achieve the objective required. An example of this approach is the ASX Corporate Governance Council *Principles of Good Corporate Governance and Best Practice Recommendations*. The guidelines set out the principles that listed companies should consider as part of their corporate governance practice, but do not prescribe how companies should satisfy those principles. The only 'regulatory' requirement upon them is to disclose if and how they apply the principles, and why their approach is suitable to the company's situation.

Overly prescriptive regulation not only adds significantly to business costs and unnecessarily dampens innovation in the market, but also creates an environment where the regulated increasingly believe that, if something is not specifically prohibited, it must be allowed. This detracts from businesses applying acceptable standards of ethics to their conduct. It also means Governments and regulators are fighting a constant losing battle to pass more and more legislation as some in business seek more novel ways of getting around black letter rules.

3.3 | REGULATION HAS A USE-BY DATE

Even where regulating is justified and produces a better outcome than not regulating, it cannot be assumed that today's solution will be right in future. As a matter of principle, it should instead be assumed that any regulation is necessary and effective for only a finite period of time. The faster-paced the industry, and the more complex its products and services, the greater is the risk that regulation will quickly date and its costs come to outweigh its benefits. In areas such as financial services, where new products and services are evolving all the time, regulation quickly becomes an inhibitor of legitimate competition and business innovation.

Ideally, all regulation should be subject to a legislatively defined sunset clause. For major pieces of legislation, however, such as the *Corporations Act* or *Trade Practices Act*, this would be too disruptive. Instead, these pieces of legislation should be subject to regular public reviews to ensure they remain relevant and achieve their policy goals in the most effective and efficient ways.

All business regulation that has been introduced to achieve a specific goal, however, should be subject to a legislatively defined sunset clause, requiring the regulation to be publicly reviewed and reapproved by Parliament, or lapse upon reaching its sunset date. A recent and topical example of such regulation is the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (CLERP 9), which amends the Corporations Act by prescribing steps to be taken by companies to improve their corporate governance. Whatever the merits of the legislation today, the detail of what is good corporate governance will vary over time, as market dynamics and expectations change. There is therefore no guarantee that the prescribed approaches to corporate governance in the CLERP 9 Act will remain best, or even good, practice in the years to come. The CLERP 9 Act provides a good example of primary legislation that should be subject to a sunset clause.

The Business Council recognises that the Commonwealth Government has already taken some steps towards introducing sunset clauses for regulation through its *Legislative Instruments Act 2003*. The Act requires some forms of regulation to be reviewed and remade after ten years, or else they lapse. The Act has a narrow scope, however, applying only to regulation made through power delegated by Parliament. In other words, the sunset provisions do not apply to primary Acts or disallowable subordinate legislation such as regulations that are put before Parliament. The bulk of business regulation is therefore not subject to a sunset provision and is only occasionally reviewed. There are few safeguards therefore to ensure regulation remains necessary, relevant and the most efficient way of achieving policy objectives.

The faster-paced the industry, and the more complex its products and services, the greater is the risk that regulation will quickly date and its costs come to outweigh its benefits.

3.4 USE THE CURRENT LAW BEFORE ADDING MORE

Introducing new regulation is an easy option for a Government that feels it needs to be seen to be doing something to deal with an issue, particularly when faced with community or media calls for immediate action.

Governments are often seen as having only two tools to achieve public policy outcomes: they can legislate (the 'stick') or they can provide incentives, particularly financial ones (the 'carrot'). Of these, legislating has strong appeal as it is seen, superficially, as the lowest-cost option.

Governments also have the option of doing nothing. Unfortunately, it is an option that seems to be rarely taken. A Government can legitimately choose to do nothing when the existing law is, or should be, adequate to deal with a particular issue or controversy. Governments should therefore adopt the principle that new regulation will not be introduced until the adequacy of the existing laws has been fully tested.

New regulation should also not be introduced when the existing requirements are not being adequately enforced. In some areas, such as food regulation, there has been a tendency to repeatedly review and introduce new regulations governing how food is prepared and handled, rather than focusing on enforcing the laws that are already in place.

While health concerns demand rules for how food is prepared, the constant reviewing of the rules and addition of new layers of regulation is counterproductive. It adds unnecessarily to costs and undermines the integrity of the regulatory system (especially where businesses see a new regulation coming in, knowing that it is likely to change in the foreseeable future).

These problems are compounded when the regulations are poorly enforced. The majority of businesses, seeking to be fully compliant with regulatory requirements, are left to bear the burden of an excessive regulatory regime, while a small minority of businesses will seek to capitalise on poor enforcement and pursue a commercial advantage by disregarding the regulations. Poor enforcement also suggests that new regulations are being introduced to address failings in the system that arise from that poor enforcement rather than gaps in the regulatory regime. It is not possible to determine what new regulations are actually needed unless the existing system is being fully enforced. Only then can the adequacy of the existing regulations be properly assessed. As a matter of principle, therefore, no new regulation should be brought in prior to testing that the existing regulatory regime is being actively and effectively enforced.

3.5 IF IT IS GOOD ENOUGH FOR US…

Enforcement also means that Governments have to show commitment to their own regulations by providing regulatory agencies with sufficient resources to fulfil the duties given to them by Government. Where Governments fail to provide adequate resources to administer regulation, it is legitimate to question the merit of the regulation in the first place. If the amount of regulation is out of step with the resources provided by Government to administer and enforce that regulation, then either the resources need to be increased, or the regulation needs to be removed.

A corollary of this principle is that more regulation does not stop law breakers, but does penalise those who abide by the law. As a general rule, it is not feasible to legislate against dishonesty. The correct response to this sort of behaviour is to prosecute vigorously the existing laws rather than immediately turn to more regulation.

Existing laws should be prosecuted vigorously before more laws are added.

It is the role of Governments to govern on behalf of the wider community. One way Governments do this is to impose regulations upon individuals and enterprises to acheive policy objectives that are seen as desirable by the community.

In a range of areas, however, Governments prescribe the activities of others, but exempt themselves from their own requirements. For example, local councils will often exclude themselves from the planning development requirements they impose on individuals and enterprises in their districts.

In the interests of fairness and to ensure the costs of accountability are fully understood, Governments should not impose regulation upon private persons or companies that they are themselves not prepared to adopt. As well as improving the consistency of the regulatory system, this would give Governments a greater appreciation of the burden they impose on others when they introduce regulation. The minds of regulators will be more focused on the regulatory burden when they themselves experience it.

3.6 EQUALITY BEFORE THE LAW

Just as regulations should apply equally to private or public interests when they are engaged in comparable activities, so too should rules apply equally across all businesses. For example, there should not be one set of rules for large corporations and another for small businesses. This is not to say that one set of rules fits all businesses in all circumstances. Listed companies, for example, have additional obligations arising from the public nature of trading in their equities. Too often, however, a new regulatory requirement is introduced, but some sectors and businesses are exempted. The rationale usually advanced is that the new regulation will impose too great a cost burden on those businesses seeking exemption. For example, most small businesses are exempted from the Commonwealth's privacy law, in part because of concern with the costs of compliance.

In effect, when small business is given an exemption from regulation on cost grounds, it is being assumed by the regulator that larger businesses are able to absorb these costs, as if the costs then disappear. In reality, of course, these costs are passed on, to customers or shareholders, or through businesses cutting costs in other areas, including their employment costs.

If the cost burden to some businesses is so great that they need to be exempted from new regulation, then there must be a serious question over whether the costs to all businesses justify any benefits arising from the regulation.

Treating different classes of companies in different ways can also lead to distortions in the market. For example, while some additional requirements may be appropriate for publicly listed companies, Governments need to be wary of imposing such a high regulatory burden on publicly listed companies that companies are discouraged from listing, or seek to go private, creating a market distortion in favour of private companies. Excessive restrictions on public companies, for example, can discourage investment in those companies, increasing their costs of capital. The BCA has previously expressed concern in the context of corporate governance regulation that the growing gap between public and private companies is having such an effect.

Governments should adopt the principle that regulation will be non-discriminatory between business in different sectors and between businesses of different size. Where Government believes there is some justification for discriminatory treatment, the basis for that should be spelled out clearly in the legislation. Where Government exempts small business from new regulation on the grounds of an unreasonable cost burden, it should provide explicit justification for why the cost to medium and large businesses is justified.

3.7 | COMPENSATION WHEN PROPERTY RIGHTS AFFECTED

Regulation frequently impacts on the ability of a property owner to use his or her property. These regulations may have sound public policy goals behind them, but typically, those policy goals will be to the advantage of others, while the costs are borne by the property owner.

Where regulation significantly restricts the property rights of individuals or businesses, compensation should be paid. The Commonwealth Constitution already requires the Commonwealth Government to provide just compensation when it acquires property. A similar principle needs to be adopted by other levels of Government. Even where the impact on property rights is less than full acquisition, there should be a general principle that those benefiting from a restriction on property rights should compensate those bearing the cost of having their rights restricted.

Regulation that is developed through an open and accountable process is much less likely to impose unnecessary costs on the regulated and the broader economy.

3.8 | TRANSPARENCY AND ACCOUNTABILITY

The final principle for better regulation concerns the processes for making and administering business regulation. The BCA argues strongly that the more transparent and accountable those processes are, the better will be the resulting regulation.

Regulation that is developed through an open and accountable process is much less likely to impose unnecessary costs on the regulated and the broader economy. Consultative processes also allow the regulator to more accurately assess whether regulation is the appropriate response to an issue, and where it is, to develop regulation that achieves the policy objective in the simplest and least costly way.

One of the greatest grievances about regulation is that it is not always clear why regulations apply. This is a particular issue for small businesses, where the small business owner may invest considerable effort in meeting Government regulatory requirements, without any clear understanding of the benefits this is supposed to provide to the owner or anyone else (see Exhibit 4). Whenever Governments set or communicate regulatory requirements to businesses, they should clearly set out why the regulation is in place and the benefit that is to be derived from the business complying with the regulation.

EXHIBIT 4: TYPICAL SMALL BUSINESS REGULATORY COMPLIANCE OBLIGATIONS

Payroll Tax

- Calculated on taxable wages paid to employees, payable monthly by the seventh day of the following month.
- Annual reconciliation for the financial year to be completed by 7 July.

Pay as you go (PAYG) Tax

- Monthly lodgement of online activity statement. Lodgement and payment by 21st of following month.
- Payment summaries must be issued to employees by 14 July.
- Lodgement of PAYG withholding payment summary annual report to by sent to ATO by 14 August.

Goods and Services Tax (GST)

- Business Activity Statement to be lodged online every quarter and payments remitted.

Fringe Benefits Tax (FBT)

- Fringe benefit payments to be lodged on Business Activity Statement together with GST every quarter and payments remitted.
- Annual FBT return to be completed and sent to ATO by 21 May.

Superannuation

- Employees able to choose their own complying fund from 1 July 2005.
- Superannuation contributions to be made on a quarterly basis.

Workcover premium

- Estimate of rateable remuneration form to be completed by April to determine premiums for the following year.
- Declaration of rateable remuneration for the financial year to be lodged by 31 July to determine confirmed premium.

ASIC

- Annual report to be lodged by the end of October.
- Notification of changes in company details must be sent no later than 60 days.

Occupational Health and Safety (OH&S)

- 2004 Act came into force on 1 July 2005.
- Changes in consultation of employers with employees in health and safety issues and duties relating to incidents.

International Financial Reporting Standards (IFRS)

- The impacts on the financial reports prepared using the Australian equivalents to IFRS as of 1 January 2005.

SECTION

4 Why Does Regulation Go Wrong?

Business regulation, particularly the amount and quality of that regulation, has a significant impact on the competitiveness of Australian businesses and therefore on the economy as a whole. Poorly conceived, inefficient and redundant regulation can add unnecessarily to the costs of running a business, reduce productivity, stifle innovation and hamper business growth. In extreme cases, poor regulation can actually have the opposite effect to that intended (see Exhibit 5). These negative impacts on business flow through to the whole economy, dampening jobs growth and reducing Australia's ability to be internationally competitive.

The *Access Economics Report* was commissioned by the BCA to assess the state of business regulation in Australia and to identify areas where business regulation needs to be improved. That report, *Benefits & Costs of Regulation*, highlights the myriad of regulatory problems faced by businesses in Australia today (see Appendix 2).

The *Access Economics Report* shows that there are three risks from regulation:

1. Advocates of regulation tend to exaggerate the extent of market failures and underestimate the ability of markets to solve problems without regulation, or with less heavy-handed regulation. They also operate under an assumption, often false, that regulation will provide a better outcome than markets.
2. Advocates of regulation also tend to understate its costs. The costs of regulation include the obvious direct costs to business, the Government and the economy, but also many costs that are indirect, or arise from the failure of regulation to keep pace with changing circumstances.
3. The benefits of regulation fall unevenly as regulation often creates big winners (often vocal interest groups) and many small losers (ordinary Australians unaware of the costs of regulation). Because the losers are often diffuse, and may not be immediately aware of the costs imposed by regulation, there is a risk that regulation will be seen by Governments as the easy 'solution', with the lowest political cost. Such risks are high when politicians need a quick fix to get a crisis off the front page of a newspaper. Indeed, many studies note that regulation often ends up hurting both consumers and businesses by taking decisions away from them and leaving power in the hands of regulators and bureaucrats.

These risks would be overcome if the eight principles set out in the previous Section were embraced by Government and applied when regulations were being developed, administered and reviewed.

Overlapping or conflicting regulation can often create compliance disasters that regulators leave consumers and businesses to resolve.

The *Access Economics Report* identifies four common mistakes in regulation:

1. **Regulatory over-reach** – Regulators often over-estimate their ability to influence outcomes through regulation and develop regulations that aim to achieve more than is achievable, resulting in worse outcomes than in deregulated markets. This flaw is typically seen when regulation is overly prescriptive, overreacts to current 'hot' issues or is imposed but cannot be enforced. The *Access Economics Report* identifies the *Financial Services Reform Act 2001* and the Uniform Credit Code as recent examples of regulatory over-reach.
2. **Regulatory overlap** – Where regulations are allowed to pile on top of other regulations, there is a risk that the total cost of regulation will be greater than the sum of its parts, and will outweigh any benefits even if each single regulation on its own provides a net benefit. Overlapping or conflicting regulation can occur between different regulatory bodies within the same level of Government, or between different Governments, or between public and private oversight bodies. Such 'regulatory cocktails' often create compliance disasters that regulators leave consumers and businesses to resolve. For example, workers' compensation and OH&S laws differ between States, despite having almost identical objectives. This generates considerable extra compliance costs for national firms, with zero additional benefits for those the laws are designed to protect.

3. **Not listening** – Regulators sometimes, but not always, meet with those they are proposing to regulate. Consultation is an important step in determining if regulation is needed, and where it is, in developing least cost, effective regulation. Too often, however, business finds these processes frustrating as regulators consult, but do not act upon what they hear. For example, many business groups came away from the consultation processes on the *Financial Services Reform Act 2001* wondering whether it had been worth the effort, given how little their concerns resulted in improvements in the Act.
4. **Not looking back** – That regulations have a shelf-life was discussed in the previous Section. The *Access Economics Report* found that, as the economy is not static, there is a high risk of regulations becoming outdated or less cost-effective than alternatives (or deregulation). A large part of the success of the National Competition Policy was its requirement to review the anti-competitive parts of existing legislation, to check they continued to make sense. Despite this success, there are many areas of the law that have not been kept under review and their ongoing applicability tested. An example of this, provided in the *Access Economics Report*, is the restrictive legislation around petrol retailing.

The *Access Economics Report* provides additional examples of regulatory failure to illustrate each of the four mistakes typically made by regulators. Further examples of the poor business regulation currently in place in Australia are set out in Exhibit 6.

Consultation is an important step in determining if regulation is needed, and where it is, in developing least cost, effective regulation.

EXHIBIT 5: GOOD INTENTIONS, POOR OUTCOMES

Regulation does not just impose costs. In some instances, it can have the opposite effect to that intended.

- Prior to financial deregulation in Australia, interest rates were capped to keep the cost of small business borrowings down. The cap, however, meant that banks found small business a more risky and less attractive proposition. As a result, small business had less access to credit, stifling their business opportunities and undermining the intended policy of the regulation.
- The Commonwealth Government prohibits the sale of Australian native animals. A private conservation agency in South Australia managed a successful platypus-breeding program; so successful they ended up with a surplus of 40 platypuses above the sustainable population for the sanctuary. Despite offers in excess of $1 million for a platypus, the agency was prohibited from selling them, leaving the only feasible alternative being to cull them.
- Australian regulators mandated that digital TV in Australia must be of the highest definition (higher than in other countries). As a result of the regulation, only large, expensive TVs could receive digital broadcasts and the costs for the development and transmission of digital content were very high. These additional costs, to suppliers and potential users, meant few aspects of digital TV were commercially feasible and there would be less competition between service providers.
- Confusing regulation can mean that it is all ignored, or makes compliance unnecessarily difficult. NSW, for example, once had in place three different sets of requirements for the distance that earthworks could be carried out from a watercourse: the Department of Conservation and Land Management required a 60 metre gap; the Department of Water Resources required 20 metres; while the Department of Planning suggested 40 metres.

Source: Banks, G., *The good, the bad and the ugly: economic perspectives on regulation in Australia*, October 2003, Productivity Commission.

EXHIBIT 6: A LITANY OF POOR REGULATION

Poor regulation-making processes, and an over-abundance of regulation, lead to poor regulatory outcomes. Poor regulation occurs at all levels of Government and affects all Australians, not just those in business. Some examples include:

Stifling infrastructure investment

Regulation requires that the owners of some infrastructure assets share their investment with their competitors. Poor decisions by the regulators overseeing this regime can lead to perverse outcomes, including serious capacity constraints in Australia's infrastructure. The pipeline delivering Bass Strait gas to Adelaide, for example, has been deliberately built to avoid any spare capacity that the regulator could insist be made available to the pipeline owners' competitors at unacceptably low prices. In another instance, the regulator set the access price of the Dampier to Bunbury gas pipeline so low, it was uneconomic for the owner to expand capacity, resulting in an undersupply of gas for electricity generation and hence blackouts.

Constraining export capacity

Infrastructure capacity is constrained when regulators set charges at levels lower than the market would otherwise determine. For example, Queensland Competition Authority signalled that prices for the Dalrymple Bay Coal Terminal would be set at a level that caused the facility's owner, Prime, not to invest in increased capacity. The port is now unable to cope with increased demand.

Slowing technology uptake

Knowledge is the high-value commodity of the 21st century, so high-level knowledge and information communication infrastructure is vital for Australia's future prosperity. The development of Australia's fibre-optic cable network is being held back because the Australian Competition and Consumer Commission (ACCC) cannot equivocally assure prospective builders that once it has been built, it won't be redistributed by the Government. As Telstra's Head of Regulatory Affairs, Bill Scales, recently pointed out before a Senate committee, Telstra is fearful that if it builds the new infrastructure, the ACCC will force Telstra to share the network with its competitors, making the initial investment uneconomic. Lack of investment means that Australia's Internet access is 5–10 times slower than in some other countries.

CONTINUED >

EXHIBIT 6: A LITANY OF POOR REGULATION continued

Rigid regulation

In New South Wales, builders are required to ensure that all power tools used on a building site are checked for safety by a qualified electrician every three months. This requires expensive checks on 50 or more tools, some of which are used only once a year, and requires 'tools' such as portable radios and the kettle for morning tea be as regularly and rigorously tested as heavy equipment. The costs of these checks are passed on to home buyers.

Perverse outcomes

The *Financial Services Reform Act 2001* aimed to ensure consumers were better informed about the financial products they were thinking of buying. As a result of the Act and the way it was interpreted by regulators and lawyers, companies felt compelled to increase dramatically the size of their product disclosure statements (PDSs) to potential clients. The CEO of the Commonwealth Bank has described how 'the FSR Act means that a simple overdraft for a business that once required 20 pages of documentation now requires 227 pages'. The CEO of Insurance Australia Group reported that one of his company's products required a 110-page PDS. The *Sydney Morning Herald* (26 June 2004) reported that for retail super funds 'the average product disclosure statement for a retail fund can run to 60 or 70 pages'. Contrary to the stated objective of the Act, the result means that consumers are less likely to read the PDS, will be less well informed and will be more reliant on professional advice instead of being able to make decisions for themselves.

Perverse incentives

The Productivity Commission inquiry into the impacts of native vegetation and biodiversity regulations found that a number of regulations put in place to protect biodiversity can actually have negative environmental consequences. State regulations preventing the clearing of regrowth vegetation after a fixed number of years results in more frequent land clearing than would otherwise be the case, leading to greater soil erosion and water quality degradation. Regulations in South Australia, Victoria and New South Wales preventing the clearing of paddock trees have prevented farmers moving from inefficient, wasteful flood irrigation to significantly more water-efficient centre-pivot irrigation. The Commission also received submissions arguing that farmers were not reforesting land with native species for fear that they would then be prevented from making economic use of these trees.

EXHIBIT 6: A LITANY OF POOR REGULATION continued

Anti-competitive regulation

Regulations prohibit 'chain' pharmacies in Australia, reducing the savings from economies of scale and scope that could be passed on by such chains to customers. The regulation was first introduced in the 1930s when UK pharmacist Boots threatened to move into Australia, and has been successfully dampening competition ever since.

Disruptive regulation

The days and times that major retailers, such as David Jones or Myer, can open over Christmas and New Year are determined by each State Government, and each has a different set of rules. To compound the problems of inconsistency, State Governments vary the rules year by year and often only determine the allowed opening hours very late in the year, disrupting the holiday plans of employees and making planning difficult for companies. For example, during November 2004, a number of State Governments decided to change the public holidays over the Christmas–New Year period. Other States, less than a month before Christmas, had not decided when they would allow stores to open or for what hours.

Unwarranted costs

The Victorian Government imposes a Fire Service levy on the mining industry to help fund fire fighting services. The Minerals Council of Australia, Victorian Division, has pointed out that the levy is imposed on underground mining assets even though the fire fighting services in question can only be used for surface fires and do not protect underground assets.

Excessive intrusion

The Child Employment Act 2003 (Victoria) forces business owners, including farmers, to undergo a police check before young relatives, friends and neighbours can help out in the business. In effect, if the grandchildren visit the family farm, the grandparents need a police check before they can let the grandchildren feed the animals or help around the farm, even if they are not paying the children.

EXHIBIT 6: A LITANY OF POOR REGULATION continued

Ridiculous rules

For 10 years, the Observatory at Cowra, NSW, has had a tourism sign advising tourists that they can visit the Observatory to look at the stars and planets. The Observatory is open every night. A committee of the Road Transport Authority and Tourism NSW has undertaken an audit of tourism signs and decreed that the Observatory's sign has to be removed, because the Observatory is open at night, not during the day. In nearby Canowindra, the internationally renowned Age of Fishes fossil museum has been unable to get a tourism sign. In a town of just 1,500 people, the museum is staffed by volunteers, who manage to keep the museum running and open from 10am–4pm, 7 days a week. The museum can't have a tourism sign because it is not open from 9am–5pm. The tourism signs are supposed to promote much needed tourism to boost regional economies, but rigid rules blindly applied are defeating that goal.

Dampening innovation

As part of the Australian Government's legislative review program in 1999, the Productivity Commission found that the legislative regime in broadcasting services imposed significant costs on the community, through:

- creating barriers to entry that reduce the diversity of views and opinions in the 'market for ideas' and lead to higher prices or reduced service quality;
- limiting the attractiveness of digital television, thereby restricting the uptake of this technology; and
- restrictions that result in inferior outcomes to regional areas, for example, constraints on datacasting that prevent it being used as a low-cost method of broadcasting regional sporting events.

Vague regulatory requirements

The vagueness of some regulations makes it very difficult for businesses to comply with the regulatory requirements. For example, State legislation requires aquaculture businesses to maximise and/or provide benefits to the broader community (NSW, WA and SA) or to 'present and future generations' (Victoria and WA). The legislation provides little or no guidance as to what factors should be taken into account in assessing public benefits and costs, how to weight benefits and costs among different community groups or how to weight the interests of future compared with current generations.

EXHIBIT 6: A LITANY OF POOR REGULATION continued

Lack of consistency

A Victorian research institute wanted to import redclaw, a species of freshwater crayfish native to tropical Queensland and the Northern Territory, into Victoria for research purposes. Its application was refused, however, under regulations restricting the movement of noxious species, even though redclaw can be purchased live from Victorian seafood wholesalers.

Strangling industry

Over-regulation can kill industries. New Victorian food safety legislation has hit the aquaculture industry hard. Yabby producers have found the fees and regulatory requirements, including food safety audits, too onerous, with the number of aquaculture licence holders falling from 223 last year to only 100, while the number of yabby growers has been reduced from 60 to just 14, with only three licensed to sell the products for human consumption.

Beautiful one day, over-regulated the next

Under new traffic rules in Queensland that came into effect on 1 January 2005, anyone who leaves a car window partially open could receive a $30 fine. The rules are apparently designed to prevent car theft, but seem impractical in the Northern Queensland heat, particularly for owners of older cars without air conditioning, dog owners who wish to leave their dogs in the car or those driving convertibles. It is also not clear what motorists with children are supposed to do when stopping at self-service petrol stations.

SECTION

5

Steps to Better Business Regulation

The quantity and quality of business regulation at the Commonwealth, State and Local Government levels clearly needs to be improved. This is no easy task. While no one knows the total number of laws, regulations and rules in Australia, let alone how many of these affect business, we do know that the number is large. We also know that the amount of business regulation is growing rapidly.

Most previous attempts to reform regulation and cut 'red tape' have focused on removing or improving existing regulations. These reviews have their benefits, particularly in stripping away the undergrowth of redundant regulation.[6] But even as these reviews take place, new regulations are being developed and imposed. The gains from such 'red tape' reviews are therefore often only temporary (see Exhibit 7).

EXHIBIT 7: WE'VE BEEN HERE BEFORE ...

In September 1984, then Prime Minister Hawke, addressing the Business Council of Australia, said:

> 'I am convinced that after eighty-four years of Federation, we have accumulated an excessive and often irrelevant and obstructive body of laws and regulations. We will examine critically the whole range of business regulation, most importantly with a view to assessing its contribution to long-term growth performance. We will maintain regulation which upon careful analysis, clearly promotes economic efficiency, or which is clearly an effective means of achieving more equitable income distribution. And we will abandon regulation which fails these tests.'

The BCA welcomed this sentiment and commitment then and would welcome a similar commitment from all Governments today. However, it should be noted that, despite the then Prime Minister's assurances, nearly twice as much Commonwealth legislation has been passed since he gave this commitment as had been passed in the eighty four years from Federation.

The reason such commitments have failed to deliver, and 'red tape' reviews, while important, are only part of the answer, is that these approaches alone do not address the underlying structural and cultural problems that drive Governments to introduce more and more regulation. This BCA *Action Plan* therefore tackles these structural and cultural issues first, before reviewing the existing stock of regulation.

A better approach is to first fix the system that is generating unnecessary and costly regulation, and to then turn attention to improving the existing stock of regulation. The BCA, therefore, proposes a step-by-step response to turning back the tide of regulation (see Exhibit 8). The first step is to improve the processes that produce business regulation to ensure it is only introduced where its benefits clearly outweigh its costs.

EXHIBIT 8: STEPS TO BETTER BUSINESS REGULATION

Step One: **Improve future regulation**

Improve the process of regulation to ensure regulation is introduced only where it is necessary and in the most cost-effective way.

Step Two: **Improve existing regulation**

Review the stock of existing business regulation, testing each piece of regulation against criteria such as: is the regulation still needed? How will the market respond if it is removed? Are there more cost-effective ways of achieving the policy outcome?

Step Three: **Rationalise Commonwealth–State regulation**

Where an area of regulation is a shared responsibility between jurisdictions, particularly between the Commonwealth and the States, there should be a move towards a single, consistent national regime. We have achieved this already with corporations law and with competition law – it is now time to target other major areas of regulation such as workplace relations law, occupational health and safety law, product standards, trade and professional licensing, personal securities and environmental laws.

The initial focus of this *Action Plan* is on the Commonwealth Government. This does not suggest that the Commonwealth level is where the greatest need for improvement lies. Overall, the Commonwealth is probably the leader in terms of improving its regulation-making processes and hence its regulation. For this reason, it is a simpler matter to bring the Commonwealth system into line with world's best practice. The revised Commonwealth system then provides a model for State Governments to adopt. The Business Council will be actively encouraging this adoption. State Governments also have a responsibility for tackling the plethora of poor, redundant and overlapping regulation at the level of Local Government. The Commonwealth has already lent its support in this area through its election commitment to establish a Regulation Reduction Incentive Fund worth $50 million to provide Local Government authorities with incentives to reduce the regulatory burden on home-based businesses. A similar commitment to reduce the regulatory burden on all businesses is now needed from State Governments.

SECTION

6

Improve Future Business Regulation

Step One

The negative consequences of poor regulation are not just felt in Australia. Most OECD countries are examining the impact regulation has on their business and economic competitiveness. In particular, they are actively implementing new approaches to developing business regulation that allow Government policy objectives to be achieved in the most effective and efficient manner possible. This highlights the need for Australia to examine its own business regulation-making system. If our competitors are capturing productivity gains through reforming business regulation, making their businesses and economies more competitive, Australia must do the same.

Australia can also learn from the experiments and experiences of other countries. The BCA has therefore reviewed in detail the approaches to better business regulation taken in other countries. The results of this review appear in the *Options Paper*, (see Appendix 1).

The *Options Paper* draws on overseas experiences to identify good practice regulatory standards against which the current Australian regulatory system can be measured. Based on overseas experience and the assessment of the current Australian process, the *Options Paper* identifies the priority areas for reform and the options available to improve the quality and reduce the quantity of business regulation in Australia.

Overseas experience, and the analytical work of the OECD[7] and the Productivity Commission, suggests two basic requirements for reforming business regulation-making processes:

- Strengthen the institutional framework for making business regulation. The institutional framework describes the organisations or bodies, both within and outside of Government, that oversee and review the development of business regulation.
- Improve the quality of new regulations, through ensuring proper processes for determining when regulation is required, the costs and benefits of regulating and for gaining input from those having to implement regulatory requirements.

6.1 STRENGTHENING THE INSTITUTIONAL FRAMEWORK

OECD research shows that the bodies overseeing the development of new regulation are most effective when they are:

Independent – free from undue influence from either regulators or private interests.

Endorsed – work under a clear regulatory policy that has been endorsed at the highest political level.

Horizontal – have the power to cut across Government.

Expert – staffed with experts who have the capacity and resources to make independent judgements.

Proactive – able to take the initiative in promoting regulatory reform.

Networked – have strong links to political authority.

Measuring the Commonwealth's regulatory system against these criteria shows that, while each element is present, there is considerable room for improvement. A detailed assessment of the Commonwealth system against these criteria is provided in the *Options Paper*.

Based on an analysis of alternative institutional frameworks in place overseas and in some Australian States, the BCA argues the Commonwealth system should be restructured along the following lines.

A. Ministerial Task Force

There needs to be a powerful 'gatekeeper' to ensure proposals to impose significant new regulation upon business are only considered by Government if the benefits of the proposed regulation clearly outweigh the costs. The 'gatekeeper' also needs to ensure that proper processes have been followed, including a detailed cost-benefit analysis and consultation with the businesses and other interests likely to be affected by the proposed regulations.

Without a 'gatekeeper', there is no guarantee that bureaucratic or Ministerial expediency will not work to undermine the proper processes for developing better business regulation. Experience has shown that political promises to improve regulation are not enough (see Exhibit 7). A Government that is committed to better business regulation will put in place the checks and balances necessary to ensure that outcome, including establishing bodies with the commitment and power to ensure reform takes place.

The BCA therefore recommends that a Ministerial Task Force, similar to that in the UK and the Netherlands, be established, consisting of 3–4 Cabinet ministers, chaired by the Prime Minister and meeting to:

- review the costs and benefits of proposals for major business regulation, including the adequacy of the regulatory impact statement and consultation processes, before proposals are considered by Cabinet, and
- develop and oversee the Government's regulatory reform agenda, including assessing reports from Ministers on their efforts to reduce and improve regulation.

B. Regulation Advisory Council

Reform of business regulation should not take place without direct input from the businesses and others affected, including consumers. Without business input, Government cannot fully appreciate the costs and impacts of regulation, or the priority areas for reform.

At present, business involvement in the development of regulation tends to be ad hoc. While there are some advisory bodies, such as the Business Regulation Advisory Group (BRAG) and the Financial Services Advisory Council (FSAC), these groups have only a limited role and do not advise Government on broader issues of regulatory reform. Even where business is consulted on proposed new regulations, it is often after the Government has already decided to regulate and business input has limited impact on the eventual outcome.

The BCA therefore recommends that a Business Regulation Advisory Council (Advisory Council) be established, consisting of representatives from across business and other affected groups, such as consumers, to:

- advise the Government on the priorities and direction of regulation reform, including identifying across all levels of Government where the biggest problems lie;
- coordinate consultation on major proposals for business regulation;
- coordinate reviews of existing regulation and whether specific regulations need to be removed or improved, and consequently make recommendations to Government;
- report on the adequacy of the existing law to deal with topical issues;
- report on the stock or quantity of regulation in place (particularly once the *Legislative Instruments Act 2003* comes fully into effect in 2007), and
- perform the above functions with the support of a full-time executive chairman or officer, a dedicated secretariat, the ability to establish ad hoc subcommittees to address specific issues and the ability to second individuals from the private sector and academia.

The Government should also undertake an audit and review of all existing advisory bodies to ensure they remain relevant and effective. In particular, a number of these groups may no longer be needed once the Business Regulation Advisory Council has been established.

C. Regulatory Impact Assessment Unit

Better business regulation needs a powerful ally within Government. At present, the Office of Regulation Review has responsibility for overseeing the Commonwealth processes designed to assess the costs and benefits of proposed regulation. The Office of Regulation Review, however, has limited tools to ensure proper regulatory impact assessment takes place and that it actually influences regulatory outcomes.

The BCA therefore recommends that the Office of Regulation Review be given an enhanced role in:

- challenging the need for new business regulation;
- overseeing and advising on the development of regulatory impact statements; and
- providing training on assessing the impacts of regulation.

In part, the role of the Office of Regulation Review can be strengthened through it reporting directly to both the Ministerial Task Force and the Advisory Council on the performance of the regulatory impact assessment system and through providing the secretariat support for the Advisory Council.

D. Departmental Regulation Units

In addition, to improve the capabilities of policy departments in developing better regulation and assessing its costs and benefits, the Office of Regulation Review should be supported by departmental regulation units established in each department with a significant business regulation role. Departmental regulation units would have responsibility for the development of regulations that affect business. They would consist of a small number of officials, answering to a senior executive in the department with responsibility for championing regulatory reform and the removal of costly, inefficient or redundant regulation. They would support the development of regulatory impact statements by the department, and act as a liaison point between the department and the Office of Regulation Review.

EXHIBIT 9: DO WE NEED MORE 'GOVERNMENT' TO GET LESS REGULATION?

The BCA proposes establishing a number of new bodies to oversee the processes for making business regulation. It is legitimate to ask whether, when we are concerned with too much regulation, we should be promoting the establishment of yet more Government or quasi-Government bodies.

The reality is that business regulation is here to stay. Complex economies and societies require regulation, and while the recommendations made by the BCA, if implemented by all levels of Government, should reduce and improve that regulation, more regulation will still be made. Given its volume and complexity, it is imperative that there are proper checks and balances in place to ensure regulation is only imposed where its benefits outweigh its costs. The reason we are seeing an explosion of poor regulation is because those checks and balances are not in place.

Putting the above structures in place will ensure there are proper checks and balances on the development of new business regulation. These bodies will not be able to stop the Government making political decisions to impose regulation. They will, however, increase the accountability of the regulation-making process and should ensure that the benefits and costs of regulation have been properly assessed, in consultation with those bearing the costs, before regulation is imposed.

As we have seen (Exhibit 7), Governments merely committing to improving regulation does not turn back the tide. Governments truly committed to reducing business regulation, and improving the quality of the regulation that is imposed, will ensure proper checks and balances are put in place.

Finally, to be effective the Business Regulation Advisory Council and the Office of Regulation Review need to be adequately resourced. While this presents an initial additional cost to Government, this cost should be recovered many times over through reducing and improving business regulation and hence the cost of its administration. If these cost savings are not realised, then the Business Regulation Advisory Council and the Office of Regulation Review are clearly not achieving their objectives.

6.2 | IMPROVING THE QUALITY OF NEW REGULATIONS

Assessing the benefits and costs of new regulation, including the costs to business, is increasingly recognised as a necessary safeguard against unnecessary, costly and inefficient regulation. Since 1997, the Commonwealth Government has required the preparation of a regulatory impact statement for all reviews of existing regulation, proposed new or amended regulation, quasi-regulation and proposed treaties involving regulation, which will directly or indirectly affect business or restrict competition (a range of exceptions apply).

Despite this requirement, regulatory impact statements have been less than successful in stemming the flow of new, costly business regulation. Only a handful of new regulations are subject to any cost-benefit analysis, and even where such analysis occurs, it is often too late in the process to influence the outcome and is based on very limited information about the actual costs to business (see Exhibit 10). The Commonwealth has made a number of attempts since 1994 to improve the processes for making legislation, however, these have been blocked by the Senate.[8]

The BCA therefore argues that improvements are needed to the Commonwealth regulatory impact statement process to ensure that Government, and the wider community, are fully informed of the expected benefits and costs of regulation before a decision to regulate is made. As a minimum, the key improvements needed include:

- legislating the requirement to produce a regulatory impact statement for all regulatory proposals likely to have a significant impact on business;
- requiring the Minister proposing new business regulation to personally certify that the benefits of the regulation will outweigh the costs;
- introducing a two-stage impact assessment process, with all regulations likely to affect business subject to a preliminary assessment, and all regulations likely to have significant impacts on business subject to a full assessment;
- requiring the release of draft regulatory impact statements for public comment and allowing sufficient time for consultation to make that consultation meaningful; and
- developing a standardised, sophisticated methodology for identifying and measuring the likely costs to business of proposed regulations.

EXHIBIT 10: EFFECTIVE REGULATORY IMPACT STATEMENTS?

In 2001, the Commonwealth Government introduced the Financial Services Reform Bill to rationalise and simplify the regulation of the financial services industries. The Bill was a major piece of legislation with wide-ranging effects on the industries involved. It has been estimated that the new regulations, which run to 600 pages, affected between 7,000 and 9,000 businesses,[9] with initial implementation costs for business in the order of $200 million.[10]

A regulatory impact statement (RIS) was prepared for the Bill. The financial impact statement component of the RIS amounted to five paragraphs. It stated that the 'FSR Bill will reduce compliance costs for industry', noting that 'industry is likely to incur some costs in the initial stages', although these costs will be 'limited by the fact that the new disclosure regime is broadly in line with existing requirements'.[11] That was the extent of the cost analysis done for this major, and as it proved, costly, piece of legislation.

In 2003, the Commonwealth Government introduced the Postal Services Legislation Amendment Bill 2003. The regulatory impact statement claimed 'there is no practical means of collecting information about the number of document exchange and aggregation services operating in Australia', although these businesses were to be affected by the new regulation. During debate on the Bill, former Federal Greens MP Michael Organ pointed out that 'I can only assume that the Internet was down that day, because a simple search of the Yellow Pages online produces a list of eight companies across the nation that do that work.'[12]

An inadequate RIS, and the poor regulation that can result, are direct consequences of not having robust, transparent processes in place, not consulting business adequately and not undertaking a robust cost-benefit analysis.

SECTION

7

Improve Existing Regulation

Step Two

Once reforms have been made to when and how new regulation is imposed, existing business regulation needs to be thoroughly reviewed. In particular, all business regulation, whether at the State, Local, or Commonwealth level, needs to be tested against criteria such as:

- Is the regulation still needed?
- How will the market respond if the regulation is removed?
- Are there more cost-effective ways of achieving the desired policy outcome?

When existing regulation is reviewed, it needs to be reviewed from the perspective of those affected by the regulation, not just from the Government's policy perspective. Priorities also need to be set, particularly targeting those regulations that restrict competition and business innovation or where there is a clear mismatch between the benefits of the regulation and the costs it imposes.

The BCA therefore recommends that one of the first tasks for the proposed Business Regulation Advisory Council should be to identify priority areas where regulation can be removed or significantly improved. That examination should look at Local, State and Commonwealth regulation, and the interface between different jurisdictions, and identify:

- where the major regulatory burden for business arises, both generally in terms of whether it is at the Local, State or Commonwealth levels, and specifically where within those jurisdictions the problems occur; and
- what the priority areas should be for reform in terms of both the biggest improvements for business and the best improvements for the economy as a whole.

SECTION 8

Rationalise Commonwealth–State Regulation

Step Three

One of the greatest frustrations for business is dealing with multiple layers of regulation. Most businesses have to deal with regulations imposed by Local, State and Commonwealth Governments. There is typically little coordination between these levels of Government, resulting in unnecessary compliance costs for business.

There are also many areas where responsibility for regulation is shared between a number of different jurisdictions. This often results in different laws in different jurisdictions, despite each jurisdiction having the same policy objectives. The increase in compliance costs, particularly for national firms, can be considerable, even though there is no additional benefit from having a multitude of different regulations (see Exhibit 11). A classic example of this problem occurs in occupational health and safety regulation, where each State has a different regime to achieve the same outcome.

Australia cannot continue to carry the burden of different regulatory regimes, each trying to achieve the same outcome.

The BCA therefore recommends that Australian Governments adopt the principle that, where an area of regulation is a shared responsibility between jurisdictions, there should be a move towards a single, consistent national regime. This is particularly the case where responsibility is shared between the Commonwealth and the States or between the different States. This does not mean that the Commonwealth should necessarily take over responsibility for all regulation. There is a range of alternative models for ensuring shared responsibility, but a single regulatory regime. The States in particular have a responsibility to harmonise their regulatory regimes in areas that are clearly State responsibilities.

Australia has already achieved this principle with corporations law and with competition law. It is now time to target other major areas of regulation, including workplace relations law, occupational health and safety law, product standards, trade and professional licensing, securities and environmental laws.

Australia cannot continue to carry the burden of different regulatory regimes, each trying to achieve the same outcome.

EXHIBIT 11: EXCESSIVE COSTS OF OVER-REGULATION

The complexity arising from multi-jurisdictional legislation across States and at a Commonwealth level imposes large compliance and administrative cost burdens on companies.

The Productivity Commission has highlighted some estimates of the direct costs of multiple workers' compensation and OH&S Frameworks around Australia:

- **Optus** estimates that, if it received a single national self-insurance licence, it would expect savings of up to $2 million per annum of its $6 million annual workers' compensation costs. It estimated that the cost of complying with multiple workers' compensation and OH&S arrangements adds about 5 to 10 per cent to the cost of workers' compensation premiums.
- **CSR** estimates the cost of maintaining and renewing five self-insurance licences at over $700,000 per annum, compared to $200,000 for a single licence.
- **Insurance Australia Group** estimates that the existence of multiple schemes added $10.1 million to the cost of setting up a single national IT platform. In total, it estimates that having to comply with multiple jurisdictions adds about $1.7 million to IT costs annually. Further, it estimates that a national scheme could offer overall operating cost savings to the group of $1.2 million per annum and reduce actuarial costs by $400,000 per annum.

CONTINUED >

EXHIBIT 11: EXCESSIVE COSTS OF OVER-REGULATION continued

- **BHP Billiton** estimated that it costs in the vicinity of $50,000 to purchase a system to manage and supply information for each State and Territory OH&S regime.
- **Skilled Engineering** estimates that the annual cost saving from operating under a single set of national OH&S and workers' compensation rules would be in excess of $2.5 million, or some 15 per cent of the company's annual costs of OH&S and workers' compensation.

A survey by the **Building Products Innovation Council** and the **Housing Industry Association** of building product manufacturing companies, has estimated the cost impact of complying with different State and Territory building laws to be between 1 and 5 per cent of company turnover. Even at a conservative 2 per cent cost impact, this equates to some $600 million annually on building product manufactures alone.

Source: Productivity Commission, *National Workers' Compensation and Occupational Health and Safety Frameworks*, March 2004; Productivity Commission, *Reform of Building Regulation*, November 2004.

SECTION

9 Conclusion

Regulation is vital to the running of complex economies and societies and much regulation has laudable policy objectives. But even where regulation has been put in place for apparently sound reasons, there is no guarantee that it is good regulation. Nor should we assume that regulation is the best way to achieve our goals, nor the best response to every problem or potential problem we see. Regulation is in fact a high-cost option. Every regulation imposes a cost: on the Government administering it; on those regulated; and on the economy as a whole. We must be certain, therefore, that whenever regulation is imposed, its benefits clearly outweigh its costs.

The BCA's research shows that the cost imposed by regulation is a serious burden for business and undermines our competitiveness. If Australia is to fund its future prosperity through continued economic growth, major reforms are needed to business regulation. Our competitors are already engaged in this process and we will be left behind unless we match and exceed their efforts.

This BCA *Action Plan* makes business regulation reform manageable but delivers benefits quickly. Step One must be to fix the current system for creating and imposing business regulation, to prevent the regulatory burden from growing further. Step Two must then address the existing stock of regulation, weeding out redundant, inefficient and inconsistent regulation. Step Three must then seriously tackle a long-term problem in Australia – the overlapping and inconsistent regulation of different layers of Government. The BCA will actively pursue these reforms with Government.

Without these reforms, poor business regulation will continue to add a significant deadweight cost to the economy, sapping the strength of Australian businesses and undermining our competitiveness. To remain competitive, Australia must remove this unnecessary burden.

Without these reforms, poor business regulation will continue to add a significant deadweight cost to the economy, sapping the strength of Australian businesses and undermining our competitiveness. To remain competitive, Australia must remove this unnecessary burden.

Notes

1 PricewaterhouseCoopers, *Bold Ambitions, Careful Choices*. 8th Annual Global CEO Survey.

2 Centre for the Study of Financial Innovation (2005), *Banana Skins 2005*, London.

3 OECD Special Group on Regulatory Policy, *2005 Policy Recommendations for Regulatory Quality*, March 2005 (draft)

4 Examples in Commonwealth statutes include s. 8Y, *Taxation Administration Act 1953*; s. 495, *Environment Protection and Biodiversity Conservation Act 1999*; s. 188, *Corporations Act*; s. 40B, *Hazardous Waste (Regulation of Exports and Imports) Act 1989*; s. 230F, *Life Insurance Act 1995*; Division 9 of Part VI, *Income Tax Assessment Act 1936*; and s. 11CG, *Banking Act 1959*. Similar provisions have recently been proposed for the *Trade Practices Act 1974* (although these have been rejected by the current Commonwealth Government) and in the Victorian Crimes (Workplace Deaths and Serious Injuries) Bill 2001 (rejected in the Legislative Council).

5 For a list of these reforms, see Business Council of Australia, *Action Plan for Future Prosperity and BCA Budget Submission 2005–06*, p. 10.

6 For example, in its first term, the current Federal Government established a Small Business Deregulation Task Force (the 'Bell Task Force') to report on ways to drastically reduce the paperwork and compliance burden faced by small business.

7 The requirements having been highlighted in the work of the OECD, see for example, presentation by C. Cordova- Novion*, Simple, Effective, Transparent Regulation: Best Practices in OECD countries*.

8 Banks, G., *Reducing the business costs of regulation*, Productivity Commission, March 2003.

9 National Tax & Accountants' Association information sheet on *Financial Services Reform Act 2001*, citing ASIC figures.

10 See, for example, 'Compliance Crunch Hits Boardrooms', *Australian Financial Review*, 7 September 2004, p. 1.

11 Explanatory Memorandum for the *Financial Services Reform Act 2001.*

12 Member for Cunningham, House of Representatives, 12 February 2004, *Hansard* pp. 246–78.

Appendix 1

OPTIONS FOR IMPROVING

Business Regulation

Contents

Glossary

ACCC	Australian Competition and Consumer Commission (Commonwealth)
ALRC	Australian Law Reform Commission (Commonwealth)
APRA	Australian Prudential Regulation Authority (Commonwealth)
ASIC	Australian Securities and Investments Commission (Commonwealth)
BRAG	Business Regulation Advisory Group (Commonwealth)
CAMAC	Corporations and Markets Advisory Committee (Commonwealth)
COAG	Council of Australian Governments
DRU	Departmental regulation unit
FSAC	Financial Services Advisory Council (Commonwealth)
NCC	National Competition Council (Commonwealth)
OECD	Organisation for Economic Co-operation and Development
OIRA	Office of Information and Regulatory Affairs (US)
ORR	Office of Regulation Review (Commonwealth)
RIA	Regulatory impact assessment
RIS	Regulatory impact statement

Executive Summary

Business regulation, particularly the amount and quality of that regulation, has a significant impact on the competitiveness of Australian businesses and therefore on the economy as a whole. Poorly conceived, inefficient and redundant regulation can add unnecessarily to the costs of running a business, reduce productivity, stifle innovation and hamper business growth. These negative impacts on business flow through to the whole economy, dampening job growth and reducing Australia's ability to be economically competitive. The companion report, *Benefits & Costs of Regulation* by Access Economics Pty Limited for the Business Council of Australia, (the *Access Economics Report*, Appendix 2) spells these dangers out in more detail.

The negative consequences of poor regulation are not just felt in Australia. Most OECD countries are examining the impact regulation has on their business and economic competitiveness and are developing and implementing new approaches to business regulation. They are actively looking for new ways to achieve Government policy objectives in the most effective and efficient manner possible.

This highlights the need for Australia to examine its business regulation system. If our competitors are capturing productivity gains through reforming business regulation, making their businesses and economies more competitive, Australia must do the same to remain internationally competitive.

Australia can also learn from the experiments and experiences of other countries.

The purpose of this *Options Paper* is threefold. First, it examines the lessons that can be learned from overseas experience in reforming the development of business regulation. Second, it uses this experience to identify best practice regulatory standards, and measures the current Australian regulatory system against these standards. Finally, based on overseas experience and the assessment of the current Australian process, it identifies areas in need of reform and the options available to improve the quality and reduce the quantity of business regulation in Australia. The conclusions of this *Options Paper* support the BCA's *Business Regulation Action Plan for Future Prosperity*, which sets out those reforms the BCA believes need to be made to the Commonwealth regulatory system.

The first step to better business regulation is to improve the way in which business regulation is made. Overseas experience and the analytical work of the OECD[1] and the Productivity Commission show there are three key requirements for reforming business regulation-making processes.

Requirement One

Strengthen the institutional framework for making business regulation. The institutional framework describes the organisations or bodies, both within and outside Government, that oversee and review the development of business regulation (see Section 3 of this *Options Paper*).

Requirement Two

Improve the quality of new regulations, through ensuring proper processes for determining when regulation is required and the costs and benefits of regulating, and gaining input from those having to implement regulatory requirements (see Section 4).

Requirement Three

Improve the quality of existing regulations, through reviewing the existing stock of regulations against criteria aimed at removing redundant, inefficient and overlapping regulation (see Section 5).

If our competitors are capturing productivity gains through reforming business regulation, making their businesses and economies more competitive, Australia must do the same to remain internationally competitive.

STRENGTHENING THE INSTITUTIONAL FRAMEWORK

OECD research shows that the bodies overseeing the development of new regulation are most effective when they are:

Independent – free from undue influence from either regulators or private interests.

Endorsed – work under a clear regulatory policy that has been endorsed at the highest political level.

Horizontal – have the power to cut across Government.

Expert – staffed with experts who have the capacity and resources to make independent judgements.

Proactive – able to take the initiative in promoting regulatory reform.

Networked – have strong links to political authority.

Assessing the Commonwealth's regulatory system against these criteria shows that, while each element is present, there is considerable room for improvement. Based on an assessment of alternative institutional frameworks in place overseas and in some Australian States, the BCA considers that the Commonwealth system should be restructured according to the following.

A. Ministerial Task Force

There needs to be a powerful 'gatekeeper' to ensure proposals to impose significant new regulation upon business are only considered by Government if the benefits of the proposed regulation clearly outweigh the costs. The 'gatekeeper' also needs to ensure that proper processes have been followed, including a detailed cost-benefit analysis and consultation with the businesses and other interests likely to be affected by the proposed regulations.

The BCA therefore recommends that a Ministerial Task Force, similar to those in the UK and the Netherlands, be established, consisting of 3–4 Cabinet ministers, ideally chaired by the Prime Minister and meeting to:

- review the costs and benefits of proposals for major business regulation, including the adequacy of the regulatory impact statement and consultation processes, before proposals are considered by Cabinet; and
- develop and oversee the Government's regulatory reform agenda, including assessing reports from Ministers on their efforts to reduce and improve regulation.

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Reform of business regulation should not take place without direct input from the businesses and others affected. Without business input, Government cannot fully appreciate the costs and impacts of regulation, or the priority areas for reform.

At present, business involvement in the development of regulation tends to be ad hoc. While there are some advisory bodies, such as the Business Regulation Advisory Group (BRAG) and the Financial Services Advisory Council (FSAC), these groups have only a limited role and do not advise Government on broader issues of regulatory reform. Even where business is consulted on proposed new regulations, it is often after the Government has already decided to regulate, and business input has limited impact on the eventual outcome.

The BCA therefore recommends that a Business Regulation Advisory Council (Advisory Council) be established, consisting of representatives from across business and other affected groups, such as consumers, to:

- advise Government on the priorities and direction of regulatory reform, including identifying across all levels of Government where the biggest problems lie;
- coordinate consultation on major proposals for business regulation;
- coordinate reviews of existing regulation and determine whether specific regulations need to be removed or improved, and consequently make recommendations to Government;
- report on the adequacy of the existing law to deal with topical issues;
- report on the stock or quantity of regulation in place (particularly once the *Legislative Instruments Act 2003* comes fully into effect in 2007), and
- perform the above functions with the support of a full-time executive chairman or officer, a dedicated secretariat, the ability to establish ad hoc subcommittees to address specific issues, and the ability to second individuals from the private sector and academia.

C. Regulatory Impact Assessment Unit

Better business regulation needs a powerful ally within Government. At present, the Office of Regulation Review has responsibility for overseeing the Commonwealth processes designed to assess the costs and benefits of proposed regulation. The Office of Regulation Review, however, has limited tools to ensure proper regulatory impact assessment takes place and that it actually influences regulatory outcomes.

The BCA therefore recommends that the Office of Regulation Review be given an enhanced role in:

- challenging the need for new business regulation;
- overseeing and advising on the development of regulatory impact statements; and
- providing training on assessing the impacts of regulation.

In part, the role of the Office of Regulation Review could be strengthened through it reporting directly to both the Ministerial Task Force and the Business Regulation Advisory Council on the performance of the regulatory impact assessment system and through providing the secretariat support for the Business Regulation Advisory Council.

D. Departmental regulation units

In addition to improving the capabilities of policy departments in developing better regulation and assessing the costs and benefits of regulation, the Office of Regulation Review should be supported by departmental regulation units established in each department with a significant business regulation role. Departmental regulation units would have responsibility for the development of regulations that affect business. They would consist of a small number of officials, answering to a senior executive in the department with responsibility for championing regulatory reform and the removal of costly, inefficient or redundant regulation. They would support the development of regulatory impact statements by the department, and act as a liaison point between the department and the Office of Regulation Review.

IMPROVING THE QUALITY OF NEW REGULATIONS

Assessing the benefits and costs of new regulation, including the costs to business, is increasingly recognised as a necessary safeguard against unnecessary, costly and inefficient regulation. Since 1997, the Commonwealth Government has required the preparation of a regulatory impact statement for all reviews of existing regulation, proposed new or amended regulation, quasi-regulation and proposed treaties involving regulation, which will directly or indirectly affect business or restrict competition[2] (a range of exceptions apply).

Despite this requirement, regulatory impact statements have been less than successful in stemming the flow of new, costly business regulation. Only a handful of new regulations are subject to any cost-benefit analysis, and even where such analysis occurs, it is often too late in the process to influence the outcome and is based on very limited information about the quantitative costs to business.

Improvements are needed to the Commonwealth regulatory impact statement process to ensure that Government, and the wider community, are fully informed of the expected costs and benefits of regulation before a decision to regulate is made.

The key improvements needed include:

- Legislating the requirement to produce a regulatory impact statement for all regulatory proposals likely to have a significant impact on business.
- Requiring the Minister proposing new business regulation to personally certify that the benefits of the regulation will outweigh the costs.
- Introducing a two-stage impact assessment process, with all regulations likely to affect business subject to a preliminary assessment, and all regulations likely to have significant impacts on business subject to a full assessment.
- Requiring the release of draft regulatory impact statements for public comment and allowing sufficient time for consultation to make that consultation meaningful.
- Developing a standardised, sophisticated methodology for identifying and measuring the likely costs to business of proposed regulations.

IMPROVING THE QUALITY OF EXISTING REGULATIONS

The level of regulation at State and Commonwealth levels has grown considerably over the past few decades. While much of this legislation may have been put in place for laudable policy reasons, badly drafted, inefficient, duplicated and overlapping legislation still imposes additional costs on business. It is not enough to just improve the structures and process surrounding the development of future business regulation. The cost burden of existing regulation also needs to be addressed.

Experience has shown that 'red tape' reviews have limited impact unless more fundamental structural reforms are made to the regulation-making and oversight systems. For this reason, the BCA has proposed a staged approach to regulatory reform, with the first stage focusing on structural reforms to how new regulation is made. Once that has been achieved, the new structures and improved processes can be used to review the stock of existing regulation, and to improve or weed out redundant, inefficient and overlapping regulation.

While much legislation may have been put in place for laudable policy reasons, it can still impose additional costs on business.

1 Introduction

There is growing concern in the Australian business community over the levels and quality of business regulation. The *Access Economics Report* (Appendix 2) points to the dangers of poor regulation, not just for business performance, but for the performance of the whole economy.

Drawing on overseas experience, this *Options Paper* examines how regulatory reform can be achieved through improving:

- the institutions governing the development and implementation of business regulation; and
- the processes for making regulation and managing regulatory reform.

This will ensure that Australia's business regulation regime contributes to, and does not undermine, Australia's continuing competitiveness in the global market.

This *Options Paper* examines a range of options developed and implemented overseas for reforming business regulation.[3] The *Action Plan* sets out those options that the BCA believes must be implemented in Australia to significantly improve business regulation.

1.1 THE THREE STRUCTURAL REQUIREMENTS FOR BETTER REGULATION

This *Options Paper* sets out and analyses the three main requirements for better business regulation,[4] and the main outcomes that need to be achieved from those requirements.

Requirement One
Strengthen the institutional framework for making business regulation. The institutional framework describes the entities, both within and outside of Government, that oversee and review the development of business regulation (see Section 3).

Requirement Two
Improve the quality of new regulations, by proper processes for determining when regulation is required, the costs and benefits of regulating and gaining input from those having to implement regulatory requirements (see Section 4).

Requirement Three
Improve the quality of existing regulations, through reviewing the existing stock of regulations against criteria aimed at removing redundant, inefficient and overlapping regulation (see Section 5).

High-quality regulations are essential if Governments are to achieve their desired policy objectives as cost-effectively as possible. As all regulation carries costs, both for the affected businesses and for the economy as a whole, Governments must have a justifiable policy stance when they decide to regulate. The process by which Governments decide when and how to regulate must be transparent and accountable, and must enable the public to fully understand the reasons for regulation. The three requirements above provide a framework for reforming regulation-making processes to achieve transparency and accountability.

1.2 | WHAT ARE REGULATIONS?

Regulations are the instruments by which Governments impose requirements on citizens, enterprises and Government itself, including laws, formal and informal orders, subordinate rules and rules issued by bodies that have been delegated regulatory powers.[5] Ideally, these regulations are intended to influence behaviour in order to achieve an improvement in social wellbeing above the position that would have been achieved in an unregulated market.

Regulations must be well designed, effectively and efficiently implemented and properly enforced to achieve the greatest benefits for society without creating unnecessary burdens on business or the community.

1.3 | REGULATORY TRADE-OFF

In liberal democracies such as Australia, regulations are generally imposed by Governments where markets are seen to have failed to achieve efficient or socially acceptable outcomes. The imposition of regulation carries its own costs, however, both to the regulated and the regulator, and consequently to the whole economy. Therefore, regulations that achieve net benefits are those where the benefits outweigh these costs. Regulations must be well designed, effectively and efficiently implemented and properly enforced to achieve the greatest benefits for society without creating unnecessary burdens on business or the community.

OECD research has shown that regulations can impose a significant and unnecessary cost burden on an economy if they are inefficient and not well designed.

- They can impede innovation or create unnecessary barriers to trade, investment and economic efficiency (reducing competitiveness in a global economy).
- There can be duplication between regulatory authorities and different layers of Government.
- They can become outdated or poorly designed if they are not flexible and responsive to changing circumstances.

Regulatory reform aims to improve the quality of regulation:

- to ensure that regulations that are created or exist are efficient, cost-effective, transparent and high-quality; and
- to ensure that regulatory burdens are reduced in a way that increases a country's competitive position.

1.4 WHY IS REGULATORY REFORM IN AUSTRALIA IMPORTANT?

Australian Governments have implemented a number of regulatory policies, tools and institutional arrangements to improve the level and quality of regulation. These processes and mechanisms for making regulation and managing reform have had a positive impact on Australia's regulatory environment. However, there are a number of areas where inefficiencies, duplication and lack of simplicity still exist in Australia's regulatory management system.

Regulatory improvement is very important to the business community. Regulatory reform enables improvement in the efficiency of business enterprises and hence of national economies and their ability to adapt to change and remain competitive. Reform that reduces business burdens and increases transparency of regulatory decision-making encourages entrepreneurship, market entry and economic growth and the ability for an economy to compete. In an increasingly global economic environment, Australia must be able to compete with other nations in finding markets for its goods and services and in attracting investment and labour. The mobility of capital, people and ideas has increased, along with economic changes and innovation.

A number of Australia's competitors are undertaking regulatory reform initiatives that go beyond those currently implemented in Australia. These reforms will enable those countries to compete more effectively.

Ongoing regulatory reform is thus vital if Australia is to maintain and improve its standing in terms of global competitiveness. While overall, Australia's business regulatory environment is in reasonable shape (by international comparisons), we cannot afford to be complacent as our competitors seek to improve their competitiveness through better business regulation.

There are already signs that we have done so. In recent years, business has faced wave after wave of new business regulation, each increasing the costs of doing business in Australia. At the Commonwealth level, for example, we have seen major new pieces of legislation come in, such as the *Privacy Act*, the *Financial Services Reform Act*, the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act* (also known as CLERP 9) and the yet to be released Anti-Money Laundering Bill. While each of these pieces of regulation may have positive policy objectives, they each add to the costs of doing business, sometimes significantly. In addition, they do not always achieve their policy objectives in the most effective and efficient way possible.

The problem is not confined to one level of Government. As the *Access Economics Report* demonstrates, the quantity of regulation continues to grow at all levels of Government in Australia.

The Productivity Commission has highlighted that there remains scope for the Commonwealth Government to do more to ensure that regulations do not impose unnecessary costs on business. It rightly argues that 'Ongoing review is required to ensure that regulations reflect changes in society and do not impose unnecessary burdens on business or the community.'[6]

Both the Commonwealth and State Governments should increase their efforts to remove regulatory overlap and duplication and to update regulatory regimes to enhance Australia's competitive environment. A more detailed discussion of the need for ongoing regulatory reform is included in the *Access Economics Report*.

While this *Options Paper* discusses potential reforms in the context of the Commonwealth Government, the models and reforms discussed are equally applicable to State Government, where the need for reform is arguably more pressing.

Inefficiencies, duplication and lack of simplicity still exist in Australia's regulatory management system.

2 The Three Structural Requirements for Better Regulation

The OECD and APEC have a joint initiative on economic and regulatory reform and have developed a checklist for self-assessment of regulatory, competition and market openness policies. The draft checklist includes the following criteria for best practice regulatory policy:[7]

- Is there a single body in charge of assuring the quality of existing and new regulation?
- Are there systematic reviews of the legal basis and economic impacts of drafts of new regulations?
- Are there systematic reviews of the legal basis and economic impacts of existing regulations?
- Are the rules, regulatory institutions and the regulatory management process clear and predictable to users both inside and outside of Government?
- Are there effective public consultation mechanisms and procedures that are open to regulated parties and other stakeholders, including non-Governmental organisations, the private sector, advisory bodies, standards development organisations and other Governments?
- Is systematic regulatory impact analysis required in the development of new regulation and the review of existing regulation and is it in accordance with agreed methodologies and criteria?
- Is consideration given to the alternatives to 'command and control' regulation?
- Is there assurance of, compliance with, and enforcement of, regulations?

Based on the work of OECD,[8] APEC and the Productivity Commission, there are three main requirements that need to be met to reform the business regulation-making process:

Requirement One:

Strengthen the regulatory institutional framework, that is the bodies within and outside of Government that influence the way business regulation is imposed, including through:

- structural reforms of the regulatory processes within public administrations;
- improving transparency and accountability mechanisms by building regulatory management capacities; and
- establishing a dedicated body (or bodies) to be consulted when new regulation is developed.

Requirement Two:

Improve the quality of new regulations, including through:

- more transparent and accountable processes for developing, consulting on and analysing the impact of new regulation, particularly through more robust regulatory impact assessment or regulatory impact statement processes; and
- clear principles and policies for good regulation, including benchmarks against which regulation and the processes for making regulation can be judged.

Requirement Three:

Improve the quality of existing regulations, through reviewing the existing stock of regulations against criteria aimed at removing or improving redundant, inefficient and overlapping regulation.

Each of these requirements, and how they are being met in other countries, is examined in the following Sections.

3 Strengthening the Institutional Framework (Requirement One)

3.1 AUSTRALIA'S INSTITUTIONAL FRAMEWORK

A well-designed institutional framework is a vital element of a regulatory quality system. It ensures that appropriate checks and balances, consultation, accountability and transparency in decision-making are achieved to produce high-quality regulation. The institutional framework consists of those bodies, both within and outside of Government, that are established to influence when and how Governments put in place business regulation.

A central element of the Commonwealth Government's framework is the Office of Regulation Review (ORR). The ORR is a unit within the Productivity Commission independent from the executive arm of Government. Its role is to promote the Commonwealth Government's objective of effective and efficient legislation and regulation, and to do so from an economy-wide perspective (see Exhibit 1).[9] The ORR provides advice to approximately 100 regulation-making bodies or regulators, including 60 Commonwealth departments and agencies and about 40 Ministerial councils and national standard-setting bodies.[10]

EXHIBIT 1: CHARTER OF THE OFFICE OF REGULATION REVIEW (ORR)

The functions of the ORR, as set out in its charter, are to:

- advise the Government and its 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 regulatory 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 regulatory impact statement guidelines, and on regulatory reform developments more generally;
- provide advice to Ministerial councils and national standard-setting bodies on COAG guidelines that 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 Government.

Source: Office of Regulation Review, www.pc.gov.au/orr

The Productivity Commission, an independent statutory authority, is the Commonwealth Government's principal review and advisory body on microeconomic policy and regulation covering all sectors of the economy. It conducts public inquiries and research into a broad range of issues, and makes recommendations to Government on improving the quality of specific regulations, sectoral policies, programs and processes.[11] The Commission is headed by a chairperson and between four and 11 other commissioners, who are appointed by the Governor-General for periods of up to five years. Its Annual Report highlights areas of regulatory reform and identifies areas for future reform. The ORR contributes through its Report, *Regulation and its Review*, mainly focused on compliance with regulatory impact statement (RIS) requirements.

The Commonwealth Government has set up a number of external independent advisory bodies to advise the Government on aspects of regulation. These include the Corporations and Markets Advisory Committee (CAMAC), the Business Regulation Advisory Group (BRAG) and the Financial Services Advisory Council (FSAC). These groups have responsibility variously for advising on ways of reducing or improving business regulation. Other permanent or ad hoc committees, advisory panels and task forces that have advised Government on regulatory issues include the Australian Law Reform Commission, the Small Business Deregulation Taskforce and Small Business Consultative Committee.[12]

Responsibility for preparing a regulatory impact statement rests with the department or agency sponsoring the regulation. The argument for this is that it ensures that regulators have 'ownership' over the assessment process, and that the assessment can be integrated early into the decision-making process. It is also argued that departments have access to expertise and resources in relation to the subject matter of the policy proposal. As discussed below and in the *Access Economics Report*, in practice these suggested advantages are often not realised.

Other components of the regulatory institutional framework include:[13]

- the Office of Small Business;
- the Treasury Department;
- independent regulators (for example ACCC, APRA and ASIC);
- the Senate Standing Committee on Regulations and Ordinances and the Senate Standing Committee for the Scrutiny of Bills; and
- Parliament itself.

There are also other institutions and mechanisms relating to regulatory reform between the Commonwealth Government and other jurisdictions (such as the States and New Zealand). These include the Council of Australian Governments (COAG) and the National Competition Council (NCC).[14]

3.2 | ATTRIBUTES OF AN EFFECTIVE INSTITUTIONAL FRAMEWORK

OECD research shows that dedicated bodies overseeing the development of new regulation are most effective if they are:[15]

Independent – free from undue influence from either regulators or private interests.

Endorsed – work under a clear regulatory policy that has been endorsed at the highest political level.

Horizontal – have the power to cut across Government.

Expert – staffed with experts who have the capacity and resources to make independent judgements.

Proactive – able to take the initiative in promoting regulatory reform.

Networked – have strong links to political authority.

As the analysis below shows, the Commonwealth Government's current institutional framework falls short of best practice.

A. Independent

The ORR is a unit within the Productivity Commission, which itself enjoys a degree of independence from the policy and regulatory arms of Government. Consideration could be given to whether this is the most suitable location for ORR. The logical alternative would be for ORR to be more closely connected to the Cabinet Office, to ensure regulatory proposals going before Cabinet satisfy the requirements of the RIS system. A number of States have adopted this model. Experience with this model, however, is that there is a much higher risk of the regulation oversight body becoming captured by the policy (and political) process.

The ORR has the multiple roles of policy development, review of draft RISs, advice and support, enforcement and review of the overall effectiveness of the RIS system. These multiple roles raise the issue of potential conflict of interests, reducing the independence of the body and therefore its effectiveness (for example, if the ORR is responsible for clearing individual RISs and therefore making a judgement on their adequacy, can it also independently review the overall effectiveness of the RIS system?). This concern could be overcome by having the ORR made accountable to another body for the performance of the RIS system, particularly a body not involved in the regulatory process, such as an external advisory body.

Bodies such as BRAG, FSAC and CAMAC are independent by virtue of their memberships. However, particularly in the case of BRAG and FSAC, the poor levels of transparency around their operation mean that the independence of that operation cannot be observed or tested.

Overall, there is scope to improve the level of independence within the current structure.

B. Endorsed

The ORR has received endorsement from the Commonwealth Government. However, ongoing public renewal of that endorsement is needed to ensure the ORR has the ability to achieve its objectives. Endorsement also needs to be matched by a commitment to give ORR the tools and resources it needs to fulfil its responsibilities.

There is a serious question over the Commonwealth Government's endorsement of other bodies established to advise the Government on improvements to the regulatory regime. For example, the Government has been slow to respond to reports of the Australian Law Reform Commission (ALRC) and CAMAC. As the recommendations of BRAG and FSAC remain confidential, it is not possible to determine whether the Government responds to their input (and hence to what extent their responses endorse the role of these bodies).

C. Horizontal

The ORR has a role across Government, providing advice to 60 Commonwealth departments and agencies and about 40 Ministerial councils and national standard-setting bodies. The Productivity Commission also has a role advising on regulatory issues across Government, although its ability to initiate its own work is limited.

There are also a number of external independent advisory bodies to Government (such as BRAG, FSAC and CAMAC). However, their roles are limited in scope. There is currently no body able to take a proactive role in recommending to Government priority areas for regulatory reform.

D. Expert

In making policy decisions, it is essential that expert opinion is sought, as regulation has a cost to the economy that needs to be appropriately assessed. Those assessing these costs should seek advice from both within and outside of Government. Seeking such expert advice should become a standard part of the process for determining the costs and benefits of proposals to introduce regulation.

At present, there are a number of advisory bodies to the Government that can give expert opinion. However, this ad hoc approach has a number of problems.

- Resources are diffused over a number of groups, meaning no group is adequately resourced.
- Each group has only a limited role, meaning there are gaps and overlaps of the development and administration of business regulation.
- Some external groups, such as BRAG, meet irregularly.

The workings of the groups are not transparent or widely known by the public and therefore the expert groups may lack the influence necessary for them to be effective.

E. Proactive

At present, none of the bodies involved in overseeing the development of regulation has a clear mandate to recommend broader regulatory reform. While this responsibility ultimately lies with the executive Government, without a formal body to develop and lead a regulatory reform agenda, there is a real danger that we will lose sight of the goals of removing unnecessary regulation and improving that regulation that remains. The evidence of a continued surge in new regulation suggests this has already happened.

F. Networked

The ORR is a unit within the Productivity Commission, and therefore has links to a prominent review authority. Its mandate covers all areas of Government as well as intergovernmental bodies. The ORR is at arm's length from policy development and regulating Government agencies. While this independence is important (see A. 'Independent' above), it can result in Government agencies seeing ORR as an intruder into the policy process, obstructing policy and regulation development.

This would be overcome if ORR had a greater role in developing and driving an overall regulatory reform agenda and if there were more formal links between ORR and other agencies, including dedicated units within other agencies charged with promoting deregulation and better quality regulation, as well as involvement in the RIS process.

The Commonwealth's structures for overseeing the development of regulation show aspects of each of the above elements. However, there is also significant room for improvement against each of these criteria. The following Sections analyse the institutional frameworks of other countries and explore possible improvements that could be made to the Commonwealth framework.

3.3 | OPTIONS FOR STRENGTHENING THE INSTITUTIONAL FRAMEWORK

Regulatory review authorities need to perform three broad functions:[16]

- advice and support: providing advice and support to regulation developers, including training and guidance;
- challenge: challenging regulation developers, including through assessing the quality of RISs; and
- advocacy: promoting regulatory reform objectives.

There are a number of functions that the BCA believes should be performed within the regulatory institutional framework as a whole, to ensure high-quality regulation. As the discussion below on possible models demonstrates, not all of these functions need to be performed within the one regulation review body.

1. Advice and support

a. reviewing proposals to regulate and the proposed regulations, including the associated RISs to ensure they comply with proper processes;

b. reviewing the implementation and administration of regulation;

c. ensuring adequate consultation with affected interests; and

d. preparing and publishing written guidance and providing training in regulatory quality issues.

2. Challenge

a. developing, advising on and overseeing a regulatory reform program (including monitoring and evaluating efforts to improve the quantity and quality of regulation); and

b. in some circumstances (such as where the regulatory proposal is likely to impose a major new burden on business), reviewing the content and merit of policy proposals and RISs, and challenging them from a broad policy perspective.

3. Advocacy

a. researching and reporting on topical issues, both proactively and at the request of Government;

b. developing policy initiatives to reform the regulatory system; and

c. articulating and promoting principles of good regulation.

Because of the broad scope of the roles, and the potential for conflicts of interest, it can be necessary to create separate institutional bodies to perform these roles. A number of OECD countries have taken the approach of developing several oversight bodies with different and distinct roles (with the exception of countries like Korea, which have very strong central Government influence).

Ideally, the model for the institutional framework in the Commonwealth system should adequately allocate responsibilities so that an efficient, transparent and accountable system is implemented in a manner that avoids overlap or conflicts of interest.

The range of possible institutional structures and divisions of responsibilities that could be implemented in the Commonwealth system are discussed below, by reference to overseas experience.

3.3.1 Independence

The ORR has the role of assessing RISs and whether they comply with proper process. The ORR also provides training for those policy agency officials who are preparing RISs and reports annually on the adequacy of RISs, RIS guidelines and regulatory reform developments.

The OECD has found that 'a well-organised and monitored process, driven by "engines of reform" with clear accountability for results, is important for the success of the regulatory quality policy'.[17]

It is essential that there is a regulatory body with the power to direct the regulatory reform program, to assess significant regulatory proposals from a merit perspective (rather than a process perspective) and to make decisions on policy issues. There is no Commonwealth entity at present that has overall responsibility for developing a regulatory reform agenda, and with the power and influence to see that agenda through. The ORR does not have this breadth of responsibility, nor a readily accessible link to senior Ministers (or the Prime Minister). The Treasury portfolio can play an important role in promoting the concept of better regulation, but is itself the source of much business regulation, with these two roles potentially coming into conflict. External bodies, such as CAMAC, BRAG and FSAC, have more limited roles and arguably lack the influence to lead a broader regulatory reform agenda.

Regulation reform program

The Commonwealth system needs a separate independent oversight and review body within the Government, with the power to:

- develop and manage a Government-wide business regulation reform program; and
- review the merits of individual regulatory proposals and the content and quality of their RISs.

On the basis of overseas experience, a body made up of Ministers and chaired by the Prime Minister appears to be an increasingly common approach. Such a body ensures that the Government's regulatory reform goals are supported at the highest level of Government and there is greater accountability for Ministers and agencies to justify new business regulation through demonstrating both the need for the regulation and that the benefits of the regulation outweigh the costs.

In Australia, such a body could be created:

- as a reconstituted ORR with a more direct link to the Prime Minister (such as the models in the US (see Exhibit 2) and Korea (see Exhibit 3)); or
- in a similar manner to the Panel for Regulatory Accountability in the UK (see Exhibit 4) or the Ministerial Committee in the Netherlands (see Exhibit 5).

There is no Commonwealth entity at present that has overall responsibility for developing a regulatory reform agenda, and with the power and influence to see that agenda through.

A Reconstituted ORR

OECD research shows that the strongest central units to promote and oversee regulatory quality are in the countries with presidential systems, such as Korea, Mexico and the United States.[18] The strength of these bodies, with power to implement the regulatory reform program and review policy proposals separate to the regulatory bodies, has resulted in all three countries making 'impressive gains in improving their domestic regulatory systems'.[19] Models that operate in a presidential system, where there is a clear separation between the executive Government and the legislature, will not necessarily translate successfully to the Australian context:

> 'More so than most parliamentary systems, presidential systems have the capacity for cross-cutting, top-down policy reforms, and have a tradition of institutional structures to carry out presidential policies.'[20]

The benefit of a single centralised body, such as the Office of Information and Regulatory Affairs (OIRA) in the US and the Regulatory Reform Committee in Korea, is that there is a clearer separation of roles and a lack of complexity compared to a system with multiple oversight entities and, as a result, there are clear communication lines within the institutional framework.

The Korean model is interesting because the Regulatory Reform Committee includes Ministers and non-Government members. While the applicability of the Korean model to Australia is limited, the ORR could benefit from having private sector individuals as members in a manner similar to the Korean model. This would ensure the ORR has cost-effective and efficient access to expert opinions when making decisions about regulation and the adequacy of RISs. The problem with having external members on the oversight body, however, is that the Government body may be seen to be unduly influenced by individuals or special interests and therefore lacking in independence.

Clear separation of roles and clear communication lines are some of the benefits of a single centralised body.

EXHIBIT 2: OFFICE OF INFORMATION AND REGULATORY AFFAIRS (US)

In the US, the Office of Information and Regulatory Affairs (OIRA), part of the White House Office of Management and Budget (OMB), is located within the Executive Office of the President. OIRA has substantial authority under a Presidential Executive Order to review rule-making proposals. OIRA was established by Congress in the 1980 Paperwork Reduction Act. OIRA is staffed by career civil servants responsible for economic and related analyses.

OIRA reviews RISs three times during the decision-making process (at the planning stage, before they are published for comment and at the final stage). OIRA's broad role covers:

- reviewing RISs and regulations to identify decisions and policies that are not consistent with the President's policies, principles and priorities; and
- coordinating agencies, identifying and discussing inconsistencies with regulators and suggesting consistent alternatives.

OIRA has up to 90 days to undertake its reviews, and seeks the opinions of other bodies, including a scientific advisory panel set up to advise OIRA on specific areas.

Source: Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, pp. 54–5; www.thecre.com.

EXHIBIT 3: REGULATORY REFORM COMMITTEE (KOREA)

In Korea, the Regulatory Reform Committee is a centralised body that has a broad spectrum of roles, including:

- responsibility for the basic direction of regulatory policy and research and development of the regulatory system;
- obtaining and responding to public opinions on regulatory improvement; and
- monitoring and evaluating regulatory improvement efforts.

The Committee, which is supported by a unit within the Prime Minister's Office, includes the Prime Minister and six Ministers, sitting alongside non-Government members drawn from academia, the economics profession and business.

Sources: Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p 82; OECD (2000), *Regulatory Reform in Korea*, p. 16.

A separate ministerial task force

In countries such as the Netherlands, Norway and the UK, there are two or three bodies with responsibility for aspects of regulatory policy that formally and informally influence regulatory policy and push reforms.[21]

In the Netherlands and the UK, Ministerial committees have been established with direct links to the executive arm of Government and therefore have the power to guide reform objectives. These bodies do not have responsibility for advising and supporting the preparation of RIAs, but have the broader role of assessing the regulatory reform agenda and, in some circumstances, the merits of individual regulatory proposals. This is a useful structure as it ensures that the regulatory reform agenda is led by a body with links at the highest level of Government, while ensuring that conflicts of interest in the various roles required are reduced (see below for discussion on conflicts).

The OECD has stated with respect to the Netherlands' institutional framework:[22]

> 'The Ministerial Committee headed by the Prime Minister, and the impressive efforts of the Ministries of Justice and Economic Affairs, have been and will continue to be instrumental in getting reform actions underway.'

While the benefit of setting up a number of central oversight bodies is that 'reform is carried out across a broad front and has numerous supporters or champions'[23], the risk with a complex institutional framework is that it 'throws the co-ordination between reform bodies into sharp relief'.[24]

EXHIBIT 4: SUMMARY OF UK INSTITUTIONAL FRAMEWORK

In the UK, a number of centralised oversight bodies have been established with different roles in the regulatory management and reform process. Some of the main regulatory reform bodies are as follows.

- Panel for Regulatory Accountability (Panel) is a Cabinet committee chaired by the Minister for the Cabinet Office (currently the Prime Minister). Other members include the Chief Secretary to the Treasury. The Panel directs the regulatory reform process. The Panel also considers, and where appropriate clears, individual proposals for new regulation where those proposals are likely to impose a major new burden on business, before the proposal is put to Cabinet. The Panel's consideration is informed by a thorough impact assessment of the proposal that has been agreed by the Cabinet Office Regulatory Impact Unit. Ministers may be asked to appear before the Panel to report on their department's programs of regulatory reform and to justify specific costly or controversial proposals. Ministers also report to the Panel on the overall regulatory activities and performances of their department. The chairman of the Better Regulation Task Force and the chief executive of the Small Business Service are asked to attend.
- The Cabinet Office Regulatory Impact Unit (RIU) provides guidance to departments and agencies on the preparation of RIAs and advises Cabinet Ministers, and the Panel, on the quality of RIAs. The RIU also supports the Better Regulation Task Force, works with stakeholders in the public sector to cut public sector red tape and promotes the better regulation agenda in the European Union. RIU has issued guidance to support the preparation of RIAs.
- An independent advisory group, the Better Regulation Task Force (BRTF), has been established to advise the Government on action to improve the effectiveness and credibility of Government regulation by ensuring that: it is necessary, fair and affordable; simple to understand and administer; and takes particular account of theneeds of small business and of ordinary people. The BRTF has a wide membership drawn from a variety of backgrounds, including large and small businesses, citizen and consumer groups, unions, the not-for-profit sector and those responsible for enforcing regulations. The BRTF has established principles of good regulation and undertakes studies on particular regulatory issues. The members and the chairperson are appointed by the Minister for the Cabinet Office (currently the Prime Minister). Members are unpaid and secretariat support is provided by the RIU.

Sources: UK 2004 Budget Report; OECD (2002), *Regulatory Reform in the United Kingdom*.

EXHIBIT 5: SUMMARY OF THE NETHERLANDS' INSTITUTIONAL FRAMEWORK

The Netherlands has established a number of centralised oversight bodies with different roles in the regulatory management and reform process. Some of the main regulatory reform bodies are as follows.

- A Ministerial committee chaired by the Prime Minister directs the reform process. Other standing members include the Ministers of Justice and of Economic Affairs (also responsible for competition policy), who are considered 'coordinating' ministers for the reform program. All Cabinet Ministers have a standing invitation to attend the committee's meetings and in practice other Ministers often participate. At the political level, therefore, the reform program is managed by a body with the authority, accountability and cross-cutting vision to provide strong impetus for reform.
- The Civil Service Commission identifies priority areas for reform and prepares reform proposals for consideration by the Ministerial Committee. It appoints ad hoc working groups to prepare specific proposals for the Ministerial Committee. It has civil service members but may also include experts from the private sector, academia, and local or provincial Governments. Notably, private sector appointees do not have full access to the deliberations of the working groups. Chairpersons of the working groups are civil servants, but for independence, they are not appointed from the department with major responsibility for the area under review.
- The Ministries of Justice and of Economic Affairs are allocated defined implementation responsibilities and day-to-day running of the reform process. Each Ministry runs a support desk providing services such as guidance and assistance on the scrutiny of regulatory proposals.

Source: OECD (1999), *Regulatory Reform in the Netherlands*.

Conflict between roles

There are differences between the 'advice and support' function, which involves providing support, training and guidance, and the 'challenge' function, which includes a quality review of RISs.[25] In Australia, the ORR conducts both functions, although the ORR generally only reviews individual RISs for their adequacy and compliance with the RIS process, rather than assessing the merit of the regulation proposal itself. The ORR is not able to make decisions on the merits of proposals to regulate or on whether regulation should be the preferred tool for achieving a policy objective. Accordingly, the 'challenge' function conducted by the ORR lacks power. The OECD states with respect to the 'challenge' function:[26]

> 'A central pillar of regulatory policy is the concept of an independent body assessing the substantive (i.e. rather than legal) quality of new regulation and working to ensure that Ministries comply with the quality principles embodied in the assessment criteria. The regulatory challenge function centres on the ability of the oversight body to question the technical quality of the RIA and of the underlying regulatory proposals. To perform these tasks, the oversight body needs the technical capacities to verify the analysis of impacts and the political power to ensure that its view prevails in most cases, rather than being overridden.'

In the Australian context, it would be appropriate to separate the 'advice and support' and the 'challenge' roles, so that an assessment of the RIS, based on compliance with proper process, is conducted by the ORR, and the assessment, based on the merits of the regulatory proposal, is conducted by a body that has strong links to, or is a central element of, the executive arm of Government. This approach finds support in the OECD's assessment of different models:[27]

> 'Because an objective assessment can be very disruptive in terms of regulatory processes ... a clear separation between the regulatory oversight body, as the examiner of RIA, and the gatekeeper to the Cabinet, may be required in order to preserve the independence and freedom to act on the former ... the requirement for a clear distance between the role of assessor and of enforcer needs to be maintained, in order to safeguard a robust assessment process, reduce any potential 'conflict of interests', and create a tension for the regulatory oversight body between its challenge function and its advice and support function.'

Further, the ORR has potential conflicts between its 'advice and support' role, its role in reviewing the adequacy of individual RISs and its review of the performance of the RIS process overall. If the ORR is responsible for providing support to those preparing RISs, but then assesses the adequacy of the results, there is a danger that its assessment of the adequacy of RISs will not be objective. Similarly, there is an incentive for the ORR to report that the RIS process overall is more effective in influencing regulatory outcomes when it is responsible for the development and support of that process. The BCA does not suggest that the ORR currently operates in this manner. However, the risk under the current structure remains.

In the UK, the three functions of 'advice and support', 'challenge' and 'advocacy' have been clearly separated out:

- the Cabinet Office Regulatory Impact Unit has responsibility for guiding the preparation of individual RISs (broadly an 'advice and support' role);
- the Panel for Regulatory Accountability has been established by the Prime Minister to take an overall view of the regulatory implications of the Government's regulatory plans and to ensure necessary improvements in the regulatory system and the performance of individual departments.[28] The Panel may also 'challenge' individual proposals for regulation where these proposals are likely to impose a major new burden on business;[29] and
- the Better Regulation Task Force provides some enforcement role in reporting on RIS compliance as well as reports and initiatives on regulatory reform (broadly an 'advocacy' role).

The Netherlands has also set up a process where the different roles are divided between the Ministerial Committee chaired by the Prime Minister, which directs the reform process, and the Ministries of Justice and of Economic Affairs, which are responsible for the day-to-day oversight and quality management of the regulatory system.

3.3.2 Endorsement

The OECD's analysis of successful regulatory reform shows that the most important ingredient is strong and consistent support at the highest political level and that:[30]

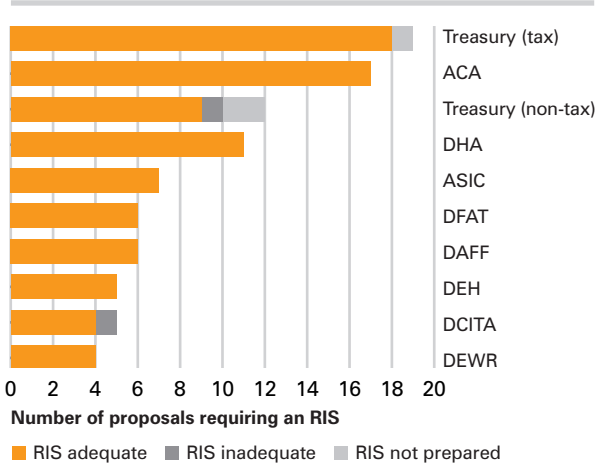
> 'Ministers have a direct role to play in assuring that strong political leadership will overcome vested interests in both public and private sectors which benefit from the status quo and resist beneficial change.'

As shown in Exhibit 4, in the UK it is a Ministerial panel that has responsibility for providing clearance for regulatory proposals that are likely to impose a major new burden on business, based on a thorough impact assessment of the proposal agreed by the RIU, before the proposal is put more widely for Ministerial approval.[31] Ministers may be asked to appear before the Panel to report on their department's programs of regulatory reform and to justify specific costly or controversial proposals. Ministers also report to the Panel on the regulatory activities and performances of their department.[32] The Prime Minister currently chairs the Panel, adding weight to this process and ensuring that Ministers are accountable for their regulatory performance.

In the Netherlands, a Ministerial committee chaired by the Prime Minister directs the reform process. Other standing members include the Ministers of Justice and of Economic Affairs.

In contrast, in Australia the ORR has limited access to the highest levels of Ministerial power. The ORR currently reports to the Parliamentary Secretary to the Treasurer and may, in exceptional circumstances, raise its concerns with a regulatory proposal with the Treasurer or the Prime Minister. One issue with this structure is that Treasury is a major source of business regulation and there is therefore a risk that the Ministerial advocate of a regulatory proposal (the Treasurer) will be more senior than the Parliamentary Secretary responsible for the ORR (a junior Minister within the Treasury portfolio). This may help explain the relatively poorer performance of the Treasury portfolio in preparing RISs (see Figure 1 below).

FIGURE 1
RIS ADEQUACY



Source:Productivity Commission, *Regulation and its Review 2003–04,* Annual Report Series.

3.3.3 Horizontal/expert advisory bodies

It is essential that advisory bodies representing a broad spectrum of private sector interests are incorporated into the institutional framework for managing regulation and the regulatory reform agenda. The OECD has identified 'advocacy' as a major role of regulatory oversight bodies. Advocacy refers to the promotion of long-term regulatory policy considerations, including policy change, development of new and improved tools and institutional change, rather than to the daily regulatory management function.[33]

Advocacy bodies can take the form of advisory bodies, think tanks or other research bodies, and they can be extremely useful in identifying priorities for the future direction of regulation-making and the regulation policy-making agenda. The Victorian Competition and Efficiency Commission defines advocacy bodies as bodies 'providing independent and/or expert advice to Ministers, regulators or departments to inform regulatory decision making and function as standing consultative mechanisms.'[34]

The Commission identifies advisory bodies as having the following characteristics:[35]

- They do not have formal decision-making powers.
- They are set up by legislation or at the initiative of a Minister or Government agency.

- They are independent from the executive Government, with a defined membership based on specific skills or ability to represent specific interests.
- They are established for an extended period or on an ongoing basis (rather than for the particular term of a project).

Important contributors to the reform process are those affected by regulation, which can include businesses, consumers and employees, and therefore open communication and consultation is an important ingredient of an effective institutional framework. The OECD states that the importance of the advocacy function is threefold:[36]

> 'First, **expert regulatory reformers** are clearly the best placed to identify new and promising tools and practices to advance regulatory quality ... Secondly, advocacy also helps monitor the benefits deriving from reform and **disseminate this information** within Government and the society generally ... Lastly, a regulatory advocate can help build and maintain constituencies for reform and undermine vested interests in their efforts to oppose socially beneficial reforms.' [emphasis added]

It is therefore essential that advisory bodies are able to capture all the relevant voices and expert advice.

At the Commonwealth level, there are a number of advisory bodies drawn from independent external sources, such as CAMAC, FSAC and BRAG, which are approached for their views on specific issues. The reports or recommendations of these bodies are not always made publicly available, so their effectiveness cannot be tested. Further, these advisory bodies have overlapping interests and no body has the overall role of promoting better business regulation, resulting in a lack of consistency, transparency, direction and simplicity within the institutional framework. Based on publicly available information, the BCA has been unable to determine the total number of bodies advising the Government on regulatory matters.

Problems with the current structure include:

- Resources are diffused over a number of bodies and no body is adequately resourced.
- Each body covers only limited functions, meaning there are gaps and overlaps in the advice Government gets on the development and administration of business regulation.
- Some external bodies, such as BRAG, meet irregularly.
- The activities and recommendations of the bodies are not public or well known, reducing their influence.
- The bodies are largely reactive to proposals of the Government, rather than being empowered to act proactively and make recommendations to Government on the regulatory reform agenda.

There is a large number of advisory bodies at the State level. In response to a Victorian Competition and Efficiency Commission survey, for example, 47 Victorian regulators provided information about a total of 80 permanent advisory bodies.[37]

The Commission identified a number of problems associated with this plethora of advisory bodies, including overlap of functions, confusion both within and outside Government about the institutional framework, lack of consistent and relevant representation of interests and undue influence over regulatory decisions.[38] The Commission recommended that advisory bodies should not have de facto decision-making powers, which may result if there is a lack of accountability and a 'closed club' on policy advice.[39] The Commission also recommended that policy development should be left to other more transparent processes, stating that while 'effective advisory bodies can provide valuable input into the regulatory process, ineffective bodies can increase confusion and raise the costs of regulation.'[40]

The Commission provided draft recommendations to improve the problems associated with multiple advisory bodies. One draft recommendation is that Victorian Government departments and regulators must include in their annual reports information on each advisory body they support, including:[41]

- how each body's activity contributes to improved policy outcomes;
- details of membership of the body, including any changes that took place during the year;
- the total remuneration, if any, of the chair and members;
- indicative estimates of the costs of administrative support of the body;
- date of formation, and when any review of the body's roles occurred; and
- a point of contact in the sponsor department or regulator, from whom further information can be obtained.

Other draft recommendations include better guidance and mechanisms for establishing and reviewing advisory bodies.

While these recommendations offer some solution in relation to dealing with multiple advisory bodies, and should be considered by the other State Governments and the Commonwealth, problems such as overlap, budgetary requirements and lack of effective accountability and representation will remain while so many bodies exist. Further, most advisory bodies lack the ability to initiate their own work program and ideas. Accordingly, a single strong independent external advocate of reform is required to bring external perspectives and interests as well as specific areas of expertise into the regulatory system.

That advocate must also have sufficient influence to allow it to make an impact, but must also operate in a transparent and accountable way. While the advisory bodies in the Commonwealth institutional framework bring a variety of interests and experience into the system, the lack of cohesion, transparency and influence means that their work is not subject to scrutiny and is less likely to influence the Government's decision-making process.

There are a number of models employed overseas for obtaining independent input within the regulatory reform institutions. These include:

- civil service bodies;
- institutionalised independent advisory groups; and
- independent advocacy groups.

Civil service bodies

In some overseas jurisdictions, special civil service departments or bodies have been established to gain expert opinion in certain areas. As an internal body, such a structure runs the risk of lacking independence.

For example, in Canada, the Deputy Ministers Challenge Team on Law Making and Governance was established to provide direction on regulatory reforms in six targeted sectors of the economy. It currently functions as an internal forum, meeting two or three times a year, for senior officials to discuss regulatory policies and propose broad directions for the improvement of regulatory governance. In the US and the UK, small business industry agencies coordinate with the bodies responsible for RIS oversight on appropriate small business impact analysis (see Exhibits 6 and 7).

While these initiatives have been helpful in ensuring that the interests of small business are considered, there is a risk that civil service bodies cannot be independent enough, nor drawn from a wide enough range of sectors, to ensure all interests are considered. The OECD suggests that this is one area for reform of the US institutional framework:[42]

> 'The effectiveness of US regulatory review could be improved by comprehensive assessments by a high-level advisory board, commission or task force of how the regulatory framework affects an economic sector, emphasising policy effectiveness and impacts on consumer welfare as performance measures.'

EXHIBIT 6: SMALL BUSINESS SERVICE (UK)

The Small Business Service (SBS) in the UK is a single organisation established to provide a voice for small firms within Government, and has a strong institutionalised position (for example, the SBS has the right to have its views recorded in the RIA in a wording of its choice). The SBS is an executive agency of the Department of Trade and Industry (DTI), and is funded by the department. The SBS consults with stakeholders, through bodies such as the Small Business Council (SBC), an advisory non-departmental body.

The SBC meets with small business by holding meetings and interviews throughout the UK. The SBC asks for initiatives to be undertaken by the SBS.

For example, the SBS was asked to publish a cross-Government strategy for small businesses, which the Government did in 2004. The SBC's 24 members are owners of small businesses, representing different sectors from all parts of the UK. The Regulatory Interest Group within the SBC has built up a working relationship with the BRTF and DTI's better regulation team. The SBC reports to the Secretary of State for Trade and Industry, advises the chief executive of the SBS and advises and reports on the effects of small businesses of the activities and potential activities of Government.

Source: OECD (2002), *Regulatory Reform in the United Kingdom*; also adapted from www.sbs.gov.uk.

Further, the OECD has cautioned against undue focus on small business interests and has stated, in respect of the US system such as the SBA,[43]

> 'Although the emphasis on SME impacts is understandable, an issue that should be closely watched is the tension between treating SMEs fairly and treating them preferentially. Too much tailoring of rules could result in 'positive' discrimination mechanism that distorts competition. Undue attention to the particular interests of a very diverse set of SMEs may create a more complex regulatory system. Exception and loopholes may reduce the transparency of the system. SME concerns may also hinder important global reforms, affecting consumers as well as other firms.'

Accordingly, while it is clear that a single advisory body with an 'advocacy' function, with sufficient prominence and power to take initiative, would be desirable in Australia, it should be representative of all business interests and have members drawn from the private sector.

EXHIBIT 7: SMALL BUSINESS ADMINISTRATION (US)

In the US, a number of initiatives have been set up to consider small business interests:

- The Small Business Administration (SBA) was set up to monitor compliance with legislation that affects small business. The body, being set up and funded legislatively, has therefore been provided with powers in the regulatory process.
- There have been legislative provisions requiring agencies to analyse the anticipated effects of proposed rules on small entities unless they certify that the rules will not have a 'significant economic impact on a substantial number of small entities'.
- There are also regulatory review panels consisting of employees from OIRA and SBA to assess small business issues. For example, legislation requires that certain departments, such as the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA) must receive input from affected small businesses before proposed rules are published. When an EPA or OSHA proposal is expected to have a significant impact on a substantial number of small entities, the agency must notify the Office of Advocacy, which then recommends small-entity representatives to be consulted on the rule and its effects. The agency then convenes a Small Business Advocacy Review Panel, consisting of officials from the agency, the SBA's chief counsel for advocacy and OIRA. The inter-agency panel reviews the draft proposed rule and the related analyses prepared by the agency. In addition, the Panel collects advice from identified small business representatives and submits a report to the agency within 60 days. Panel reports often include comments on the agency's preliminary analysis of the impact of the rule on small businesses and recommendations for regulatory alternatives. The agency reviews the report, makes any appropriate revisions to the rule and publishes the proposed rule with the Panel report as part of the record. The Panel process takes place in the early stages of the rulemaking. It does not replace publishing the proposed rule and accompanying economic analyses for general public comment.

Source: OECD (1999), *Regulatory Reform in the United States*; also adapted from www.sba.gov.

Independent advisory groups

Independent advisory groups take a number of forms. Some independent external advisory groups are legislated, like the Social and Economic Council in the Netherlands, while others, such as the Small Business Deregulation Taskforce in Australia, are ad hoc in nature and created with a specific objective or issue in mind.

As previously highlighted (see Exhibit 4), in the UK an independent advisory group, the Better Regulation Task Force (BRTF), has been established to advise the Government on action that improves the effectiveness and credibility of Government regulation by ensuring that it is necessary, fair and affordable, simple to understand and administer and takes particular account of the needs of small business and of ordinary people. Task Force members and publications have had a strong influence on setting the regulatory reform agenda in the UK.[44] The BRTF has a wide membership drawn from a variety of backgrounds, including large and small businesses, citizen and consumer groups, unions, the not-for-profit sector and those responsible for enforcing regulations. For assessing the broader implications and impacts of regulatory reform, it is essential that such a body has the necessary expertise and the independence to achieve its objectives.

In the UK, the BRTF has an important role in undertaking studies of particular issues. All reports are endorsed by the full Task Force and are then sent to the relevant Ministers, seeking their response. The Prime Minister has instructed Ministers that they must respond to BRTF reports within 60 days of publication. This ensures that the public is made aware of the recommendations of BRTF and also of the responses of Ministers. It places pressure on Ministers to demonstrate how recommendations are being implemented or to justify why particular recommendations are not being implemented.

Further, the BRTF has the role of regularly reviewing how Ministers and departments have acted on earlier BRTF recommendations, further adding pressure and accountability to ministers. In practice, the UK Government has taken up and implemented a large proportion of the BRTF recommendations.[45]

The OECD has found that a reason for the success of the BRTF has been that 'the Task Force's chairman since 1997 who enjoys high respect in Government and the business community'.[46]

Accordingly, a prominent chair, as well as political endorsement, is a key element for the success of such an independent body.

As previously described (see Exhibit 5), the Civil Service Commission in the Netherlands is made up of civil servants and independent experts. It appears that under the Netherlands model, the information sought from private sector interests is ad hoc, and the process is not always transparent (as the private sector members are not privy to all the available information discussed by the Civil Service Commission).

Accordingly, similar problems of lack of transparency and independence associated with the advisory bodies in the Australian system may be associated with such a system.

An independent advisory body in Australia set up along the lines of the BRTF and replacing some of the current independent advisory bodies, such as BRAG, would fit within the current Commonwealth institutional framework. The main funding requirements would be in relation to the secretariat role of the advisory body. This could be provided by the ORR.

Independent advocacy groups

Rather than the Government establishing independent advisory groups, private sector independent advocacy groups could make submissions to Government and conduct research themselves. For example, the Center for Regulatory Effectiveness (CRE) in the US (see Exhibit 8) conducts research into regulation-making and publishes the research on its website. This form of advocacy, however, lacks political endorsement and faces the challenges of funding and influence that many lobby groups face when attempting to influence political decision-making. Independent advocacy groups are arguably also more entrenched in the US, where there are strong notice and comment processes for new regulation, as well as a more adversarial approach to regulation making.

EXHIBIT 8: CENTER FOR REGULATORY EFFECTIVENESS (US)

The Center for Regulatory Effectiveness (CRE) in the US conducts research into regulation-making and publishes the research on its website. CRE staff have served at OMB and other federal agencies, so they possess both a technical understanding of substantive regulatory issues and of the procedural mechanisms that can be used to modify or halt regulations with serious problems. Based on this expertise, CRE is able to offer analysis and advocacy on regulatory issues in a cost-effective fashion. CRE's mode of operation is to undertake work on a range of issues for a number of firms, so the Center does not represent per se any particular member of an industry. CRE is supported by a number of trade associations and private firms, usually in the form of a monthly contribution to support the Center's activities.

Source: www.thecre.com

3.3.4 Proactive approach

The advisory bodies that form part of the current Commonwealth institutional framework are largely reactive, either reacting to issues that are referred to them (as in the case of CAMAC), or reacting to specific regulations put before them (as in the case of BRAG). While CAMAC has some scope to initiate its own research, overall the Commonwealth's advisory bodies cannot be proactive in terms of driving better regulation and regulatory reform.

Not only does this fragmentation mean that no single entity has the mission of driving reform across the spectrum of business regulation, but there is also a danger of these groups becoming co-opted into a system that is leading to ever greater levels of business regulation, rather than acting as a brake on this trend.

A strong independent regulatory body like the UK Business Regulation Task Force is necessary to address these shortcomings. Such a body should have substantial authority to determine its own work program and priorities. The issues examined by the BRTF are primarily selected by the BRTF itself.[47]

3.3.5 Networked

To be effective, the bodies charged with overseeing the regulation development and reform processes need to be networked with those parts of the Government that are responsible for the development of new business regulation. As noted above, however, this needs to be achieved in a way that does not impinge upon the independence of the review bodies.

The ORR is a unit within the Productivity Commission, and therefore has links to a prominent review authority. Its mandate covers all areas of Government as well as intergovernmental bodies. The ORR is at arm's length from policy development and regulating Government agencies. While this independence is important, it can result in Government agencies seeing ORR as an 'intruder' into the policy process, obstructing policy and regulation development.

This would be overcome if ORR had a greater role in developing and driving an overall regulatory reform agenda and if there were more formal links between ORR and other agencies, including dedicated units within other agencies charged with promoting deregulation and better quality regulation, as well as involvement in the RIS process. Such structures already exist in the UK (Exhibit 9) and Canada (Exhibit 10).

EXHIBIT 9: UK DEPARTMENTAL REGULATORY IMPACT UNITS (DRIUs)

In the UK, departmental regulatory impact units (DRIUs) have been established within Government departments as satellites of the central Cabinet Office Regulatory Impact Unit (which is responsible for the independent oversight of RISs and regulatory quality overall). DRIUs comprise from one to four staff, whose role is to advise and support policy teams in developing their RISs. Policy teams prepare RISs, which are then submitted to Government Ministers who, following consideration, are asked to sign off with a statement that in their opinion the benefits justify the costs.

Departments have to report annually on their better regulation performance, and this is linked by Treasury to their funding. There are non-executive Board members and individual board-level champions of better regulation in each department. The BRTF analyses the reports and publishes their analysis. This centralised body increases the accountability of each of the DRIUs (as their better regulation performance is linked to funding) and also increases the 'ownership' of the RISs and the policy proposals produced within the department.

Source: Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003.

EXHIBIT 10: SPONSORING DEPARTMENTS (CANADA)

In Canada, sponsoring departments are responsible for drafting regulations, drafting the RIA and related documents. Departments have set up one or two units in charge of these tasks. They vary in size, resources and quality. There are seven major regulatory departments.

Reports are provided by the departments to Parliament, each department presenting two reports, one covering planning and priorities and the other covering performance and outcomes.

Source: OECD (2002), *Regulatory Reform in Canada*.

The position of ORR would also be strengthened if it had closer links with the external advisory bodies set up by Government to advise on regulatory reform.

3.4 | PROPOSED MODEL FOR THE INSTITUTIONAL FRAMEWORK

Section 3.3 of this *Options Paper* analysed the current institutional framework of the Commonwealth Government and models employed overseas against the OECD's criteria for effective bodies to oversee the development of new regulation:

Independent – free from undue influence from either regulators or private interests.

Endorsed – work under a clear regulatory policy that has been endorsed at the highest political level.

Horizontal – have the power to cut across Government.

Expert – staffed with experts who have the capacity and resources to make independent judgements.

Proactive – able to take the initiative in promoting regulatory reform.

Networked – have strong links to political authority.

Based on this analysis, the most effective and appropriate model for the Commonwealth Government would be one based upon the institutional framework that operates in the UK and the Netherlands. The basic elements of this model are set out below.

3.4.1 Elements of an effective institutional framework

The three elements of the proposed model are:

1. A Ministerial Task Force (the 'challenge' element);
2. An enhanced regulatory impact assessment unit, supported by departmental regulation units (the 'advice and support' element); and
3. An external regulation advisory council (the 'advocacy' element).

Ministerial Task Force

A Ministerial Task Force should be established, consisting of 3–4 Cabinet Ministers, chaired by a senior Minister (ideally the Prime Minister), and meeting to:

- review the costs and benefits of proposals for major business regulation, including the adequacy of the RIS and consultation processes, before proposals are considered by Cabinet, and
- develop and oversee the Government's regulatory reform agenda, including accepting and assessing reports from Ministers on their efforts to reduce and improve regulation.

Ideally, the members of the Task Force would be: the Prime Minister (chair); the Treasurer; the Attorney-General; the Minister for Finance and the Minister for Industry.

Regulatory impact assessment unit

An improved regulatory impact assessment unit, such as an enhanced ORR, should be created, with responsibility for

- overseeing and advising on the development of RISs;
- providing training on assessing the impacts of regulation;
- reporting to both the Ministerial Task Force and the Business Regulation Advisory Council on the performance of the RIS system; and
- providing secretariat support to the Business Regulation Advisory Council (see below).

The regulatory impact assessment unit should be supported by departmental regulation units (DRUs) in each line department. DRUs would have responsibility for the development of regulations that affect business. They would consist of a small number of officials, answering to a senior executive in the department with responsibility for championing regulatory reform and the removal of costly, inefficient or redundant regulation. They would support the development of RISs by the department, and act as a liaison point between the department and the ORR.

Regulation advisory council

A Business Regulation Advisory Council (Advisory Council), be established consisting of representatives from across business and other affected groups, such as consumers, to:

- advise Government on the priorities and direction of regulatory reform, including identifying across all levels of Government where the biggest problems lie;
- coordinate consultation on major proposals for business regulation;
- coordinate reviews of existing regulation and whether specific regulations need to be removed or improved, and consequently making recommendations to Government;
- report on the adequacy of the existing law to deal with topical issues;
- report on the stock or quantity of regulation in place (particularly once the *Legislative Instruments Act 2003* comes fully into effect in 2007), and
- perform the above functions with the support of a full-time executive chairman or officer, a dedicated secretariat, the ability to establish ad hoc subcommittees to address specific issues and the ability to second individuals from the private sector and academia.

4 Improving the Quality of New Regulations (Requirement Two)

4.1 REGULATORY IMPACT STATEMENTS

Regulatory impact statements (RIS) are designed to allow a better informed, independent and objective assessment of the costs and benefits of regulatory proposals. The RIS process should be both a process for assessing these benefits and costs and a method of communicating the results of that assessment to decision-makers, those to be affected by the regulation, and the broader community.

There is widespread agreement that an RIS, when done well, 'improves the cost-effectiveness of regulatory decisions and reduces the number of low-quality and unnecessary regulations'.[48]

The OECD's report, *Regulatory Impact Analysis*,[49] has developed 10 best practice principles to assess RIS programs in country reviews prepared under the OECD's regulatory reform program. These principles are a starting point for designing a system likely to maximise the benefits of the RIS system.

4.3.1 Maximise the political commitment to RISs

There should be clear Ministerial accountability for compliance with the RIS process. The use of RISs should be endorsed at the highest levels of Government.

4.1.2 Allocate responsibilities for RIS program elements carefully

Locating responsibility for RIS development with regulators improves 'ownership' and integration into decision-making. A central body is needed to oversee the RIS process and ensure consistency, credibility and quality. It needs adequate authority and skills to perform this function.

4.1.3 Train the regulators

Well-designed programs are necessary to give the regulators the skills required to perform the RIS function.

4.1.4 Use a consistent but flexible analytical method

The cost-benefit principle should be adopted for all regulations. Mandatory guidelines should be issued to maximise consistency.

4.1.5 Develop and implement data collection strategies

Quality data on the costs and benefits of proposed regulation is essential to useful analysis.

4.1.6 Target RIS efforts

Resources should be applied to those regulations where impacts are most significant and where prospects are best for improving regulatory outcomes.

4.1.7 Integrate RISs with the policy-making process

RISs should be integrated into the policy and regulation development process and development of the RIS should begin as early as possible. Regulators should see RIS insights as integral to policy decisions, rather than as an add-on requirement for external consumption.

4.1.8 Communicate the results

The results of RISs must be communicated clearly with implications and specific options identified.

4.1.9 Involve the public extensively

Those affected by regulation and other interest groups should be consulted widely and in a timely fashion.

4.1.10 Apply the RIS process to existing as well as new regulation

The disciplines of the RIS process should be applied to reviews of existing legislation, as well as to the development of new regulation.

4.2 | AUSTRALIA'S RIS SYSTEM

A Guide to Regulation[50] sets out the Commonwealth Government's policy on regulatory best practice and quasi-regulation. It is designed to assist officials in preparing RISs and provides guidance on aspects of best practice in regulatory design.

Since March 1997, the Commonwealth Government has required the preparation of an RIS for all reviews of existing regulation, proposed new or amended regulation, quasi-regulation and proposed treaties involving regulation, which will directly or indirectly affect business or restrict competition (a range of exceptions apply).[51]

An RIS should set out the relevant policy objective along with all the viable alternatives for achieving that objective. The intended purpose of an RIS is to ensure that Government departments and agencies fully consider the costs and benefits of all viable alternatives, to assist the Government in choosing the alternative with the maximum positive impact.

The ORR has the roles of training officers from departments and agencies in the preparation of RISs, providing advice to regulators about whether an RIS should be prepared (on a case-by-case basis) and reviewing compliance with RIS requirements. The Parliamentary Secretary to the Treasurer has been given overall policy responsibility to ensure compliance with regulatory best practice procedures.[52]

Overall, the RIS requirements set out in *A Guide to Regulation* are consistent with the OECD best practices listed above. In theory at least, the strengths of the Commonwealth Government system include:[53]

- Wide scope, both in terms of the regulatory instruments and types of bodies covered.
- Application of RIS requirements to reviews of existing regulations as well as to new proposals.
- Cost-benefit methodology that seeks to assess all important economic, social and environmental impacts, but at the same time is flexibly applied based on the principle of proportionality.
- Independent assessment of RISs by the ORR.
- Monitoring and reporting of compliance.

In its latest report, *Regulation and its Review 2003–04*, the Productivity Commission states that adequate RISs were produced for 92 per cent of proposals that required an RIS, and that 18 out of 24 agencies required to produce RISs were fully compliant (compared with 12 out of 23 in 2002–03).

However, evidence suggests that while the regulation-making processes may be being followed in many cases, the quality of regulation and the methods of seeking private sector input into the regulation-making process are far from adequate. A more detailed critique of the adequacy of the current RIS system can be found in the *Access Economics Report*.

That there is scope for significant improvement in the Commonwealth RIS system is well recognised. Productivity Commission Chairman, Gary Banks, stated:[54]

> 'Looking forward, the challenge is to increase the quality of the regulation impact statements, particularly in canvassing lighter handed regulatory options and assessing compliance costs.'

In particular, the Productivity Commission has highlighted that departments and agencies have had problems with fully complying with the RIS process as a result of:[55]

- **the late preparation of RISs in the policy development process;**
- **poor integration of the RIS requirements into the policy development processes; and/or**
- **duplication of the policy development processes.**

The ORR noted that 'At present, RISs typically contain a relatively brief qualitative assessment of the compliance cost burden of regulatory proposals.'[56]

While the Commonwealth RIS process has many of the characteristics of a sound process, as identified by the OECD, in practice there are significant weaknesses in the process, including late integration of the RIS into the regulation development process and a lack of quantitative assessment of costs and benefits of regulations in many RISs (see Exhibit 11).

EXHIBIT 11: 'ADEQUATE' ASSESSMENT OF COSTS AND IMPACTS

The Commonwealth Government's adequacy criteria for RISs require only that quantitative information on costs and benefits of viable regulatory options are set out where possible. Often this information will only be available if policymakers actively seek it out. Those without the time or inclination to identify and consult with affected parties can prepare an 'adequate' RIS by relying on the lack of available information.

Former Federal Greens MP Michael Organ highlighted a particularly bad example. The RIS that accompanied the Postal Services Legislation Amendment Bill 2003 asserted that there was no practical means of collecting information about the number of document exchange and aggregation services operating in Australia.

Mr Organ remarked 'I can only assume that the Internet was down that day, because a simple search of the Yellow Pages online produces a list of eight companies across the nation that do that work.'[57]

4.3 | SUGGESTED REFORMS FOR THE AUSTRALIAN RIS PROCESS

The following sections identify, by reference to the OECD 10 best practices, some of the potential areas for reform of Australia's RIS processes. Based on this analysis, the BCA has set out its preferred options in Section 4.4.

4.3.1 Maximise the political commitment to RISs

Government needs to continually review and update the RIS process, including the oversight body responsible for reviews of RISs (see Section 3). The institutional structures are extremely important for the integrity of the RIS process.

It is important that the RIS process is both announced and endorsed by Government, but also that the requirements are regularly reviewed and reaffirmed by the Government. The current Commonwealth RIS requirements were announced by the Prime Minister and are set out in the Cabinet-endorsed *A Guide to Regulation* (the 'Guide').

One option is for the Government to legislate the Guide to give it greater weight and transparency. While this could have some negative effects, such as a lack of flexibility and inability to easily amend the document, these may be offset by the increased importance given within Government to the development of better business regulation.

The Commonwealth Government should also reconfirm its endorsement of the Guide, and continuously review its applicability. For example, the *Regulatory Impact Guide* in the UK has a foreword by the Prime Minister, which highlights the review and updates that have occurred to the RIA process.

Further, accountability for RISs can be increased where they are signed off or certified by the responsible Minister or high-level officials (this is discussed in more detail in Section 4.3.2).

The OECD considers that a lack of credible sanctions for non-compliance with RIS requirements is a major weakness in many RIS systems. The Productivity Commission states, with respect to sanctions that the ORR can currently impose, that they represent 'relatively mild sanctions in the case of non-compliance'.[58]

The main sanctions for non-compliance (or incentives for compliance) within the current RIS system in Australia are as follows:[59]

- ORR reports to the decision-maker (for example, Cabinet) on the adequacy of RISs, prior to decisions being taken.
- ORR can report cases of non-compliance to the Assistant Treasurer, who may take the matter up with the relevant Minister or decision-maker (in extreme cases, the Assistant Treasurer may suggest the withdrawal of the submission and in less extreme cases, the Prime Minister can co-opt the Assistant Treasurer for the relevant cabinet discussion).[60]
- ORR maintains a compliance database and its assessment of compliance with RIS requirements is published annually as part of the Productivity Commission's annual report on *Regulation and its Review*.

In the UK, any regulatory proposal likely to place a 'major new burden on business' has to be cleared by the Panel for Regulatory Accountability (see Exhibit 4). A similar requirement should be introduced through the proposed Ministerial Task Force.

4.3.2 Allocate responsibilities for RIS system elements carefully

Ministerial and ORR sign-off

Ministerial and departmental accountability for the quality of regulations and RISs can be increased by requiring Ministers to sign off on the content of the RISs, certifying that the benefits of the proposed regulation justify the costs (as is required in the UK and New Zealand, and some Australian States).

OECD research supports this approach, suggesting that, to 'further increase accountability, it seems to be useful to require RIAs to be signed by Ministers or by high-level officials'.[61]

There is currently no formal requirement for certification of RISs by Ministers or officials at a Commonwealth Government level.

In some Australian jurisdictions, sign-off is required. For example, in Victoria, Ministerial sign-off is required to certify that the *Subordinate Legislation Act 1994* (Vic) has been followed, and that the RIS adequately assesses the likely impact of the proposed rule.[62] Under the COAG *Principles and Guidelines* (1997), in relation to the development of national standards and regulations, RISs must be certified by the relevant Ministerial council or national standard-setting body.[63]

In Queensland, agency heads must sign a compliance certificate, which must accompany the proposed instrument for the information of Cabinet and Executive Council. In Tasmania, the responsible Minister must, after the RIA is prepared, obtain a certificate from the secretary of the responsible agency certifying that the RIA complies with the requirements and that the nature and the extent of the consultation is appropriate (if this is not complied with, the Executive Council will not provide the required endorsement).

In the UK, the Minister must authorise that the benefits of proposed regulation justify the costs. In New Zealand, officials preparing Cabinet papers on behalf of the Minister must include a certifying statement in the Cabinet paper that the RIS and business cost compliance statement (BCCS), where relevant, comply with the requirements.[64]

In addition to Ministerial sign-off, the ORR should be required to add to the end of the RIS its statement as to whether or not the RIS process has been adequately followed.

Peer review of RISs

It is common in overseas jurisdictions for external independent peer reviews of RISs to be sought from experts. The Small Business Service in the UK and the Small Business Administration in the US are examples of specific agencies with responsibility for small business interests that are consulted on RISs that may have an impact on small business. Further, in the US, OIRA recommends that draft RISs be subject to formal, external peer review by independent experts.[65] The guiding principles for such peer reviews include that they should be conducted in an 'open and rigorous manner'.[66]

4.3.3 Train the regulators

Along with the obvious need for the ORR to continually train the regulators (and produce quality guidance materials for the regulators to use in producing policy), there need to be resources within departments to ensure that regulators are able to prepare RISs adequately. There also need to be performance measures and incentives to ensure the RIA process is taken seriously and approached by departments as a process requiring properly trained officials capable of performing the task effectively.

A limited number of regulatory agencies in Australia have introduced 'gatekeeper' roles by adopting a centralised or coordinated approach to the preparation of RISs. However, this has only been on an ad hoc and inconsistent basis.[67] This approach is more advanced in some overseas jurisdictions, such as the UK, Canada and Ireland. For example, the UK and Canada have created specialist units devoted to regulatory reform within departments (see Exhibits 9 and 10). Specialised units can ensure there are appropriately trained and responsible personnel for assessing regulations and preparing RISs.

In Ireland, senior officials in each department are allocated responsibility for the regulatory reform program in their respective departments and for reporting on progress.[68] In the US, the Office of Management and Budget recently issued Government-wide guidelines relating to the quality of information disseminated by federal agencies, including that agencies must issue their own tailored guidance compatible with the general guidelines.[69]

Motivational incentives are also required within Government departments. A common method of changing cultures relating to regulatory reform has been the linking of performance and results. For example, in the UK, regulatory performance is linked to departmental funding, while in the US, the *Performance and Results Act* of 1993 established a Government-wide system, including for regulators, to set goals for program performance and measurement, with publication of the results.[70]

Consistent processes for monitoring performance help to ensure that personnel have adequate training and expertise. For example, in Canada, departmental reviews are conducted on the basis of Regulatory Process Management Standards and a capacity check tool, which identifies five levels of capacity for each of the compliance criteria. Departments are rated on a Government-wide basis.[71] In 2000, the *Results for Canadians – A Management Framework for the Government of Canada* strengthened accountability for the use of regulatory powers, and in July 2001, a *Lexicon on Results-Based Management and Accountability* was published to help standardise terminology.

4.3.4 Use a consistent but flexible analytical method

Content requirements

The content requirements for Australian RISs are in line with OECD good practice. According to *A Guide to Regulation*,[72] RISs should include the following seven elements:

- a clear definition of the problem;
- an assessment of the regulation's objective;
- an assessment of all feasible options for addressing the problem;
- an impact analysis, including cost-benefit, impact and risk analyses;
- a summary of the consultation process and the views of stakeholders;
- a conclusion and recommended option; and
- how the regulation will be implemented and reviewed.[73]

The Government has endorsed a set of seven criteria for the ORR to assess whether an RIS meets the Government's regulatory good practice requirements (which broadly correlate to the seven sections of an RIS).[74] The Government has also imposed additional content requirements, which relate specifically to impacts on competition, the environment, small business and international trade and cost recovery issues.

While the Commonwealth's RIS content requirements are generally in line with OECD recommendations, there are a number of additional elements that should be included in RISs, specifically:

- details of the timing of the RIS process, including the time allowed for consultation; and
- a requirement for Ministerial sign-off, as discussed above.

The checklist for RISs should include a requirement for the regulation developer to set out publicly the timetable for the RIS process (including the timing of consultation and decision-making). This will ensure that those who are being consulted are made aware of the details of the timing. By including a timeline for the development of the RIS into the document, the ORR can determine whether that consultation took place at an appropriate point in the regulation development process and for a sufficient period of time to allow for meaningful consultation.

Cost-benefit analysis

In theory, the Commonwealth's RIS process is based on a cost-benefit analysis, including an assessment of all significant economic, social and environmental costs and benefits for all affected groups, with the depth of analysis commensurate with the significance of the impacts.[75] A *Guide to Regulation* encapsulates the concept that the 'benefits of any regulations should outweigh the costs'.

There are a variety of costing methods used in other countries. In the UK, for example, extensive policies, such as cost-benefit policies and a Code of Practice on Consultation, have been developed.

The cost-benefit policy should identify particular tests (such as impacts on all business and not just small business) to ensure that all relevant considerations are made. At present, most cost-benefit analyses used in Australia are rudimentary and there is a clear need to develop more comprehensive and sophisticated methodologies.

Compliance costs

A Guide to Regulation makes it clear that the expected compliance costs imposed by new regulation on business must be addressed in RISs.[76] In practice, the analyses included in many RISs are qualitative rather than quantitative. In *Regulation and its Review 2001–02*,[77] the Productivity Commission noted that improvements were required in RIS analyses of compliance costs and small business impacts (particularly in providing quantitative assessments of such costs).

More detailed guidance on assessing compliance costs is required to ensure that the impact of regulation on business is adequately assessed. In New Zealand, for example, departments are required to include, as part of the RIA, a business compliance costs statement, including the key issues relating to compliance costs identified in consultation.[78]

In the UK, the Cabinet Office has issued *Better Policy Making: A Guide to Regulatory Impact Assessment* (2003), which provides guidance on making cost assessments and requires total cost estimates to be accompanied by analyses showing the effects on typical businesses and on small businesses. According to the OECD, the UK guide provides an 'exceptionally well-designed set of tasks guiding the analyst in drawing a vivid picture of cost and benefit magnitudes and their distribution across those affected by regulation'.[79]

4.3.5 Develop and implement data collection strategies

Proper regulatory impact analysis cannot occur without quality data on the range of businesses likely to be affected by new regulation, the likely extent of the impact and the consequences for businesses of that impact. Much of this information is available already to Government, for example, through the data sets of the Australian Bureau of Statistics. Specific information can also be gained by identifying and consulting with those businesses likely to be affected by the regulation. Part of the reason that many Commonwealth RISs contain only qualitative, and not quantitative, information on the likely costs of new regulations is that consultation with business is not a standard feature of the Commonwealth RIS process, yet this information is not otherwise available except from the businesses likely to be affected. Better systems for consultation with the private sector are required. In overseas jurisdictions, various methodologies for consultation have been developed, including test panels and the use of Internet and email for achieving better targeted consultation with a cross-section of business interests (for example, by the European Union).

While consultation at the Commonwealth level is advised in *A Guide to Regulation*, it is not a requirement and there are no prescribed methods for conducting consultation. Further, it is important that affected interests such as business are consulted in a meaningful and targeted manner to avoid producing consultation fatigue.

A common overseas approach to targeting business interests has been to set up business test panels to be consulted on regulations that will have an impact on business.

In Canada, there is a two-stage business impact test process. The Business Impact Test is a software program that enables surveys to identify business views on the impacts of proposed regulation. The Business Impact Cost Analysis Protocol verifies and analyses the results of the surveys using interviews and accounting methods.[80]

In Denmark, business test panels have been created to obtain feedback from a cross-section of businesses and to identify any unanticipated major impacts from policy proposals. The test panels consist of a cross-section of businesses that are asked directly about the expected administrative burdens of proposed legislation.[81] In the Netherlands, a 'help desk' can assist with data collection[82] and provides statistical information, while under the Danish model, an enterprise program calculates total administrative burdens from extensive interviews with 'model' enterprises.[83]

In the Netherlands, a computer program (MISTRAL) is used to evaluate the impact of regulations on business in three stages. A process of consultation and discussion, individually and in groups, is used to obtain the data to be analysed in the computer process.[84] There would be considerable merit in exploring the development of a similar computer-based analytical tool in Australia.

4.3.6 Target RIS efforts

The assessment of regulatory impacts should be concentrated on those regulations that are expected to have the greatest impact on business and where the prospects are best for improving regulatory outcomes.

Under the current Commonwealth process, the level of detail required in the RIS should be commensurate with the magnitude of the problem and with the size of the potential impact of the regulatory proposals.[85] There are no specific threshold tests by which the ORR assesses this, but the ORR considers first the nature and magnitude of the proposal (and the problem), and second its impacts on affected parties.

A useful two-stage approach has been adopted in other jurisdictions, where almost all policy proposals are submitted to a preliminary RIS, but an in-depth RIS is only prepared where the impacts of the regulation are likely to be substantial. For example, in 2002, the European Commission adopted the *Simplifying and improving the regulatory environment* action plan, including a two-stage RIA process: a preliminary assessment is prepared on all major policy proposals; and, on the basis of this assessment, the Commission determines which proposals will require an extended impact analysis.[86]

A similar two-stage approach should be adopted at the Commonwealth level, with the ORR determining, based on the preliminary RIS, when a full RIS is required.

An alternative to the ORR determining when a full RIS is required would be to develop published thresholds, above which a full RIS is required. For example, in Mexico, the significance of a regulatory proposal is indicated by a combination of monetary and qualitative tests. Many Australian States have adopted monetary thresholds.[87]

In Korea,[88] a full RIA is applied to significant regulations only, which are defined as having:

- an annual impact exceeding KRW 10 billion; or
- an impact on more than 1 million people; or
- a clear restriction on market competition; or
- a clear departure from international standards.

A similar test to the Korean test is applied in the Netherlands (so that only approximately 8–10 per cent of draft regulations are subject to full RIA).[89]

In the US, a full cost-benefit analysis of a rule is required in the following instances:

- if annual costs exceed $US100 million; or
- where rules are likely to impose a major increase in costs for a specific sector or region; or
- if the rules have significant effects on competition, employment, investment, productivity or innovation.[90]

The problem with monetary thresholds, however, is that regulators have an incentive to underestimate the significance of their proposal in order to avoid having to conduct RIA analysis.

4.3.7 Integrate the RIS with the policy-making process

It is essential that RIS processes are integrated into the regulatory decision-making process and actually inform decision-makers. To be truly effective, the RIS process should influence decision-makers before a decision to regulate is made. Without this level of integration, the RIS process runs the real risk of becoming 'meaningless paperwork'.[91]

The OECD recognises that many developed countries continue to use RISs as a retrospective justification for a regulatory decision, stating that an RIS 'is typically regarded as an additional procedural requirement that, at best, explains the merits of the policy decision rather than determining the decision itself'.[92]

RISs can only assist in decision-making if the RIS process is commenced early in the decision-making process, before regulators are wedded to any particular regulatory proposal. Further, the RIS must be able to be amended and improved as new information and ideas are gained during the impact assessment and decision-making process. This can best be achieved through a staged approach to developing the RIS.

Early in the process

While *A Guide to Regulation*[93] states that the analytical framework underpinning an RIS should be used throughout the policy development process, one of the main failings of the Commonwealth system is that RISs are not being implemented early enough. The Productivity Commission stated that a:[94]

> 'common problem is that RISs are prepared late in the policy-making process, diminishing the capacity of the RIS to aid decision making. Late preparation can be a sign of poor internal management and planning, or may reflect underestimation of the complexity or impacts of a regulatory proposal, resulting in insufficient time being allocated to do the analysis and consult with the ORR.'

There is a policy requirement that RISs are implemented early in the process and in consultation with the ORR. Specifically, *A Guide to Regulation* provides that an 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 Government or its delegated officials that regulation is in fact necessary.[95] In practice, however, the RIS process is often 'tacked' onto the end of the regulation development process.

Some initiatives to alert departments and agencies to the requirements of RISs have been established, such as the 'gatekeeper' roles performed within the Department of the Prime Minister and Cabinet.[96] They are, in general, 'alert' functions regarding the requirement to produce an RIS, but because this generally occurs at the concluding stage of the policy development and drafting process, in practice they are unlikely to have a direct bearing on compliance at the more important decision-making stage.

Staged approach

The Commonwealth RIS process requires an RIS at the decision-making stage (that is, when regulatory proposals go before Cabinet) and at the Parliamentary tabling stage. At both stages, a full impact analysis is required. In practice, the tabling RIS is substantially the same as the initial decision-making RIS.

As has already been noted, one of the problems with the Commonwealth RIS process is that the RIS is often prepared too late in the policy process, and therefore regulators are already wedded to a particular regulatory response.

This could be overcome by requiring a two-stage approach for full RISs.

This approach is already being used in Australia in relation to the RISs required for Ministerial Councils and national standard-setting bodies. In this case, an RIS assessed by the ORR is required at two stages: the first for community consultation with parties affected by the regulatory proposal; and the second or final RIS, reflecting feedback from the community, for the decision-making body. This is a useful method of integrating the RIS into the decision-making and consultation program.

In Italy, the RIS is based on a two-stage submission: a preliminary assessment to be prepared in the initial stage and a fully-fledged RIS to accompany the final draft when submitted to the Council of Ministers (or before adoption of subordinate regulation not reviewed by the Council).[97] The initial stage focuses mainly on the justification and alternatives (including the 'do nothing' option) before the full text is written.[98]

In Ireland, the current process of regulatory reform recognises the need to ensure that RISs are conducted early in the process, and accordingly, the Irish Government has stated that:[99]

> 'It is envisaged that there will be a two-phase approach, the first stage involving relatively light preliminary assessments. In many cases, these will provide sufficient insight into likely impacts and costs. The second stage – the actual RIA – will be a more thorough analysis.'

The RIS system is also a two-stage process in the UK, Canada and the United States. In Denmark, a preliminary RIS justifying proposals on cost-benefit grounds is required at a relatively early stage. Before the Regulation Committee considers proposals for inclusion on the legislative program at the start of each year, Ministries must provide:

- a thorough description of the policy problem;
- a description of the purpose of the Bill;
- a description of the expected impacts on business, citizens, the environment and public authorities; and
- a demonstration that alternatives to traditional 'command and control' regulation have been considered.[100]

Overall, a two-stage approach has twin benefits: it can be used to determine when a full RIS is required (see Section 4.3.6), and the initial RIS can be used as the basis for consultation.

4.3.8 Communicate the results

Where regulation-makers and regulators are introducing new regulations that affect private interests, they should be accountable for the regulation and able to demonstrate that the benefits of regulatory intervention outweigh the costs. Improving the transparency of regulation-making processes, through increasing the amount of information put into the public domain, increases the accountability of regulators for their decisions. As there are deficiencies in the current reporting of regulatory decisions, there is a lack of transparency and accountability within the regulatory system.

Transparency is increasingly more easily achieved because information technology allows the establishment of publicly accessible, centralised databases with search engines, electronic filing and institutional re-engineering.

The OECD has highlighted that greater transparency in the making and administration of regulation is a pressing area for improvement among many OECD countries that have RIS requirements.[101] Increased transparency can help address many regulatory failures and the scrutiny and accountability that go with greater transparency increase the incentives for policy-makers to apply best practice processes in regulation development.

There is considerable scope for improving the transparency of the Commonwealth regulation-making process.

Tabling in Parliament

In Australia, an RIS becomes public when it is tabled in Parliament. The tabling requirement, however, only applies to Bills, disallowable instruments and treaties. RISs for other types of regulation, such as non-disallowable instruments and quasi-regulation, are not tabled in Parliament, although they may be made public. They are also not subject to formal assessment by the ORR.[102]

Ideally, an RIS should be released for public comment prior to being finalised. This would allow those likely to be affected by the proposed regulation and other interested parties to comment on the scope and content of the RIS and to provide any additional information before a final decision to regulate is made.

Monitoring and reporting on compliance

To improve scrutiny and accountability, transparency needs to be improved not just for the process of producing individual RISs, but also to improve the performance of the whole RIS system and business regulation.

There are some requirements for accountability of Australian regulatory departments, such as the requirement for preparation of regulatory plans, and the assessment of Regulatory Performance Indicators by the Office of Small Business[103] as well as the publication of *Regulation and its Review,* assessing compliance of RISs.

In the UK, the BRTF provides annual reports that include the RISs that have been reported to the National Audit Office for review. The BRTF is independent from Government and therefore provides an independent assessment of the quality of RISs. The National Audit Office assesses and reports on the RISs that are referred to it by the BRTF.

The OECD has advocated the need for clear assessment mechanisms and standardised assessments to provide clear feedback to Ministers about their efforts and the need for improvement. They point to the Mexican Economic Deregulation Unit and its grading mechanism to evaluate the quality of RISs as an example of a useful grading approach.[104]

4.3.9 Involve the public extensively

Consultation is a means of achieving transparency and also improving the quality of decision-making. Consultation promotes engagement between regulators and stakeholders to create a 'sense of ownership' among the interested parties and therefore increases the degree of compliance with the regulation when it is applied. Consultation also assists the collection of data from the people or groups to whom the regulation is addressed (including appropriate assessments of costs and benefits). Consultation should therefore be a key element in the RIS process.

The Commonwealth Government has, in recognising the importance of consultation, enshrined the requirement for consultation before legislative instruments are made in Part 3 of the *Legislative Instruments Act 2003* (which came into effect on 1 January 2005). The Act, however, provides little guidance on how consultation should be done or what constitutes adequate consultation (including the time to be allowed for consultation and response from consulted parties). Further, the Act only requires consultation when legislative instruments are made, but not when policy proposals are being considered and RISs prepared.

In *A Guide to Regulation*, there appears to be lack of commitment to the integration of consultation into the policy development process, as it states that 'Where consultation is not possible before regulation is made, consultation should occur afterwards.'[105]

The Government has also issued some limited guidelines on consultation, such as how consultation should be undertaken with particular groups, including small business.

The Small Business Ministerial Council has set out the key features of effective consultation as:

- flexibility;
- timeliness;
- accessibility;
- transparency;
- responsiveness;
- resources;
- evaluation; and
- continuity.[106]

In essence, guidance on effective consultation must answer four important questions:

- how to consult;
- whom to consult;
- how long to consult for; and
- when to consult.

How to consult

There are five tools of consultation: informal consultation; circulation of regulatory proposals for public comment; public notice and comment; hearings; and advisory bodies.

In Australia, under *A Guide to Regulation*, it is not compulsory for a draft RIS to be provided to stakeholders during the consultation process (although exposure of a draft RIS is noted as desirable). The Productivity Commission reports that, in relation to providing draft RISs during consultations, the 'practice is rarely followed'.[107]

In the US and UK, it is compulsory for the RIS to be provided to the stakeholders. Under the Australian COAG *Principles and Guidelines*, RISs prepared for national standards and regulations must be released in draft form for formal public consultation.[108]

Consultation regarding the wording of draft regulations does not always occur until the end of the process. In Italy, drafts of consolidated texts and simplification decrees have been published on a notice-and-comment basis. Such consultation increases the likelihood that the regulation will be understood and complied with, and also increases the likelihood that amendments will not be needed following the passage of the regulation through Parliament.

In the US, RIS procedures require that RISs for both proposed and final rules be released for public consultation, ensuring agencies are accountable for the quality and relevance of the RIS throughout the decision-making process.[109] It can also be argued that the considerable exposure of the US rules to legal challenge in the courts favours effective integration of the RIS with the policy process (RISs can be used as evidence).[110]

The Productivity Commission warns that stakeholders can be frustrated by consultation, which:[111]

- implies that a regulatory decision has already been made;
- does not provide adequate feedback on how the stakeholder's inputs have been used; and
- is unnecessary and overly burdensome and therefore results in consultation fatigue.

A process that ensures that there is consultation on important issues and in a manner that is accessible and provides feedback, without resulting in consultation fatigue, is required.

There have been some initiatives in Australia to improve the consultation process. In Queensland, for example, interactive consultation websites have been developed, allowing the public to provide input into regulatory proposals directly to the agency involved.[112]

The Productivity Commission has highlighted, however, that generally there is a lack of information about how and when members of the community can provide input to the consultation process, which can frustrate stakeholders. Not all methods are available for all stakeholders (e.g. the Internet) and stakeholders may not have been informed that their input is required if they do not regularly monitor agency websites.

A problem associated with consultation that has been experienced in countries like Canada that have good consultation practices, is consultation fatigue, resulting from stakeholders becoming exhausted and feeling that their input is not valued. The Productivity Commission has found that consultation fatigue can occur where stakeholders feel overwhelmed by requests for input.[113] Accordingly, consultation should include strategies to:[114]

- reduce the cost of participation (including the use of draft RISs);
- allow adequate periods for responses; and
- generate confidence that feedback will be taken into account.

Consultation fatigue can be countered in part by having regulatory policy-makers pose specific questions, as well as providing additional explanatory and analytical information such as regulatory impact analysis to help focus the review.[115]

In the UK, all consultation documents, including RISs are published on departmental websites and at www.ukonline.gov.uk. In addition, the SBS operates *Direct Access Government for Business*, a web gateway that includes all consultations about regulations affecting small business.[116]

Setting up test panels for consultation can ensure that consultation is conducted cost-effectively, in a timely and targeted manner and in a way that provides feedback to the stakeholders (see Exhibit 12).

Whom to consult

Appropriate stakeholders are sometimes not identified or adequately consulted in the consultation process. The Government should determine a consultation period (discussed below) sufficient for stakeholders to respond.

A combination of passive methods, such as notice and comment, and active methods, such as advisory groups, will ensure a wide range of interests are consulted. Advisory groups can be ad hoc or permanent, although there are advantages and disadvantages to both forms. In respect of ad hoc advisory bodies set up in the consultation process, the OECD has warned that:[117]

> 'Permanent advisory bodies are likely to be more transparent because their role in the decision process is clear and predictable and their membership known. Matching this level of transparency where ad hoc bodies are used requires the adoption of clear general guidelines for their use. Permanent advisory bodies are also better placed to provide consistent and informed advice over the long term. Importantly their membership is less vulnerable to manipulation by regulators to produce preferred answers on specific issues.'

One method that may prove useful is to set up test panels for consultation, that is, permanent bodies with a broad cross-section of representation, but with a rotating membership to avoid consultation fatigue. Various forms of test panels have been set up in several OECD jurisdictions, including business test panels in Denmark.

The EU model (see Exhibit 12) requires that notice be given to industry bodies prior to the consultation, ensuring that they are aware their input is being sought. Setting up industry bodies specifically for the purpose of consultation, as well as setting up a procedure for consultation (e.g. via the Internet and with specific designated responsible parties) may be one method of overcoming the problems associated with ad hoc procedures and consultation fatigue.

EXHIBIT 12: EUROPEAN BUSINESS TEST PANEL (EBTP)

In the EU, the EBTP is made up of business members. Membership is voluntary and lasts initially for three years. One third of the membership is rotated every year, beginning in the fourth year of operation of the EBTP. Internet consultations are conducted between six and eight times a year and may include specific and general questions that impact business. The contact person responsible for completing the questionnaire consults within their own organisation. The results, and how they were used or influenced the regulation-making, are published to ensure transparency (but with a password for the participants so that the wider public cannot view the results). The final results are published more widely. Notice of a forthcoming consultation is given by email at least 10 days before the questionnaire is accessible online. A minimum of ten days is given for completion of the questionnaire, but for complex consultations, a longer period may be given.

Source: http://europa.eu.int/yourvoice/ebtp.

How long to consult for

The UK has produced a *Code of Conduct for Written Consultation*, which gives regulators guidance on consultation. Included in the code is a recommendation for a 12-week consultation period. In Victoria, the Victorian Competition and Efficiency Commission has recommended that a 60-day consultation period be adopted where possible, because:[118]

> 'Failure to give stakeholders time to provide adequate feedback on RISs would contribute to recurrent problems by, for example, increasing concerns about fairness and effectiveness of regulation and reducing the scope to use stakeholder feedback to identify the cumulative impact of regulation.'

The *Victorian Guide to Regulation* includes a 60-day recommended consultation period (see Exhibit 14).

The Commonwealth Government should adopt a similar standard for consultation periods and provide similar guidance on timing and the conduct of consultation to the regulators.

EXHIBIT 13: CLAYTON'S CONSULTATION – THE CLERP 9 EXPERIENCE

The years 2000 and 2001 saw a number of spectacular corporate collapses and near-collapses, with companies such as Enron and WorldCom in the US and Harris Scarfe, One.Tel, Pasminco, HIH and Ansett in Australia.

The Commonwealth Government responded initially with the HIH Royal Commission and an inquiry into company auditors (the Ramsey Inquiry). Then, in June 2002, the Treasurer announced a more wide-ranging proposal to examine and legislate on audit and disclosure issues (to become known as the 'CLERP 9' legislation).

In September 2002, the Treasurer released a 200-page 'proposals paper' setting out complex potential changes to the Corporations Act. The paper was available for public comment until November, although during this time and subsequently the Government made it clear that many of the proposals in the paper were 'not negotiable'. While the Government sought input on the proposals on the one hand, it was clear on the other that the effort invested by business and professional groups and others would have little effect on the Government's decisions.

The original timetable announced by the Government was for exposure draft legislation to be released for public comment by December 2002. In fact, the draft legislation was not released until October 2003, nearly a year after the initial consultation process. In the meantime, the ASX had changed its Listing Rules and had established the ASX Corporate Governance Council, which had finalised and released its *Principles of Good Corporate Governance and Best Practice Recommendations*. These went a considerable way towards addressing the issues raised by the corporate collapses. The Australian Law Reform Commission had also recommended against key proposals in the CLERP 9 proposals paper.

The draft CLERP 9 legislation was released for public comment in October 2003. The draft Bill was 220 pages long and accompanied by 148 pages of commentary covering complex areas and interactions of corporate law. Those wishing to understand the implications of the proposed legislative changes and to comment on them were given one month in which to respond.

CONTINUED >

EXHIBIT 13: CLAYTON'S CONSULTATION – THE CLERP 9 EXPERIENCE continued

Despite a number of practical concerns being raised with the proposed Bill, the Government made only minor amendments before the Bill was introduced into Parliament a mere three weeks after the public consultation process closed.

The CLERP 9 Bill was subject to Parliamentary inquiry and debate and was passed in its final form only a week before it came into effect.

The CLERP 9 legislation dealt with very complex areas of corporate law. Many of the changes proposed interacted with other areas of the law and careful examination was needed to ensure that, in practical terms, the proposed changes would have their intended effect. The Government required a year to develop this complex legislation, but allowed only a month to those having to implement and comply with the regulation to understand its impact and consequences.

The BCA understands the political imperative the Government faced to act on corporate collapses and has publicly applauded the Government for not adopting the highly prescriptive approach to these issues taken in the US through the Sarbanes-Oxley Act. The process for developing CLERP 9 was, however, flawed – and flawed processes produce flawed regulation.

EXHIBIT 14: VICTORIAN RECOMMENDATION ON CONSULTATION TIMEFRAMES

The *Victorian Guide to Regulation* provides as follows:

'Under the Act, there is to be a minimum 28-day period from the publication of the notice about the availability of the RIS to the receipt of public comments and submissions. However, where feasible, a longer time period for public submissions is encouraged as part of the Victorian Government's pursuit of a best practice regulatory regime. To this end, a consultation period of at least 60 days is recommended wherever timelines allow.'

Source: Victorian Government, *Victorian Guide to Regulation*, February 2005, pp. 4–20 to 4–21.

When to consult

Those carrying out consultation need to plan for it early in the policy development process and make sure that meaningful information is available for stakeholders. *A Guide to Regulation* stipulates that, in preparing an RIS for regulation that affects business, consultation should take place early with groups likely to be affected by the options. However, as stated above, the actual experience is that consultation rarely occurs and when it does, it occurs too late in the process. The Productivity Commission reports that:[119]

> 'Short time frames within which policy developers are directed to put forward regulatory proposals are often the main cause of inadequate consultation. Overly short consultation periods or consultation undertaken at inappropriate times can be counterproductive. It is particularly difficult for poorly resourced representative organisations and those that need to contact their membership before developing their responses'.

4.3.10 Apply the RIS process to existing as well as new regulation

The disciplines of the RIS process, including consultation and proper cost-benefit analysis, should be applied to reviews of existing legislation, as well as to the development of new regulation (see Section 5).

4.4 | MINIMUM REFORMS REQUIRED

The BCA believes that significant improvements are needed to the Commonwealth regulatory impact statement process to ensure that Government, and the wider community, are fully informed of the expected costs and benefits of regulation before a decision to regulate is made.

As a minimum, the key improvements needed include:

- Legislating the requirement to produce a regulatory impact statement for all regulatory proposals likely to have a significant impact on business.
- Requiring the Minister proposing new business regulation to personally certify that the benefits of the regulation will outweigh the costs.
- Introducing a two-stage impact assessment process, with all regulations likely to affect business subject to a preliminary assessment, and all regulations likely to have significant impacts on business subject to a full assessment.
- Requiring the release of draft regulatory impact statements for public comment and allowing sufficient time for consultation to make that consultation meaningful.
- Developing a standardised, sophisticated methodology for identifying and measuring the likely costs to business of proposed regulations.

5 Improving the Quality of Existing Regulations (Requirement Three)

Once reforms have been made to when and how new regulation is imposed, the new structures and processes can be used to review existing business regulation. In particular, all business regulation needs to be tested against criteria such as:

- Is the regulation still needed?
- How will the market respond if the regulation is removed?
- Are there more cost-effective ways of achieving the desired policy outcome?

When existing regulation is reviewed, it needs to be reviewed from the perspective of those affected by the regulation, not just from the Government's policy perspective. Priorities also need to be set, targeting in particular those regulations that restrict competition and business innovation or where there is a clear mismatch between the benefits of the regulation and the costs it imposes.

The BCA therefore recommends that one of the first tasks for the proposed Business Regulation Advisory Council should be to identify priority areas where regulation can be removed or significantly improved.

Notes

1 For example, presentation by C. Cordova-Novion, Regulatory Reform, OECD, *Simple, Effective, Transparent Regulation: Best Practices in OECD countries*.

2 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. XVII.

3 The principal sources are (i) OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*; (ii) OECD reviews of the regulatory governance frameworks in selected OECD countries; (iii) Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series; and (iv) Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003.

4 The requirements having been highlighted in the work of the OECD. See, for example, presentation by C. Cordova-Novion, Regulatory Reform, OECD, *Simple, Effective, Transparent Regulation: Best Practices in OECD countries*.

5 OECD (1997), *The OECD Report on Regulatory Reform: Synthesis*, Paris, p. 6.

6 Productivity Commission, *Regulation and its Review 2001–02*, Annual Report Series, pp. XII–XIII.

7 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 120.

8 For example, presentation by C. Cordova-Novion, Regulatory Reform, *Simple, Effective, Transparent Regulation: Best Practices in OECD countries*.

9 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 1.

10 ibid.

11 ibid., p. 37.

12 ibid., p. 28.

13 ibid., pp. 27–8.

14 ibid., pp. 33–6.

15 OECD (1997), *The OECD Report on Regulatory Reform*: *Synthesis*, Paris, p. 29; OECD (2002), *Regulatory Reform in Canada*, p. 23.

16 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, pp. 89–90.

17 ibid., p 84.

18 ibid., p. 87.

19 ibid.

20 ibid.

21 ibid., p. 89.

22 OECD (1999), *Regulatory Reform in the Netherlands*, p. 38.

23 OECD (1999), *Regulatory Reform in the Netherlands*, p. 13.

24 ibid.

25 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 89.

26 ibid.

27 ibid.

28 OECD (2002), *Regulatory Reform in the United Kingdom*, p. 17.

29 UK (2004) Budget Report, April 2004, para 3.55, p. 60.

30 OECD (1997), *The OECD Report on Regulatory Reform*: *Synthesis*, Paris, p. 2.

31 UK (2004) Budget Report, April 2004, para 3.55, p. 60.

32 OECD (2002), *Regulatory Reform in the United Kingdom*, p. 17.

33 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 90.

34 Victorian Competition and Efficiency Commission, *Regulation and Regional Victoria Challenges and Opportunities*, Draft Report January 2005, p. 23.

35 ibid.

36 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 90.

37 Victorian Competition and Efficiency Commission, *Regulation and Regional Victoria Challenges and Opportunities*, Draft Report January 2005, p. 23.

38 ibid., p. 261.

39 ibid., p. 262.

40 ibid.

41 ibid., pp. 262–3.

42 OECD (1999), *Regulatory Reform in the United States*, p. 38. The OECD recommendations refer to the Australian Small Business Deregulation Task Force, the Netherlands system of high-level commissions and task forces and the UK BRTF.

43 OECD (1999), *Regulatory Reform in the United States*, p. 19.

44 OECD (2002), *Regulatory Reform in the United Kingdom*, p. 19.

45 ibid.

46 ibid.

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48 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 48.

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55 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 8.

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62 Victorian Guide to Regulation incorporating: Guidelines Made under the *Subordinate Legislation Act* 1994, February 2005, Part 4.3.5, pp. 4–25; Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 52.

63 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 51.

64 ibid., p. 52.

65 ibid., p. 55.

66 ibid., p. 56.

67 ibid., p. 26.

68 ibid., p. 54.

69 ibid.

70 OECD (1999), *Regulatory Reform in the United States*, p. 12.

71 OECD (2002), *OECD Reviews of Regulatory Reform, Regulatory Reform in Canada*, p. 12.

72 ORR (1998), *A Guide to Regulation*, pp. C1–C3.

73 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 5; p. XV.

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75 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 60.

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85 ORR (1998), *A Guide to Regulation* p. D.19; Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 61.

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87 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, pp. 61, 66.

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92 ibid., p. 101.

93 ORR (1998), *A Guide to Regulation*, p. A.5.

94 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. XVI.

95 ORR (1998), *A Guide to Regulation*, p. A.5.

96 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 26.

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101 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 65.

102 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 13.

103 ibid., p. 9.

104 OECD (2001), *Regulatory Reform in Italy*, p. 31.

105 ORR (1998), *A Guide to Regulation*, p. A.5.

106 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 27.

107 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 30.

108 ibid.

109 OECD (1999), *Regulatory Reform in the United States*, p. 38.

110 ibid.

111 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, pp. 36–7.

112 ibid., p. 34.

113 Productivity Commission, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Staff Working Paper, S. Argy and M. Johnson, July 2003, p. 92.

114 ibid.

115 OECD (2002), *OECD Review of Regulatory Reform: Regulatory Policies in OECD Countries: From Intervention to Regulatory Governance*, OECD, Paris, p. 161.

116 ibid.

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118 Victorian Competition and Efficiency Commission, *Regulation and Regional Victoria Challenges and Opportunities*, Draft Report January 2005, p. 234.

119 Productivity Commission, *Regulation and its Review 2003–04*, Annual Report Series, p. 35.

Appendix 2

BENEFITS & COSTS OF

Regulation

Report by Access Economics Pty Limited
for **The Business Council of Australia**

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THE HOW AND WHY OF REGULATION – AND ITS RISKS

> "The [NSW] Government also accepts that the planning system is a regulatory disaster, beset by duplication and obfuscation. The Department of Planning's own fact sheet admits the system is 'bogged down in complex rules and process'. There are 5,500 local planning instruments in use across the state's 152 councils, as well as 3,100 zones and 1,700 definitions of parks, hospitals and roads."
>
> **David Poole,** *Sydney Morning Herald,* **3 December 2004**

Why regulate? Because sometimes we can use rules to reduce risks such as cheating, stealing or overcharging. As the Productivity Commission notes, "Regulation serves a vital role in improving social, environmental and economic standards for Australians. At their most fundamental level, laws — merely a form of regulation — define and enforce property rights, which are the basis for economic exchange. There are also other persuasive rationales for regulation based on the failings of the market. Uninhibited markets can produce undesirable outcomes, such as environmental degradation, unnecessary health hazards, excessive prices and 'unfairness'. By shaping incentives and influencing how people behave and interact, regulation can help societies deal with otherwise intractable problems. At their best, regulations create order, preserve norms and provide a basis for stable progress."

But what are the risks? (1) Advocates of regulation tend to exaggerate market failure and underestimate the ability of markets to solve problems without regulation, or with less heavy-handed regulation. There is no guarantee a regulator will achieve a better outcome than markets. (2) Advocates of regulation tend to understate its costs. Aside from obvious direct costs to business, the government and the economy, many costs of regulation are indirect, or arise from the failure of regulation to keep pace with the times. And (3) regulation often creates big winners (often vocal interest groups) and many small losers (ordinary Australians unaware of the costs of regulation). That produces the wrong incentives, and runs the risk that regulation is merely the easy 'solution' with the lowest political cost. Such risks are high when politicians need a quick fix to get a crisis off the front page. Indeed, many studies note that regulation often ends up hurting both consumers and businesses by taking decisions away from them and leaving power in the hands of bureaucrats.

How deep does regulation run? No-one knows how many regulations have been imposed on Australians – we don't even know how many regulatory bodies there are in Australia. But we do know the flow of new regulation is rising, and we can safely say that many thousands of regulations imposed by different jurisdictions are in force at one time. For example, a dozen pieces of regulation and over 200 pages of documentation can be required to open a business bank account. Yet despite the enormous and growing stock of regulations in place, ignorance is no excuse – the onus is on each individual business to locate, digest and comply with all of the regulations that are imposed on it. That is an almost impossible task.

THE COST OF REGULATION

How much does regulation cost us? The costs are often subtle and well hidden – there is (1) the burden on taxpayers to finance the cost to governments of *administering* regulations, (2) the cost to businesses in *complying* with these regulations; and (3) higher prices and lower wages resulting from the *efficiency losses* induced by regulation.

These are hard to measure, but the Productivity Commission identified at least $4.5 billion in *administration* costs paid by taxpayers just to run Federal regulatory bodies in 2001-02. And the most detailed overseas model finds that a fifth of all administration costs borne by business are caused solely by *compliance* responsibilities. (The OECD estimated direct compliance costs of more than $17 billion in 1998 for small and medium sized Australian businesses alone.)

The *efficiency* losses are more difficult still to measure, but are likely to be the largest of all. An indirect yardstick of the current burden of regulation on Australian prosperity comes from estimates of the efficiency gains from two decades of deregulation and reform. An Access Economics study has estimated these at 10.8% of GDP, while the likes of the Productivity Commission, the Melbourne Institute and others have estimated smaller efficiency gains from individual reforms (such as national competition policy or tax reform).

A different yardstick of efficiency costs is provided by a World Bank study of regulatory reach across 137 nations. It found those nations that regulate lightly (but protect property rights) grow faster than others. That finding suggests the deadweight efficiency losses to Australia of our less than best practice regulatory record is likely to be costing us dearly.

So why aren't we more worried? Australians lack a sense of urgency about the troubles we are piling up. It seems good times have lulled people, businesses and governments into a false sense of security regarding the reach, complexity and cost of regulation. Fourteen years of good growth (moving us from 15th to 8th in income per head terms within the OECD) may have led Australians to be more accepting of regulatory costs. So it is ironic that today's good times are partly attributable to our strong record of deregulation over the past twenty years. Governments of all stripes, State and Federal, deregulated money and foreign exchange markets, addressed national competition policy and began to wind back the centralised regulation of labour markets. That process of deregulation has helped to turn Australia into a prosperous nation. But these good times have also allowed policymakers greater scope to respond to policy (or political) problems with often less-than-carefully-tested regulatory responses.

THE MISTAKES WE ARE MAKING

What mistakes are Australian regulators making? They suffer from:

(A) Regulatory over-reach – Regulators and regulations often aim at achieving more than the achievable, meaning worse outcomes than deregulated markets would give. That can arise if regulators:

1. Overestimate their ability to get better outcomes than the market.
2. Are overly-prescriptive in regulation.
3. Overreact to current hot issues.
4. Cannot enforce their rules.

The Financial Services Reform Act and Uniform Credit Code are good examples. And regulators often regulate symptoms rather than causes, or try to fix one problem by regulating another area (an almost always guaranteed disaster, such as the nightmare compliance issues spawned by exempting fresh food from the GST – the aim was to help the poor, but that should have been done directly via welfare and taxes, not via bad regulation).

(B) Letting regulations overlap – Regulations pile atop other regulations, so that even if a single regulation on its own has net benefits, there is a risk that the sum of the net costs of all regulations is rather greater than their parts. Overlapping or conflicting regulation can

occur between different regulatory bodies at the same level of government, or different governments, or between public and private oversight bodies. Such 'regulatory cocktails' often create compliance disasters which regulators let lie with consumers and businesses.

(C) Not listening – Regulators sometimes meet with business but do not listen. Again the Financial Services Reform Act is a good example. That's a mistake: industry has an incentive to ensure regulation has low compliance costs, and enforcing compliance is easier where the regulator has consulted with industry.

(D) Not looking back – There are likely to be many regulations in force which may have been valid a decade ago, but have now passed their shelf-life. Regulations can become outdated or less cost-effective than alternatives (or deregulation). And as we learn more about the economy and markets, new and more effective ways of regulating arise. Yet there is little by way of official arrangements to ensure that the good regulation of the past doesn't evolve into the bad regulation of today.

OUR PROCESSES ARE FLAWED

Why are bad regulations still getting passed? Economists agree on the need for a light regulatory touch, yet the total stock of Australian regulation continues to climb. Why? Because the Office of Regulation Review (ORR) – the last line of defence between the Australian public and bad regulation – is being ignored, side stepped and overruled.

Despite the rising flow of new regulation, scrutiny of it by ORR is falling – just 7% of new Federal regulations were assessed in 2003-04. Miraculously, more than 90% of all such assessments were deemed 'adequate', and on only 9 (out of 105) occasions in 2003-04 did the preparation of a Regulatory Impact Statement (RIS) affect the nature of the subsequent regulation. And, mysteriously, the frequency with which ORR says a regulatory risk assessment is required has been steadily falling, halving in the past five years. Yet these trends should come as no surprise – the Federal system is flawed as the bureaucrat in favour of a regulation also assesses its impact, albeit 'in consultation with the ORR'.

THE RIGHT APPROACH

The consensus among economists is that regulation is best used to lay down the basic ground rules of society and the economy.

For years now think tanks such as the Fraser Institute and the Heritage Foundation have pointed to close links between regulation and national income – prosperity is higher where regulation is less heavy, and grows faster after deregulation. Now the World Bank has concluded that countries that have performed well have five common elements to their approach to regulation – they consistently:

1. Protect property rights with simple and clear rules.
2. But they otherwise regulate lightly – and deregulate in existing markets.
3. They use new technologies to reduce compliance costs to business.
4. They minimise recourse to lawyers and the courts.
5. And they never pretend that the task of deregulation is finished.

Access Economics
May 2005

1. THE WHY AND HOW OF REGULATION

What is regulation? How is it imposed? What benefits can regulation bring? What are its costs? Given those benefits and costs, what is 'good regulation' and 'bad regulation'? And what are the politics of regulation?

This chapter sorts through these basic issues. It finds that regulation – the rules we set ourselves – reaches deeply into our daily lives in many ways.

Yet the costs which regulations impose are often subtle and hidden (as higher prices, higher taxes and lower wages), while beneficiaries of regulation tend to be well aware they are on a good thing. And that combination of **some big winners** (typically vocal interest groups) and **many small losers** (ordinary Australians unaware of the costs of regulation) gives the wrong incentives to politicians.

As a result, regulation can often be imposed on an unsuspecting public as the easy 'solution' with the lowest political cost (or maximum political benefit), rather than the best policy option overall. Such risks are highest when politicians are in need of a quick fix – typically, when they announce new rules to get a particular crisis off the front page, but such rules can have many unintended consequences.

Indeed, many studies note that regulation often ends up hurting both consumers and businesses by taking decisions away from them and leaving power in the hands of bureaucrats.

So what is the right regulatory approach? The World Bank studied the regulatory practices of 137 nations in depth. It found that successful nations have five common elements to their approach to regulation:

1. **They protect property rights with simple and clear rules.**
2. **But they otherwise regulate lightly – and deregulate in existing markets.**
3. **They use new technologies to reduce compliance costs to business.**
4. **They minimise recourse to lawyers and the courts.**
5. **And they never pretend that the task of deregulation is finished.**

1.1 THE STRUCTURE OF THIS REPORT

Chapter 1 answers the basic questions – What is regulation? How is it imposed? What benefits can regulation bring? What are its costs? Given those costs and benefits, what is 'good regulation' and what is 'bad regulation'? And, what are the politics of regulation?

Chapter 2 then discusses regulatory costs in greater detail – the administrative, compliance and deadweight losses of Australian regulation, and gives examples of some less-than-optimal regulation.

Chapter 3 notes the importance of good regulatory processes, lays out the gaps between current and best practice.

And **Chapter 4** lays out what our regulators are doing wrong.

1.2 WHAT IS REGULATION?

Regulations are a way in which society sets rules for itself – everything from 'thou shalt not murder' to 'thou shalt not put cream on cakes baked for the school fete'.

Why impose rules on ourselves? Because there are times when having rules is better than not having them – when we want behaviour to differ from what it otherwise would be.

Regulation tends to respond to perceived risks of cheating, stealing or overcharging. And such risks are seen arising when markets fail, or when monopolies have market power, or when we want to 'improve' competition within deregulated markets, or when we want to achieve a degree of safety (or environmental protection, or degree of information given to consumers) that deregulated markets would not otherwise provide.

Regulation runs deeper than most of us realise. The rules and regulations we set for Australians continue to multiply at an impressive rate. As a result, and whether we realise it or not, the reach of regulations into our daily lives goes ever deeper. For example, Dudley[1] sets out *A Regulated Day in the Life* of an American family:

- It begins with the radio (broadcast over a regulated frequency on a licensed station),
- Continues at work (where minimum terms and conditions of employment are regulated), and
- Ends with dinner (where the packaging on food products is also regulated).

1.3 THE SCOPE OF THIS REPORT

Studies typically characterise regulations as either economic or social.

Economic regulations restrict conditions of entry or pricing decisions in a specific sector or industry, but also include tax, finance and investment policy, as well as regulations affecting day-to-day business operations.

Social regulations are enacted primarily for health, safety or environmental reasons. [2]

There is no clear dividing line between these two: a regulation which requires electricity generating companies to have an environment protection licence will affect who enters an industry (as the generator cannot operate without the licence) and prices (as the firm will incur costs to obtain and comply with licence conditions).

Moreover, the tests that delineate good regulation from bad can be equally applied to either economic or social regulation.

[1] Dudley, S (2004) 'A Regulated Day in the Life' *Regulation*, Summer 10-11.

[2] Office of Management & Budget (2004), *Informing Regulatory Decisions*: 2004 Draft Report to Congress on the Costs and Benefits of Federal Regulation and Unfunded Mandates on State, Local and Tribal Entities.

1.4 HOW IS REGULATION IMPOSED?

Rules can take many forms:

> *"These include, at the highest level, Acts of Parliament. They also include subordinate legislation, where the Parliament delegates powers to a Minister, board or organisation. But regulation can also include codes, instruments and standards which governments use to influence business behaviour, but which do not involve 'black letter' law (known as 'quasi regulation'). And of course there are also various international treaties which impact on business, either directly or indirectly."* [3]

1.5 THE BENEFITS AND COSTS OF REGULATION

Why is regulation imposed? Because it can often have notable net benefits. Gary Banks of the Productivity Commission lays out the potential benefits of regulation well:

> *"[R]egulation serves a vital role in improving social, environmental and economic standards for Australians. At their most fundamental level, laws — merely a form of regulation — define and enforce property rights, which are the basis for economic exchange. There are also other persuasive rationales for regulation based on the failings of the market. Uninhibited markets can produce undesirable outcomes, such as environmental degradation, unnecessary health hazards, excessive prices and 'unfairness'. By shaping incentives and influencing how people behave and interact, regulation can help societies deal with otherwise intractable problems. At their best, regulations create order, preserve norms and provide a basis for stable progress."* [4]

Australian society could not function without regulation. In particular, regulations which define property rights and the institutions which enforce them form the basis for economic transactions. Farmers would not work if others could simply remove what they wanted from their fields without paying. Similarly, land provides collateral for bank loans which facilitates lending to entrepreneurs wanting to start up new businesses and generate economic wealth. Increasing the number of such exchanges increases the welfare of Australians.

And what of costs? The following chapter examines the costs of regulation in detail. In brief, there are three types:

- costs to taxpayers (*administration*),
- costs to business (*compliance*), and
- costs to the economy (*efficiency* or *deadweight losses*).

[3] Banks, G (2003) *Reducing the business costs of regulation,* Address to the Small Business Coalition, Canberra, 20 March.

[4] Banks (2003) *The good, the bad and the ugly: economic perspectives on regulation in Australia*, Address to the Conference of Economists, Business Symposium, October, p1.

1.6 THE POLITICS OF REGULATION

Aside from its net economic costs and benefits, regulation has significant potential to impose costs and benefits on particular groups in society and to generate large transfers of wealth.

So regulation usually creates (some big) winners and (many small) losers. It therefore gives politicians some dangerous incentives.

There are political pressures from groups seeking to influence regulatory processes and outcomes. At their worst, political systems convert these pressures into corruption and graft. At best, competing interest group pressures reveal the strength of community feelings and help governments design better economic policy.

> A politician or regulator may be able to buy popularity or a quiet life by regulating to serve vocal interest groups, rather than society as a whole. So regulation can often be the 'solution' with the lowest political cost (or maximum political benefit), rather than the best policy option overall.

Regulators often have a range of options to address problems or implement policies. While some options may entail lower total costs for society, their costs might be concentrated on a small group. A second option may be preferred if it spreads larger costs over a bigger group, as its costs are less visible and so there is less political damage to the regulator / politician.

And regulators usually have regular contact with Ministers and decision makers, in contrast to bodies set up to monitor the regulatory burden (who are generally more on the sidelines). Without the broader community keeping regulatory burden at the forefront for Ministers and decision makers, it can quickly die down as an issue.

A further political consideration is that the implementation of regulation tends to occur far more smoothly than its subsequent removal – **we regulate in haste, and repent at leisure**. Sometimes whole industries develop around a given regulation (such as tax legislation), creating resistance to removal or reform. Hence, regulatory decisions can become political when a policy choice risks alienating political interest groups. The OECD notes:

> *"there is little doubt that most governments can substantially reduce regulatory costs, while increasing benefits, by making wiser regulatory decisions. A wide range of anecdotal and analytical evidence supports the conclusion that governments often regulate badly, with too little understanding of the consequences of their decisions, and with little or no assessment of any alternatives other than traditional forms of law and regulations."*[5]

1.7 WHEN SHOULD GOVERNMENTS REGULATE?

So when should governments regulate? There are three main theories.

The first is the oldest – the **public interest theory of regulation** points to market failure as the trigger for regulating, and suggests such failures are relatively common, particularly in developing economies. So Governments need to protect society (individuals or corporates)

[5] OECD (2002b), *OECD Review of Regulatory Reform*, p44.

from the 'law of the jungle' amid market failure – they (for example) regulate who can enter a market, the quality of the products sold and, where there are monopolies, the prices charged.

Yet critics argue this theory overstates the frequency of market failure, and underestimates the ability of competition (or the threat of competitive entry) to ensure good behaviour. As the World Bank notes: "For example, competition for labor ensures that employers provide good working conditions for employees. If an employer failed to do so, competitors would offer better packages and attract workers. Similarly, private markets ensure efficient safety levels in a variety of products and services, such as food, houses, and cars. Sellers who fail to deliver those levels lose market share to competitors who sell unspoiled food, build safer houses, or produce safer cars. [Indeed], the data show that stricter entry regulation is not associated with better consumer protection." [6]

The second, the **contracting theory of regulation**, takes a different tack. It argues regulation is less necessary than the public interest theory would suggest because there are other ways to ward off any risks associated with market failure. Notably, contracts can specify risks and their outcomes via guarantees, collateral and the like, and the courts can adjudicate.

The **capture theory of regulation** takes issue with the underlying assumption in the public interest theory that governments are benevolent, effective, well informed and always ready to update their past regulatory moves in response to new developments. To quote the World Bank again: "First, incumbent business interests typically capture the process of regulation. Regulation not only fails to counter monopoly pricing—it sustains it. Second, even where regulators try to promote social welfare, they lack the capacity to do so, and regulation makes things even worse. Empirical evidence provides support for this conclusion. Bureaucratic entry is associated with more corruption, and heavy regulation of court procedures leads to less impartiality and longer delays." [7]

The latter two theories were developed after the first. It is perhaps no coincidence then that they are more sceptical about the success of government regulations compared with market outcomes.

1.8 WHAT CONSTITUTES GOOD REGULATION?

So what constitutes good regulation? Economists agree that regulation is better if applied in some areas and worse in others. **The consensus among economists is that regulation is used best to lay down the basic ground rules of society and the economy.** In particular, as the World Bank put it, "Heavier regulation of business activity generally brings bad outcomes, while clearly defined and well-protected property rights enhance prosperity."

Nations with regulations that define and protect property rights (such as bankruptcy creditor rights and efficient court processes to enforce contracts) achieve better economic and social outcomes. [8] This is true comparing both developed and developing nations with their peers.

And the consensus among economists is that, outside of protecting property rights, regulation should be imposed with the lightest possible touch. For years now private

[6] World Bank, *Doing Business in 2004*, at page 91.

[7] World Bank, *Doing Business in 2004*, at page 91.

[8] World Bank, *Doing Business in 2004*, at page 88.

think tanks such as the Fraser Institute and the Heritage Foundation have pointed to close links between the degree of regulation and national income – noting that national income was higher where the hand of regulation was less heavy, and grew faster after deregulation. And now the public sector has launched its own studies, with the World Bank conducting the most detailed cross-country analysis of regulation and its effects ever attempted.

Indeed, many studies note that regulation often ends up hurting both consumers and businesses by taking decisions away from them and leaving power in the hands of bureaucrats.

Regulation has a role in some cases of market failure, but it is not always the best answer, and the risks of overlapping regulations are higher than generally recognised. Regulations often overlap, so interaction between regulations must be watched, particularly if different regulators (often different levels of government) legislate across similar areas.

That suggests regulation should be limited to cases where it is the best and least costly way to achieve the desired policy outcome. The aggregate burden on individual firms can end up being prohibitively large, and quite possibly greater than the sum of the separate impacts if the regulations enforced by different bodies conflict with one another.

So good regulation should:

1. consider both direct and indirect costs to the economy,
2. result in a net benefit through efficiency gains,
3. consider the potential implications of overlap with other regulations,
4. not reflect the interests of policymakers or special interest groups, and
5. be the outcome of good processes (as good regulatory processes encourage good regulatory policy).

1.9 'WORLD'S BEST REGULATORY PRACTICE'

The World Bank is now releasing results from a large and on-going study of its membership and the manner in which nations are regulating themselves.

The study considers the regulatory practices of 137 countries.

The Bank concludes that the most economically successful nations consistently:

1. **Simplify and deregulate in competitive markets.** The message is simple – let the market do the heavy lifting. And stop believing that bureaucrats do it better. "Where there is enough competition in business and in labour markets, markets would be enhanced if fewer regulations were imposed on the participants."

2. **Focus on enhancing property rights.** There is evidence that governments do too little to protect property rights. The best-practice countries build efficient courts and support laws and institutions that define the rights of citizens and businesses to their property. The resultant better protection of property rights benefits everyone, but especially the poor.

3. **Expand the use of technology.** Appropriate use of technology improves efficiency, increases the availability of information, and reduces opportunities for bureaucratic discretion. In the best-practice countries, modern technology minimises the compliance burden on business. And in high tech regulatory environments, entrepreneurs never have to face a bureaucrat, so there are fewer opportunities to play favourites.

4. Reduce court involvement in business matters. Regulations are rules. Where those rules are simple, clear, and well enforced, there will typically be less need for recourse to lawyers in general, and the courts in particular. Legal processes are expensive. The Bank notes the role of courts can be reduced by introducing summary procedures for commercial disputes, thereby limiting the time for judgment.

5. Make reform a continuous process. Don't rest on your laurels. Continuous reforms require political will, but not necessarily large resources. Indeed, if properly implemented, deregulation can save the government money it can otherwise spend elsewhere.

Consistent with those five principles, and as spelt out in the following charts, the World Bank's study found that more regulation:

FIGURE 1.1: LEADS TO LOWER PRODUCTIVITY AND SO TO LOWER PER CAPITA INCOMES

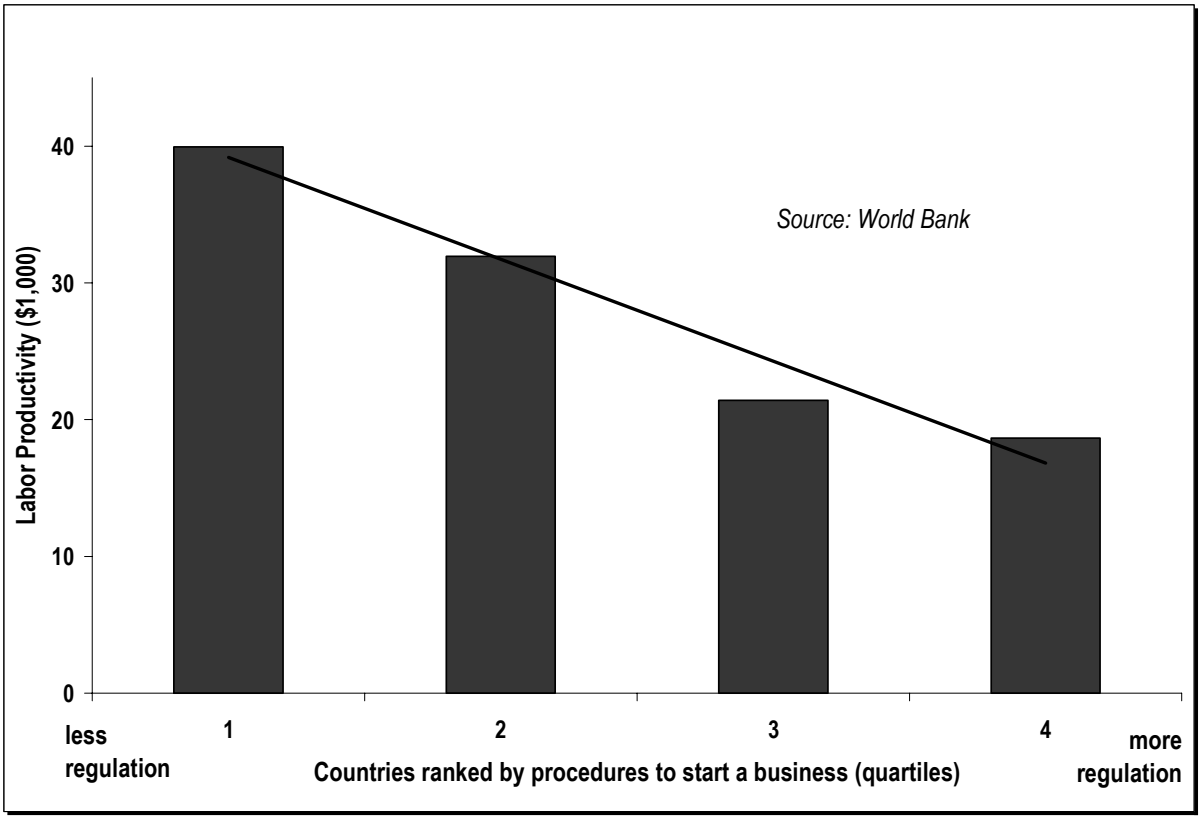


FIGURE 1.2: IS ASSOCIATED WITH A LARGER BLACK ECONOMY

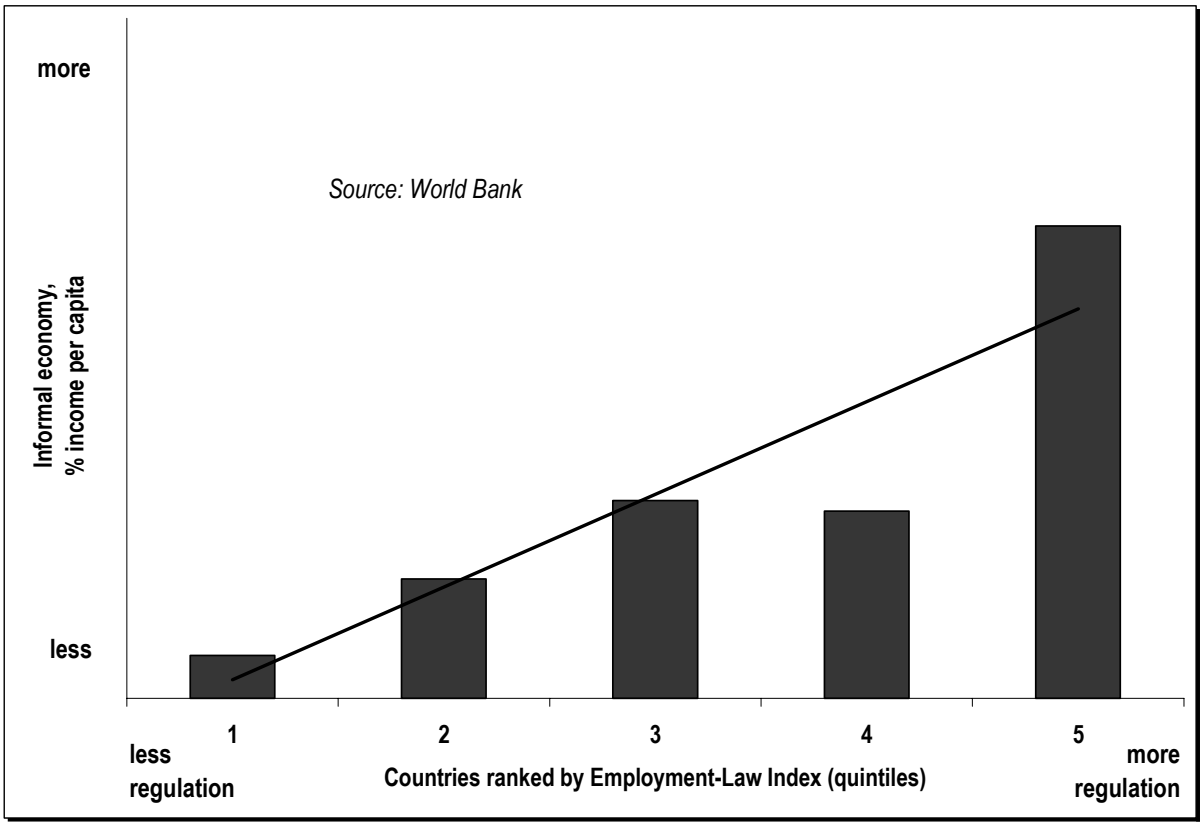


FIGURE 1.3: IS ASSOCIATED WITH MORE CORRUPTION

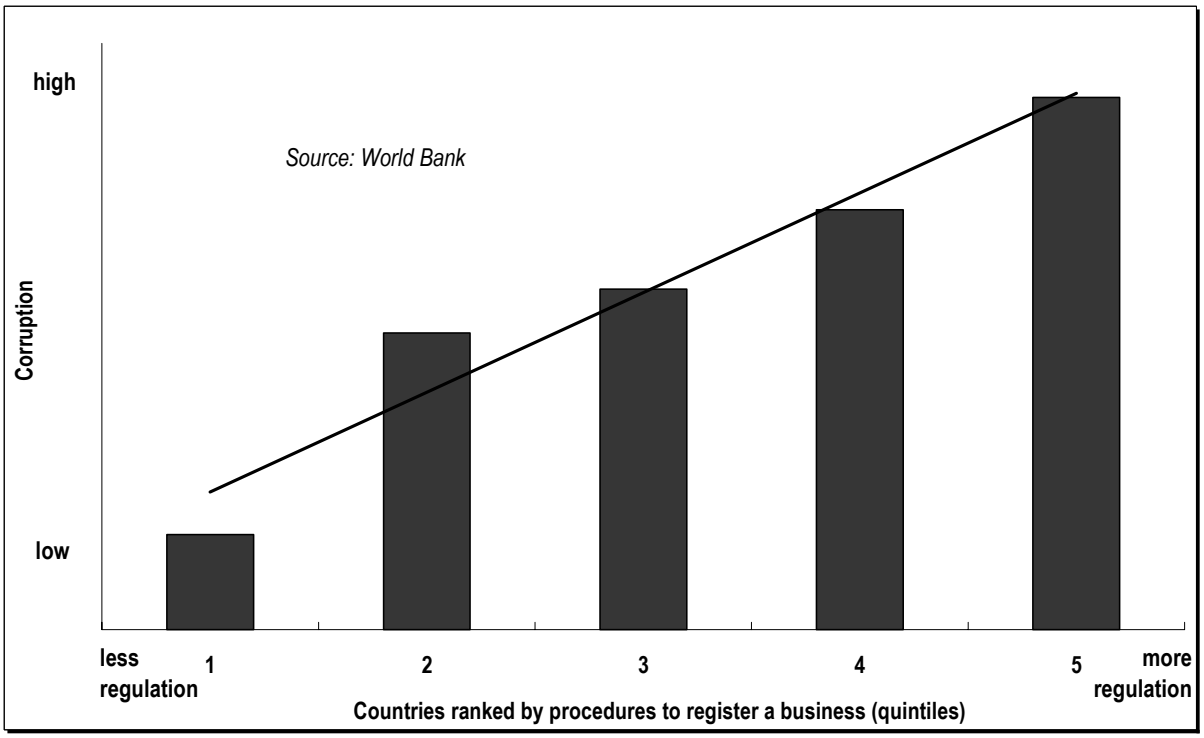


FIGURE 1.4: IS ASSOCIATED WITH MORE AND LONGER BUREAUCRATIC DELAYS

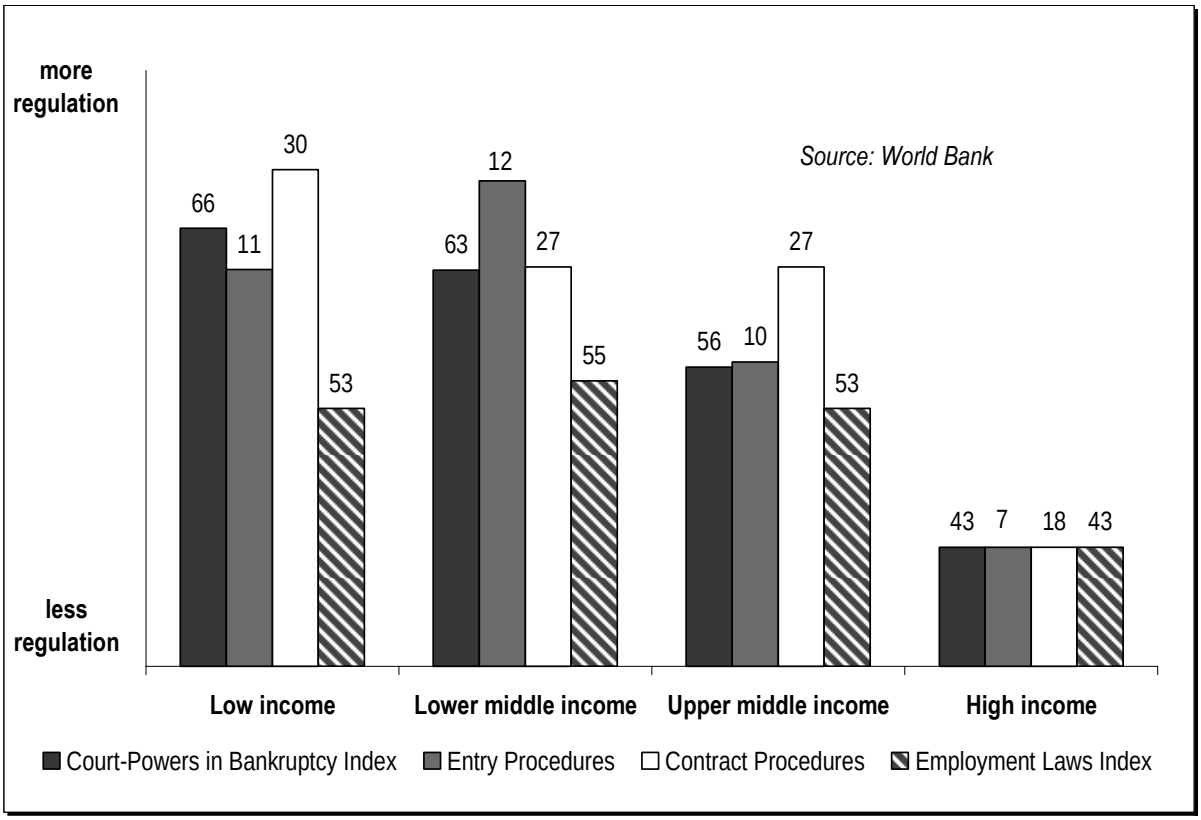
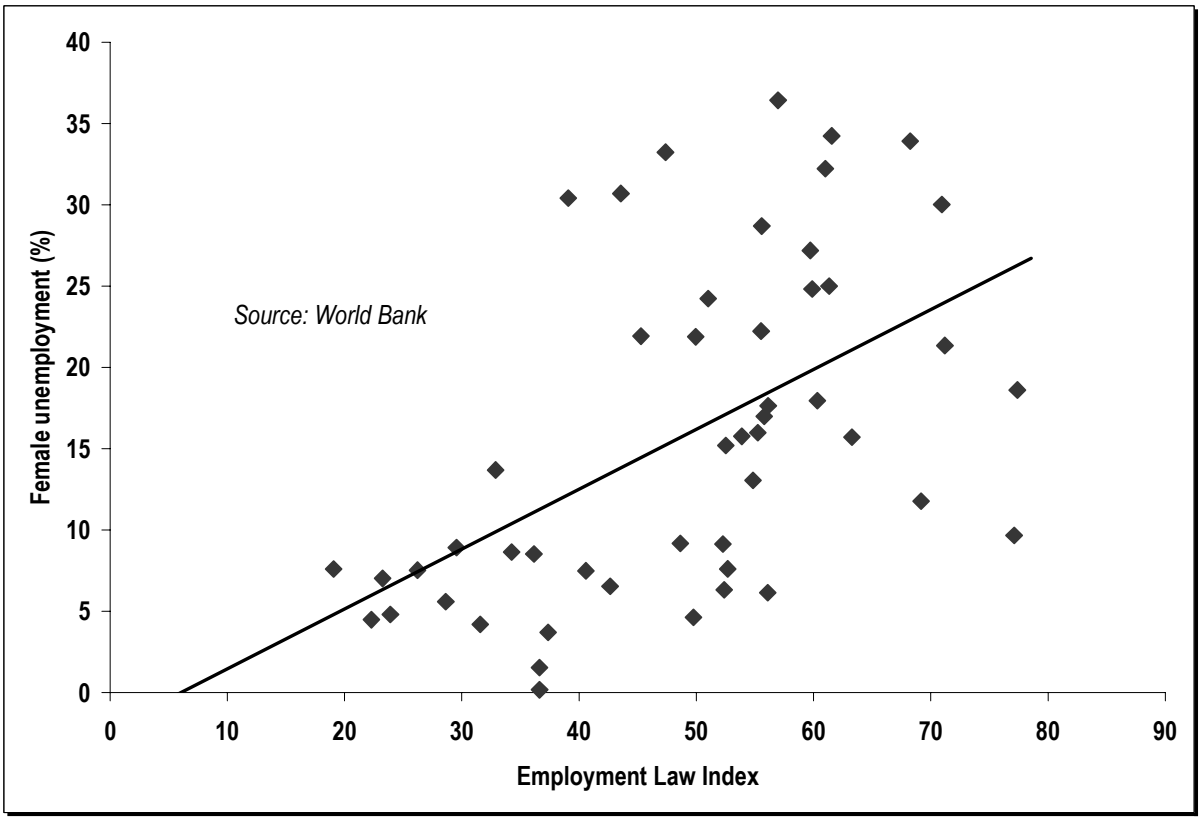


FIGURE 1.5: AND MEANS WORSE OUTCOMES FOR THOSE WITH LESS POWER



2. THE CURRENT COST OF REGULATION IN AUSTRALIA

How many regulations are imposed on Australians? No-one knows – we don't even know how many regulatory bodies there are in Australia. To the best of our knowledge there has never been a comprehensive inventory of the stock of regulation. But **we do know the flow of new regulation is rising**, and we can safely say many thousands of regulations imposed by different jurisdictions are in force at one time. For example, **a dozen pieces of regulation and up to 200 pages of documentation are required to open a business bank account.**

Yet despite the enormous and growing stock of regulations in place, ignorance is no excuse – **the onus is on each business to locate, digest and comply with all of the regulations that are relevant to it**. That is an almost impossible task.

So are we drowning in badly designed rules and regulations? That depends on the benefits and costs of individual regulations, and the overlaps between them. Yet **the costs of regulation are often subtle and well hidden**. There are three costs – the extra burden on taxpayers to finance the cost to governments of *administering* regulations, the cost burden on businesses in *complying* with these regulations, and the higher prices and lower wages resulting from the *efficiency losses* induced by regulation. These are hard to measure, but the Productivity Commission identified at least $4.5 billion in **administration** costs just to run Federal regulatory bodies in 2001-02. And the most detailed overseas model finds that a fifth of all administration costs borne by business are caused solely by **compliance** responsibilities. (The OECD estimated direct compliance costs of more than $17 billion in 1998 for small and medium sized Australian businesses alone.)

The **efficiency** losses are likely to be the largest. An indirect yardstick of the current burden of regulation on prosperity comes from estimates of the efficiency gains from two decades of deregulation and reform. **Access Economics has estimated these at 10.8% of GDP**, while the Productivity Commission, the Melbourne Institute and others have estimated smaller efficiency gains from individual reforms (such as national competition policy or tax reform).

A different yardstick of efficiency costs is provided by a World Bank study of regulatory reach across 137 nations. It found those nations that regulate lightly grow faster than others. That finding suggests the deadweight efficiency losses to Australia of our less than best practice regulatory record is likely to be costing us dearly.

Yet we lack a sense of urgency about the troubles piling up on our doorstep. It seems good times have lulled Australians (people, businesses and governments) regarding the reach, complexity and costs of regulation. Fourteen years of good growth (moving us from 15th to 8th in income per head terms within the OECD) may have led us to be more accepting of regulatory costs. So it is ironic today's good times are partly attributable to a strong record of deregulation over the past twenty years. Governments of all stripes, State and Federal, deregulated money and foreign exchange markets, addressed national competition policy and began to wind back the centralised regulation of labour markets. **That process of deregulation has helped to turn Australia into a prosperous nation today**.

2.1 STOCKTAKE OF THE AMOUNT OF REGULATION

How many regulations are imposed on Australians? No-one knows. The vast quantity of regulations in force at any one time across a multitude of industries, sectors and levels of government creates great difficulty in attempting a stocktake of the current regulatory burden.

Nobody even knows how many bodies can impose new regulations on Australians – let alone how many regulations there are. Most regulation occurs at the State and Territory level (though local councils are no slouches either). Yet at the Federal level alone: [9]

- There are around 60 departments and agencies responsible for making and/or administering regulations, along with another 40 Ministerial Councils and other standard setting bodies.
- **Unlike other nations, Australia has little idea of the total stock of Federal regulations***:* We have some idea of the *flow* of new Federal regulation. But no-one knows the *stock* of existing Federal regulation, because the likes of the Productivity Commission isn't asked to keep track of it. At least we do know that more than 1,800 Acts were in force at October 2003, including 170 new Acts passed in 2002, and that over 7,200 regulations were made between 1997-98 and 2001-02. But the total number of Commonwealth regulations currently in force is not yet known. [10]
- **And we have even less idea at the State level:** Most new red tape is enacted by the States and Territories, where the analysis of new regulation and understanding of the stock of existing legislation appears to be generally less thorough.

From the limited information available, it is clear that:

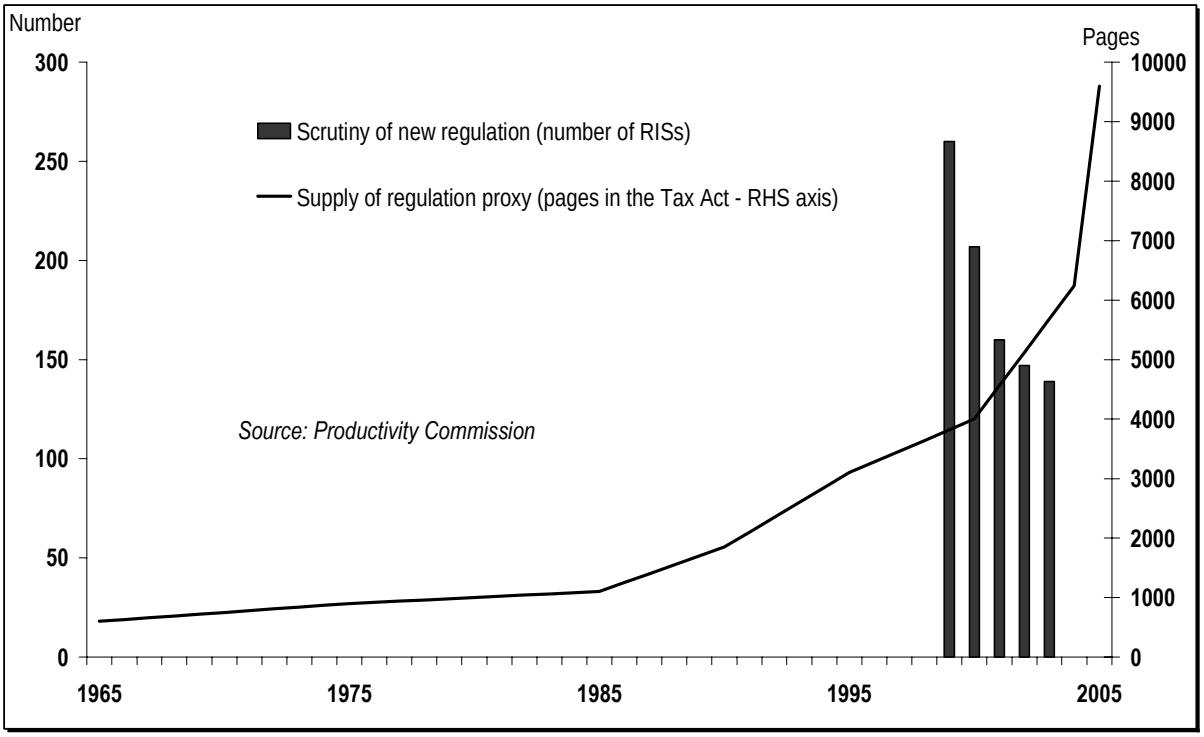
- *The burden of new regulation is rising:* New regulations are being introduced at a comparable pace to earlier years. The absolute stock of regulation is not known, but the number of pages of the Tax Act is often used as a convenient and readily observable proxy. Page length also operates as a useful proxy for complexity of regulation. The average length of a piece of legislation has doubled during the last decade.
- *Yet the scrutiny of it is falling:* The proportion of new Federal regulation subjected to analysis (any analysis, let alone well researched cost/benefit analysis on consistent principles and assumptions) is low and falling fast (half of what it was five years ago).

Figure 2.1 illustrates the problem – that the stock of regulation keeps rising, and getting more complex, but that the scrutiny of the flow of new regulation appears to be falling, and that the scrutiny of the stock of old regulation is almost non-existent.

[9] Banks, G (2003) *Reducing the business costs of regulation* Address to the Small Business Coalition, Canberra, 20 March and Banks (2003) *The good, the bad and the ugly: economic perspectives on regulation in Australia,* Address to the Conference of Economists, Business Symposium, October.

[10] The *Legislative Instruments Act (2003)* will require all departments and agencies to place new and existing regulations on a centrally-maintained register by the end of 2007.

FIGURE 2.1: STOCK OF REGULATION VERSUS THE SCRUTINY OF THE FLOW OF NEW REGULATION



The end result is frustrating. To the best of our knowledge, no one has published similar statistics covering the amount of regulation imposed by State and Territory and local government. That said, the NSW Parliamentary Counsel's Office lists over 1,300 Acts of NSW State Parliament, and more than 650 principal statutory instruments in force at 1 January 2005. [11] Some 115 Acts and 625 regulations (both major and minor) were imposed in 2004 alone, while just under 3,800 regulations and by-laws were imposed in the five years to 2004.

And that's probably just the tip of the iceberg

As noted in the *Sydney Morning Herald* on 3 December 2004, "The [NSW] Government also accepts that the planning system is a regulatory disaster, beset by duplication and obfuscation. The Department of Planning's own fact sheet admits the system is 'bogged down in complex rules and process'. There are 5,500 local planning instruments in use across the state's 152 councils, as well as 3,100 zones and 1,700 definitions of parks, hospitals and roads."

And a similar number of Acts and subordinate instruments are in force in Victoria. [12] The Victorian Competition and Efficiency Commission recently conducted an exhaustive study of that State's regulatory system. It identified 69 State-based business regulators who, as at November 2004, administered a combined total of 170 Acts of Parliament, totalling over

[11] NSW Parliamentary Counsel's Office (2005) *Legislation in Force* downloadable at http://www.pco.nsw.gov.au/nswleg.html

[12] Victorian Law Today Database, available at http://www.dms.dpc.vic.gov.au/Domino%5CWeb_Notes%5CLDMS%5CPubLawToday.nsf?OpenDatabase

19,600 pages. There were also 176 regulations associated with these Acts, amounting to a further 6,400 pages.[13]

Local Government laws are even more difficult to tally up. The Queensland Government estimates that Councils across Queensland have adopted around 3,000 local laws. [14] And the Business Licence Information Service includes entries for over 3,000 State and local government licences in South Australia, Tasmania and the Northern Territory. [15]

While it is difficult to estimate the volume of State and local Government regulation, these regulations may have a greater impact on the day to day operations and compliance costs of a business than the more widely known Federal laws. For example, submissions to the recent Senate Committee Inquiry into Small Business Employment [16] stated that a new development may require planning and environmental approval from each level of Government, all of which impose different standards. The problems of jurisdictional overlap also arise in other areas of business regulation, and can be compounded by functional overlap between regulations and regulators at each level of jurisdiction.

Firms that operate in more than one State or Territory will also need to meet the differing requirements of each jurisdiction, potentially increasing compliance costs. The problem of multiple regulatory arrangements is discussed in more detail in section 4.2 of this report. Similarly, Australian companies that also operate offshore may find costly differences between local and overseas regulation, such as the United States' Sarbanes-Oxley Act dealing with corporate governance.

Obviously, not every regulation will affect every firm. But businesses are not allowed the luxury of ignorance – **the onus is on each individual business to locate, digest and comply with all regulations that are relevant to it**. Based on the above information it seems that many thousands of regulations imposed by different jurisdictions are in force at one time. Little wonder then that deputy PM John Anderson says State environmental laws are so complicated that he has no idea if he obeyed them on his north-west NSW property.

2.1.1 A CASE STUDY OF REGULATORY COMPLEXITY

Just how complex are our regulations? While it is not possible to accurately count up the total number of regulations currently in force around Australia, Access Economics has undertaken a narrower case study – how much regulation is associated with opening a simple business bank account?

A dozen pieces of regulation and over 200 pages of documentation may be required to open a business bank account

[13] Victorian Competition and Efficiency Commission (2005) *The Victorian Regulatory System,* Victorian Government, Melbourne, January 2005, p10-11.

[14] Queensland Government Local Government & Planning Website http://www.lgp.qld.gov.au/Default.aspx?ID=134

[15] http://www.hs.com.au/resource/blis.htm

[16] Senate Employment, Workplace Relations and Education References Committee (2003) *Small Business Employment*, Canberra, February, p.115.

Twelve pieces of 'regulation' directly affect dealings between an Australian financial institution and its clients. These cover both Federal and State laws as well as enforceable industry codes, including:

- Financial Services Reform Act
- ASIC Act
- Fair Trading Act
- Privacy Act
- Corporations Act
- Code of Banking Practice
- Trade Practices Act
- Financial Transactions Reports Act
- Proceeds of Crime Act
- Real Property Act
- APRA Act
- Consumer Credit Code

To ensure compliance with all these regulations, a consumer opening a new business bank account or taking out a home loan may receive over 200 pages of documents. In 1985 the average documentation required was around 20 pages.

What is not clear yet is whether all this additional paperwork is leading to the desired outcome – better informed consumers. Anecdotal information from financial institutions is that consumers are in fact more confused than ever before. Overwhelmed by the amount of information made available, they read none of it, instead approaching their advisor at the financial institution for clarification of key terms and conditions.

Moreover, the regulated content of some of the information required may actually mislead consumers. For example, obligations to present comparison rates of return that oversimplify the differences between financial products can lead consumers to choose products based on an equally oversimplified understanding of those differences that may not reflect their true preferences.

So it is clear that Australians have a lot of regulation – but is it an excessive amount? Some commentators may suggest that the rise in the amount and complexity of regulation is merely a function of a growing economy. That is not necessarily so.

But the real question is whether our regulations would pass cost/benefit analysis. And to answer that requires an understanding of the costs of regulation.

2.2 THE COSTS OF REGULATION

The costs of regulation include:

- costs to taxpayers (*administration*);
- costs to business (*compliance*); and
- costs to the economy (*efficiency* or *deadweight losses*).

Economists expect the magnitude of costs to increase down that list, so that administration costs are just the tip of the regulatory cost iceberg. However, as we move down those categories it also becomes ever harder to accurately quantify the amount of costs involved.

There is no widely agreed methodology with which to calculate the costs of regulation. [17] Previous studies have taken different approaches, though none are comprehensive. Most Australian research is generated by surveys which ask business respondents to estimate the amount of time spent complying with a particular or a range of regulations. Up to date examples of these include ACCI and AIG industry surveys.

The United States, and to a lesser extent the United Kingdom, also make use of information published by the government in regulation impact statements or on the cost of government programmes to estimate the economy-wide burden from a number of regulations.

2.2.1 COSTS TO TAXPAYERS – ADMINISTRATIVE

The cost incurred by taxpayers (through their governments) in designing, implementing and enforcing regulation are typically the most visible and easily identifiable costs. Even so, it is generally not possible to isolate the total of government resources devoted to a particular piece of legislation.

Federal agencies with direct regulatory power had a total budget of $4.5 billion in 2001-02 and employed over 30,000 staff, but many more bureaucratic resources within Government departments are devoted to researching, formulating and monitoring policy with regulatory impacts. Governments must also fund the legal institutions such as courts and tribunals.

It is difficult to determine the total resources consumed by regulatory agencies at the State level, as many regulators do not produce annual reports that are separate to those of the Department to which they report (and are not always separately identified in those Departmental accounts).

But some comparisons across jurisdictions are possible for specific regulatory tasks. Table 2.1 shows the budgets of State competition and taxation bodies, compared with their Federal counterparts; the ACCC and the ATO.

[17] For a synthesis of possible approaches, including econometric studies, business surveys, engineering needs and general equilibrium models, see Hahn R and Hird J (1991) 'The Costs and Benefits of Regulation: Review and Synthesis' *Yale Journal on Regulation* 8(1), 233-78.

TABLE 2.1: OPERATING EXPENSES OF STATE COMPETITION/TAX REGULATORS, 2002-03

JURISDICTION	COMPETITION REGULATOR	2002-03 $M	TAXATION REGULATOR	2002-03 $M
NSW	Independent Pricing & Regulatory Tribunal	11.4	Office of State Revenue	79.3*
VIC	Essential Services Commission	11.7	State Revenue Office	56.2
	Victorian Competition & Efficiency Commission#			
QLD	Queensland Competition Authority	5.6	Office of State Revenue	37.2
SA	Essential Services Commission of SA	4.3	RevenueSA	24.8^
WA	Economic Regulation Authority**	n/a	Office of State Revenue	31.3^^
TAS	Government Prices Oversight Commission	0.2	State Revenue Office	6.2
	Office of the Tasmanian Energy Regulator	1.5		
ACT	Independent Competition & Regulatory Commission	2.1	ACT Revenue Office	n/a
NT	Utilities Commission	0.6	Territory Revenue	5.2*
State Total		**37.5**		**240.1**
Federal Govt	***Australian Competition & Consumer Commission***	***73.0***	***Australian Taxation Office***	***2,133.0***
Australian Total		**110.5**		**2373.1**

* Excludes First Home Owner Grants # Not established until July 2004 ^Based on cost allocated to sub-program 2.1: Revenue Collection and Management ** Not established until January 2004 to replace the Office of Gas Access Regulation, Office of the Rail Access Regulator, Office of Water Regulation ^^Based on cost allocated to Land Tax, Payroll Tax, Stamp Duties and Grants & Subsidies

2.2.2 COSTS TO BUSINESS – COMPLIANCE

The direct costs of regulation include the costs incurred by businesses in complying, such as:

- staff time needed to comply with regulations;
- hiring of any additional staff required to meet the additional administration burden;
- maintaining and developing new and up-to-date reporting systems;
- obtaining advice (lawyers, accountants, architects etc);
- educating staff about the new requirements; and
- any associated costs of advertising, travel or the like.

These costs also indirectly affect the broader community by increasing prices and sometimes by delaying the introduction of new products and services.

That said, business compliance costs are that proportion of a firm's administrative processes and resources which are devoted to activities *they would not do if the regulation did not exist*.

Some compliance procedures, such as accurate record keeping, would likely occur even without regulatory stipulation. That makes it very difficult to make judgements about what activities would occur without regulation.

The leading example of this incremental cost approach to compliance costing is the MISTRAL model used in the Netherlands. A Dutch study using the MISTRAL model found that **around one fifth of all administration costs borne by business were caused solely by compliance responsibilities**. [18] Moreover, some activities may still be undertaken, but they would be structured in a more efficient or less costly manner than that required to meet particular regulatory requirements. The MISTRAL model cannot calculate the latter costs. While caution is required when extrapolating from the Dutch experience to Australian regulation, a figure of around 20% would support Australian survey data that regulatory compliance costs are significant.

As noted above, most Australian research is generated by surveys which ask business respondents to estimate time spent complying with a particular or a range of regulations, such as ACCI and AIG industry surveys (see the comments in the box). These focus on particular types of regulation, such as tax or environmental regulation. There have been no major studies on the overall costs of regulation to Australian businesses in recent years.

What are Australian businesses saying about compliance costs?

- In dealing with government regulation, the greatest concern to business is the complexity of regulation, followed by the costs of compliance.[19]
- 91% of small businesses and 76% of large firms surveyed prior to the 2004 election described the frequency of changes to tax laws and rules as a major or moderate concern for their business.[20]
- Firms, regardless of size, expressed more concern over labour regulations and on-costs than labour costs themselves. In ACCI's pre-election survey the greatest concern was over workers' compensation costs, unfair dismissal legislation and termination, change and redundancy regulations.[21]
- Regulations have varying impacts depending on firm size. Larger firms report greater concern with environmental and OH&S regulations.[22]
- The Australian Industry Group estimated that each Australian manufacturer spends 102 hours a month of staff time managing compliance, equivalent to 1.8 hours per employee. At average manufacturing wage costs, this totals over $680 million per year for the Australian manufacturing sector.[23]

[18] Chittenden, F, Kauser, S & Poutziouris, P (2001) *Regulatory Burdens of Small Business: A Literature Review,* Manchester Business School, p.*3.* This result is obviously applicable to the Dutch context. However, it is indicative of the scale of regulatory compliance costs in a modern developed economy.

[19] ACCI (2004), *ACCI Review,* June 2004, p.8

[20] ACCI (2004), *ACCI Review,* June 2004, p.4

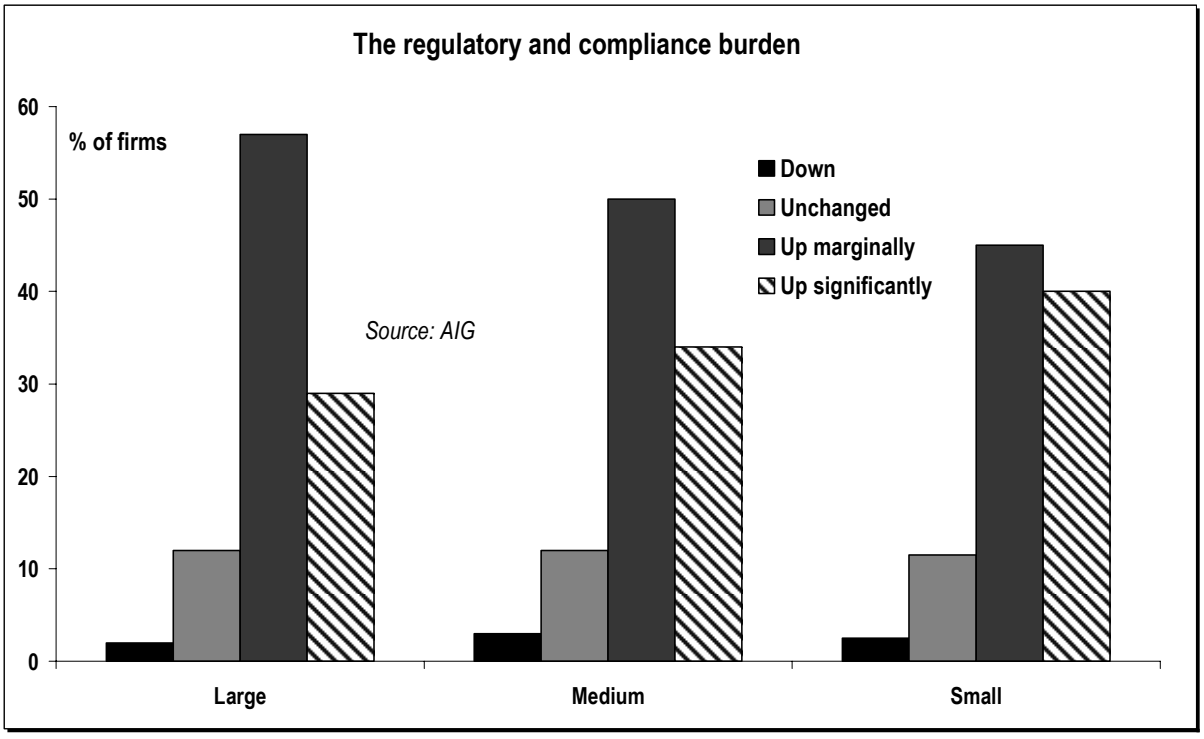
[21] ACCI (2004), *ACCI Review,* June 2004, p.7

[22] ACCI (2004), *ACCI Review,* June 2004, p.9

[23] Australian Industry Group (2004), *Compliance Costs Time and Money,* Sydney, November 2004.

- A US analyst suggests paperwork-related compliance burdens amount to around one third of the aggregate regulatory burden in the United States. If this same multiplier applied in Australia, total compliance costs would amount to as much as 7% of GDP. [24]
- The Productivity Commission found that, in 1994-95, the administrative burden resulting from regulation amounted to some $11 billion for businesses. [25] A more recent OECD study estimated that the direct compliance costs of taxation, employment and environmental regulations totalled more than $17 billion in 1998 for small and medium sized Australian businesses alone. [26]
- While such surveys occur regularly enough to identify current trends in compliance activity, there will be a potential upward bias in the results due to a lack of common understanding about what constitutes a compliance cost; an inclination for business people to overestimate their compliance burden; and an inability accurately to estimate and allocate the costs of compliance activities to particular forms of regulation, especially if the survey respondent is being asked to give an immediate answer.
- An alternative way to use business surveys is to focus on business perceptions about changes to the overall level of compliance required, rather than resources spent on a particular regulation. For example, AIG found 85% of manufacturers thought the time spent complying with Federal regulation had increased over the three years to 2004 (see Figure 2.2).

FIGURE 2.2: PERCEPTIONS OF CHANGES IN THE COMPLIANCE BURDEN 2001-04



Source: AIG (2004) *A Survey of Business Priorities in the lead up to the Budget*

[24] Banks (2003), *The good, the bad and the ugly: economic perspectives on regulation in Australia*, Address to the Conference of Economists, Business Symposium, October, p6.

[25] Banks (2003), *The good, the bad and the ugly*, p5.

[26] OECD (2001), *Business' views on red tape: administrative and regulatory burdens on SMEs*, October.

Concern about the rising costs of compliance is not limited to manufacturers. Government business liaison programs have detected a more general concern that the costs of meeting regulatory requirements have risen significantly. [27]

For example, business representatives from the financial services sector indicate that the cost of meeting financial sector regulatory requirements had increased '3 or 4 times over the past 5 years'. [28] And, according to some estimates, the combined annual costs to the top 50 listed companies of compliance with CLERP 9, the Financial Services Reform Act and the Australian Stock Exchange's corporate governance guidelines is as high as $375 million. [29]

Another recent study for the Australian Financial Review (AFR) found half of surveyed firms spend an extra day per week on governance and have hired an average of 18 extra staff to deal with this. [30] This survey found that one of Australia's largest financial service companies spent 20% of board time on regulatory issues, while another firm said compliance and governance issues took up as much as half of its board's agenda. A third noted that four additional board meetings needed to be held each year to deal with regulatory issues.

Similarly, the Australian Bankers' Association (ABA) has forecast that the compliance bill for the major banks is likely to increase by $125 million this year, up 20% in some cases owing to new governance regulation and financial and accounting reforms. [31]

2.2.3 COSTS TO THE ECONOMY – EFFICIENCY

The economy-wide costs stem from an allocation of resources which is different to that which would otherwise have prevailed in the absence of regulation. Its impact shows up as:

- **Higher prices** for consumers and other businesses and **lower wages** to employees (to finance compliance costs, and because less efficiently allocated resources mean productivity is lower than it would have been), and
- **Higher taxes** paid to governments (to finance administration costs).

These are typically the largest costs and most well-hidden costs of regulation. Moreover, they are often incurred by policymakers with the best intentions, but with less than perfect information, and less than adequate assessment, so that regulators end up enforcing less than optimal outcomes.

It should also be noted that efficiency costs are not merely static. **There are dynamic efficiency costs to the economy as well because regulation can discourage risk-taking and reduce accountability**. In particular, bad regulation can breed a culture of unaccountability among individuals and corporations and – at greater still potential cost – it can reduce the return to risk. That discourages entrepreneurs and others from the innovation that leads to growth in national income.

[27] Treasury (2004) *Key themes from the Treasury Business Liaison Program – April 2004*, Canberra, April.

[28] Treasury (2004) *Key themes.*

[29] Nicholas, N & Buffini, F (2004) '*Backlash against regulation costs*' Australian Financial Review, 5 July, p.1, 60.

[30] Australian Financial Review (2004) *Editorial: Beware the Overkill on Regulation*, 5 July, p62.

[31] Nicholas, N & Buffini, F (2004) 'Backlash against regulation costs' Australian Financial Review, 5 July, p.1, 60.

But how big are they? These costs are not counted in business compliance cost surveys or in regulation impact statements.

Nevertheless, the available indicators do suggest a strong link between greater regulation and poorer economic outcomes – lower GDP, higher unemployment, and a less equitable distribution of wealth.

Two yardsticks of the efficiency costs of Australia's regulatory burden are considered here:

- The first indirect yardstick of the current burden of regulation on prosperity comes from estimates of the efficiency gains from two decades of deregulation and reform.
- A second yardstick of efficiency costs is provided by a World Bank study of regulatory reach across 137 nations.

2.2.4 ESTIMATES OF EFFICIENCY SAVINGS FROM PAST DEREGULATION

Looking back, **there is evidence that Australians have reaped a significant dividend from previous moves to deregulate**. That dividend provides indirect evidence of the remaining cost burden on Australians and their economy from regulation.

The consensus in the literature appears to be that **the largest single boost to the size of the Australian economy from deregulation comes from national competition policy reforms**. Ahead of the implementation of those reforms, the then Industry Commission (in its 1995 Final Report to the Council of Australian Governments, *The Growth and Revenue Implications of Hilmer and Related Reforms*) estimated that those reforms would boost the size of the Australian economy by 5.5%. A 1999 Productivity Commission report (*Impact of Competition Policy Reforms on Rural and Regional Australia*, using the ORANI model) was more modest. Its estimate was that GDP had lifted 2.5 percentage points in response to those reforms.

Similarly, several studies were made both before and after the implementation of **the 2000 tax reforms.** Some were, for example, cited in a Senate inquiry in 1999. A study by the Melbourne Institute found that broad indirect tax reform could boost GDP by 3.75 percentage points over time. The same Senate inquiry noted a study reported by Salomon Smith Barney Stockbrokers based on Econtech estimates found that indirect tax reform could increase GDP by about two percentage points. The changes modelled were similar to but not the same as the indirect tax reforms in the eventual package. After the release of the package, the Melbourne Institute estimated those reforms would add 1.7 percentage points to GDP.

In addition, an unpublished Access Economics study in 2000 estimated that the tax reforms of that year would eventually lead to a 2.5 percentage point increase in GDP.

There have also been studies estimating the impact of **lower tariff barriers** on prosperity. *Trade 2004, A statement by Mark Vaile, Minister for Trade*, notes that "For Australian families and consumers, trade and increasingly open markets boost living standards by giving them a wider range of goods and services to choose from at lower prices. Even conservative estimates suggest that over the past ten to twenty years, as tariffs in Australia have come down, Australian families have found themselves at least $1000 per annum better off because of their much greater purchasing power. Cars imported into Australia are now around 25 per cent cheaper than if 1987 tariffs still applied, and clothing and footwear are around 14 per cent cheaper."

That estimate of $1000 per family per year is consistent with tariff reform boosting the size of the Australian economy by somewhere around 0.75 percentage points. However, to date the

Productivity Commission has not compiled an overarching review of the impact that Australia's tariff reductions of the past two decades have had on the size of the economy. Smaller studies across single sectors in which tariffs have been cut or are proposed to be cut – such as the TCF sector and the car industry – suggest that there are gains to be made. Given the relative size of these sectors the boosts they imply to GDP are relatively small. Clearly the aggregate effects of the rather more broad-based tariff reductions which have taken place in Australia over the past two decades may imply a greater gain in GDP than these individual estimates would suggest – perhaps up to 0.5 percentage points.

Finally, estimates of the impact of **workplace relations reform** are lacking. Access Economics has previously expressed broad agreement with the view that workplace relations policy reforms have added at least 1.7% to GDP by cutting average rates of unemployment.[32]

Adding up those gains to GDP, as estimated in the literature, points to a lift in prosperity of something like 7% of GDP over the past two decades being attributable to the deregulation adopted over that period.

However, that may well be an understatement, as (1) many smaller reforms are not covered by these studies, and as (2) the productivity improvements resulting from particular reforms can interact with other reforms in other markets, with the result that the benefits achieved from the interaction of those reforms can become greater than what the sum of their parts might otherwise suggest. Or, in other words, there are additional benefits available through greater productivity growth when reform is pursued on a broad front.

With the latter caveats in mind, a forthcoming Access Economics report commissioned by the Business Council has separately estimated the reform dividend from the deregulatory agenda of the past two decades at 10.8% of GDP. [33]

Looking forward, can we expect further reforms would generate similar dividends? A recent report commissioned by the National Competition Council found that, despite the progress to date, there remains "considerable opportunity for the extension of the National Competition Policy reform program to capture efficiency improvements across a broad range of sectors."[34] This finding was based on a comparison of Australian reforms to our OECD peers. In particular, the report concluded that reforms to Australia's health, education, communications and environment sectors are likely to produce the greatest net benefits.

[32] Access Economics (2005), *The Reform Dividend: A Report for the Business Council of Australia* (unpublished).

[33] Access Economics (2005), *The Reform Dividend: A Report for the Business Council of Australia* (unpublished).

[34] National Competition Council (2004) *Microeconomic Reform in Australia – Comparison to other OECD Countries,* NCC Occasional Series, AusInfo, Canberra, November 2004, p.12

2.2.5 BENCHMARKING AUSTRALIAN REGULATORY PRACTICE

Another indicator of the efficiency costs to Australia of our less than best practice regulation is provided by a World Bank study of regulatory reach across 137 nations.

The Bank is now releasing results from a large and on-going study of how its membership is regulating. [35]

In benchmarking Australia's regulatory practice, the World Bank study makes it clear that:

- **Business needs a clear, consistent and simple framework in which to operate:** Yet in Australia it takes 11 procedures, 157 days and 14.4% of the money owed to enforce a contract. A delay of 157 days to enforce a contract leaves us ranked poorly (16th) against countries such as France (75 days), Japan (60 days), New Zealand (50 days) and Norway (87 days). And the costs of enforcing a contract in Australia are also relatively high (ranking us 44th) when compared with Japan, NZ, Norway, Sweden and the US.
- **Our stamp duties are very high and dampen the incentive to invest:** Australia's processes for registering a property (including stamp duties) are very expensive – we rank 62nd in the world, a less-than-impressive effort. As stamp duties and the regulatory processes surrounding them are highly inefficient taxes on investment, they are a high priority area for reform.
- **The cost to create collateral in Australia is 5.5% of income per capita:** That leaves us 59th in the world, a rank bettered by most developed nations.
- **Business people need to be able to take risks, and financial markets need to be able to support them in risk-taking with confidence:** Efficient insolvency procedures lead to higher recovery rates when businesses close, so banks are more willing to lend and thus entrepreneurs are more likely to start up a new business. Yet the associated costs of closing a business in Australia amount to 8% of the estate – compared with the UK at 6%, NZ and Japan at 4% and Norway at 1%. Australia's ranking on this global indicator is 26th, suggesting we could do better in fostering an entrepreneurial culture.
- **And fostering an entrepreneurial culture is easier if starting businesses is easier:** If starting a business proves too difficult, costly or time consuming, there is strong incentive for would-be entrepreneurs to operate in the black economy. And if that happens, then taxes aren't paid, credit is hard to get, products are not subject to quality controls, and corruption thrives. In short, many of the benefits that good regulation can provide are lost. So there is room for improvement on the costs of starting a business in Australia, with 2.1% of income per capita required to start a business here.
- **'Barriers to firing are barriers to hiring':** Yet in Australia, firing costs amount to 17 weeks worth of pay. In New Zealand, this cost is zero, in Norway it is equivalent to 12 weeks, in the US, 8 weeks. And the World Bank's rigidity of hours index shows Australia ranked 23rd in the world (versus perfect scores in several of our peers, including Canada, the US and NZ).

For more detail on Australia's relative rankings, see Appendix A.

[35] World Bank (2004) *Doing Business in 2004: Understanding Regulation.*

3. GOOD PROCESS = BETTER REGULATIONS

Chapter 1 noted that the benefits of regulation are often overstated and its costs understated, and noted that economists increasingly agree on the need for a light regulatory touch. Yet Chapter 1 also noted regulators and politicians have some incentives to regulate when they shouldn't, and Chapter 2 noted the total stock of Australian regulation (and its costs) continues to climb.

So we are still headed in the wrong direction. Why? This chapter investigates the processes for regulation formulation in Australia.

It does so for two reasons – first, better processes can give better regulation (or reduce the risk of bad regulation). Second, given the incentives in favour of bad regulation, the public needs a champion to 'guard the guards themselves' – to help make sure Australians aren't lumbered with more and more bad regulation.

In brief, **we are concerned that, despite the rising flow of new regulation, scrutiny of it by the Office of Regulation Review (ORR) is falling – just 7% of new Federal regulations were assessed in 2003-04**. Miraculously, more than 90% of such assessments were deemed 'adequate', and on only 9 (out of 105) occasions in 2003-04 did the preparation of a Regulatory Impact Statement (RIS) affect the subsequent regulation. And, mysteriously, the frequency with which ORR says a regulatory risk assessment is required has been steadily falling, halving in the past five years.

The wolf seems to be roaming the hen house. The Federal system is flawed as **the bureaucrat in favour of a regulation also assesses its impact, albeit 'in consultation with the ORR'**. And there are other risks too – even if the RIS process is perfect, last minute political compromises such as Senate amendments can override good process and lead to bad outcomes.

This chapter therefore examines how Australia's regulatory review processes compare with OECD best practice guidelines.

3.1 BACKGROUND ON CURRENT RIS PRACTICE

The Office of Regulation Review (ORR) in the Productivity Commission is charged with improving the efficiency and effectiveness of legislation and regulation.

It is therefore the only organised body which can protect the interests of Australians against the rising cost of regulations, and the known risks arising from the incentives that politicians and regulators have to opt for populism over policy. In effect, the ORR 'guards the guards themselves' [36] – those who add new rules to the burden of existing ones.

[36] So the old joke 'Why is there only one competition regulator?' actually has a response: the ACCC is among the organisations whose regulations are monitored by the ORR. However, the ORR doesn't seem to be a strong influence on the ACCC – in 2003-04 only one RIS was required of the ACCC, yet the ORR rated the ACCC's effort on that RIS "as inadequate": see the Productivity Commission's 2003-04 Annual Report, page 53.

The key element of the ORR's regulation review system is the Regulation Impact Statement (RIS). Since 1997, preparing a RIS has been compulsory for all reviews of existing regulation, proposed new and amended regulation, and proposed treaties involving regulation which will directly affect business.

All government departments, agencies, statutory authorities and boards that make or review regulations are subject to RIS requirements. Once an administrative decision is made that regulation may be necessary, and before a policy decision to regulate is made, a RIS should be developed in consultation with the ORR.

Once the ORR finds that a given draft RIS complies with the Government's requirements, the RIS is attached to the proposals to be considered by the relevant decision maker (such as Cabinet, the Prime Minister, the Minister, or a board).

But the problem with this process is that the poacher is asked to play gamekeeper. The bureaucrat in favour of a particular regulation also assesses its impact, albeit 'in consultation with the ORR'.

And there are other risks here too – even if the RIS process is perfect, last minute political compromises such as Senate amendments can override good process and lead to bad outcomes.

A Guide to Regulation (1998) outlines seven key elements to a RIS:

1. Identifying the problem
2. Identifying the objective
3. Listing regulatory and non-regulatory options
4. Assessing impacts on consumers, business, government and the community
5. A consultation statement
6. A recommended option
7. A strategy to implement and review the preferred option.

And ORR guidelines exempt regulatory proposals 'of a minor or machinery nature', yet 'minor' is not defined, so the ORR must ensure a consistent interpretation. But it seems most proposals must be 'minor', because those regulatory proposals which are deemed to require preparation of a RIS under the guidelines constitute only a very small proportion of total regulatory proposals put forth each year. For example, in 2003-04, the Australian Government introduced approximately 1,700 regulations. The ORR advised that RISs were required for 174 of these proposals, though many of these were not considered by decision-makers within that financial year, so the final figure for the number of regulatory proposals that required RISs in 2003-04 was 114, less than 7% of the total number of regulations.

Once the requirements of RIS preparation are triggered, relevant departments and agencies must submit all RISs prepared to the ORR for advice and assessment prior to the decision-making stage.

In some respects the State and Territory subordinate legislation Acts have a broader trigger for RIS requirements than does the Commonwealth. This is largely owing to the recognition of community as well as business impacts of regulatory proposals in the States and Territories. However, in other respects, the Commonwealth guidelines are wider in scope:

- covering all forms of regulation and quasi-regulation, and
- requiring proposals that involve both significant costs and benefits to undertake a RIS.

A comparison between State and Territory regulatory review practices and those of the Commonwealth is in Section 3.4.

Although the ORR makes it a practice to provide advice to agencies on improving the readability and user-friendliness of the RIS, there are no formal requirements to include an executive summary, and there is no length limit.

And RIS quality is not formally enforced by the Commonwealth Parliament's Senate Standing Committee on Regulations and Ordinances, though the Committee does occasionally use RISs (as published in explanatory materials) in reviewing legislation.

There is some formal forward planning for regulatory proposals in so far as Commonwealth departments and agencies are required to publish their annual regulatory plans. However compliance in this respect is uneven and patchy.[37]

The Australian Government's *A Guide to Regulation* sets out requirements for community consultation. It stipulates that regulators should consult with relevant parties early in the process. Although not compulsory, it also recommends exposing draft RISs to consultation.

3.2 EVALUATING THE RIS PROCESS

In 2003-04, the ORR found that 18 departments and agencies were fully compliant with the Government's RIS requirements (compared to only 12 in 2002-03).[38]

Figure 3.1 and Figure 3.2 depict compliance with RIS requirements over time at the decision-making and tabling stages. Figures at the top of each bar show numbers of RISs assessed as adequate as a percentage of the total number of RISs required.

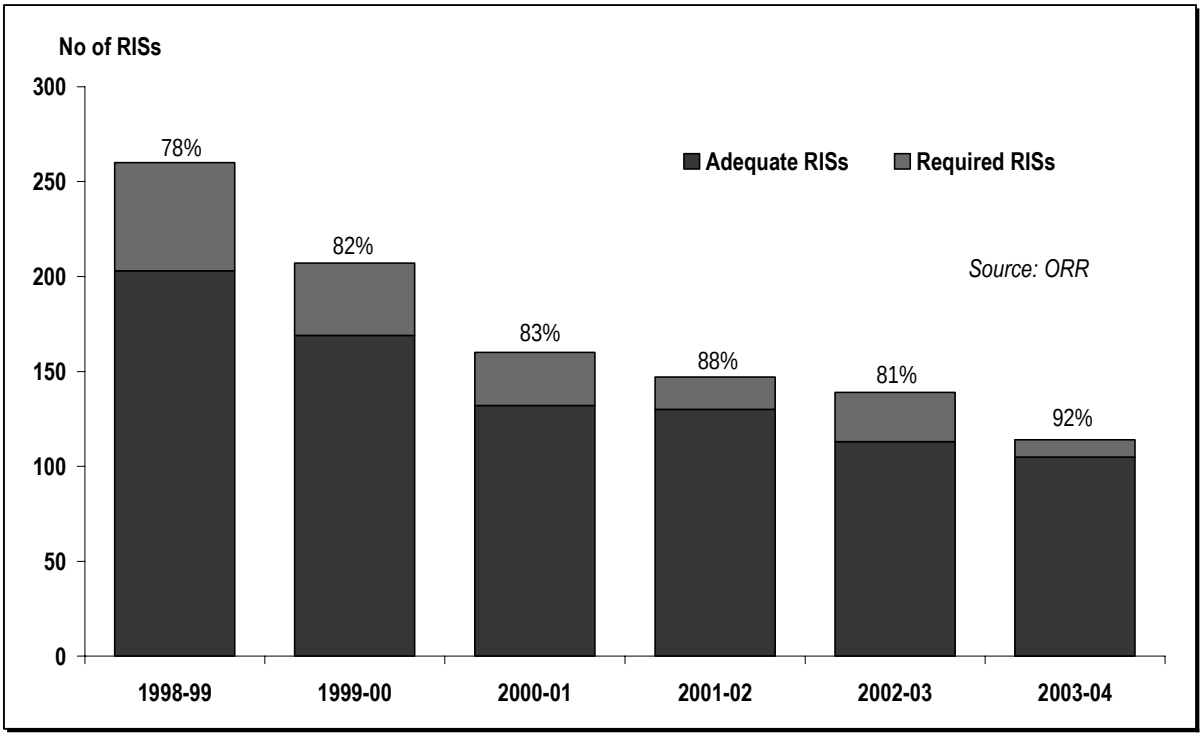
A concern underscored by Figure 3.1 is that the frequency with which the ORR is saying that a regulatory risk assessment is required has been steadily falling, indeed halving in the past five years.

One means for measuring the effectiveness of the RIS process is to examine those instances in which a change to the proposed regulation was effected during the review stages, thereby indicating a more robust analysis of regulatory alternatives. The ORR found that in 2003-04 the regulatory response changed during the policy development process in nine of the 105 RISs prepared by the Government.

[37] Steven Argy, Matthew Johnson, *Mechanisms for Improving the Quality of Regulations: Australia in an International Context*, Productivity Commission Staff Working Paper, July 2003, at page 85.

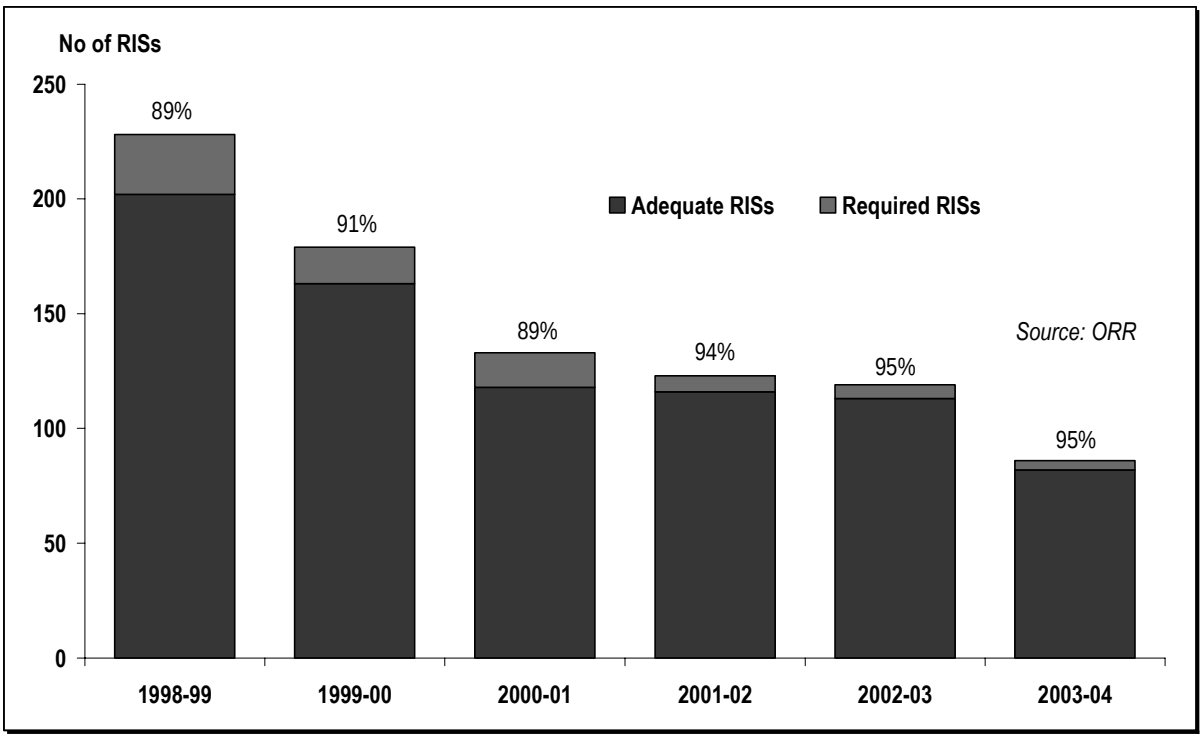
[38] *Regulation and its review*, 2003-04, Productivity Commission, at page xvii.

FIGURE 3.1: DECISION-MAKING STAGE



It seems many RISs are completed too late in the regulation design process to have any real impact on the ultimate decisions.

FIGURE 3.2: TABLING STAGE



Furthermore, there is no explicit requirement for policymakers to consider how proposed new regulation would interact with other regulation at the same or different levels of government.

Although this would naturally be a part of a proper assessment of the impact of any proposed regulation, such assessments as currently occur tend to be narrowly focussed and ignore the existing regulatory environment.

3.3 GAPS BETWEEN CURRENT SYSTEM AND BEST PRACTICE

Good processes help ensure good regulation. Efforts to improve the regulatory process can range, for example, across transparency, timeliness, consultation arrangements and the like. Examining the practice of regulation development and review in other jurisdictions within Australia (see Section 3.4) and practice abroad can provide useful insights and lessons for the Commonwealth to improve current systems.

International comparisons also provide useful benchmarks; the US and the UK are generally thought to be world leaders in regulatory quality control processes. Regulatory policies in developed countries everywhere are evolving at a rapid pace. The OECD and APEC are currently approaching the end of a four year process to finalise guidelines on good regulatory practice while the World Bank has begun an annual review of regulation in more than 130 countries (see *Doing Business 2004* and *2005).*

Despite widespread study of regulatory processes and review, it is nevertheless difficult to nominate a 'world's best practice'. That said, the OECD lists ten best practices as reference points for designing an effective program and evaluating existing RIS programs.[39]

The OECD recommends:

1. Maximise political commitment to RIS
2. Allocate responsibilities for RIS program elements carefully
3. Train the regulators
4. Use a consistent but flexible analytical method
5. Develop and implement data collection strategies
6. Target RIS efforts
7. Integrate RIS with the policymaking process
8. Communicate the results
9. Involve the public extensively
10. Apply RIS to existing as well as new regulation

The following examines these benchmarks in light of current Commonwealth practice.

(1) Maximise political commitment to RIS. Australia's RIS requirements are set out in *A Guide to Regulation* (ORR 1998), and further advice on the adequacy of RISs can be sought from the ORR. But the consequences of non-compliance amount to little more than a slap on the wrist. For example, reporting of non-compliance occurs with a 4-16 month lag, and so fails to inform parliamentary discussion when it is most timely. The Minister and relevant

[39] The World Bank, like many countries within the OECD, use the term regulatory impact assessment rather that RIS. For consistency, we use the term RIS throughout as the two concepts are identical.

bureaucrats have already moved on, and there is little scope to revisit the regulation or penalise the authors of an inadequate RIS assessment.

(2) Allocate responsibilities for RIS program elements carefully. Currently, departments and agencies are responsible for RISs – assessing their own proposals for regulation. These are then assessed by ORR who report on their compliance or otherwise in the Productivity Commission Annual Report. That means there is no central body with the skills and authority to oversee the RIS process to ensure consistency, credibility and quality.

(3) Train the regulators. The ORR trains officials through formal seminars, meetings and ad hoc advice in addition to publication of *A Guide to Regulation* and distribution of example RIS material, including on websites. Limited in-house training is provided by some departments and agencies. In contrast, several other countries provide more intensive training and/or access to more comprehensive support material (including the UK, Korea and Italy). In the Netherlands, the regulatory review office maintains a help desk as a means of providing expert advice on appropriate completion of RIS requirements.

(4) Use a consistent but flexible analytical method. All regulation reviews should be completed using the benefit-cost principle. However, analytical methods can vary as long as the RIS identifies and weighs all significant positive and negative effects and integrates qualitative and quantitative analyses. The Commonwealth stipulates that all significant economic, social and environmental costs and benefits must be identified, but the degree of detail and depth of analysis (and requirement for quantification) depends on the significance and impact of proposals. For those proposals which maintain or establish restrictions on competition, the COAG requirements must also be met.

(5) Develop and implement data collection strategies. If there is no good data, then the bureaucrats are guessing (meaning that they run the risk of assuming that they can achieve better outcomes than markets without the data to analyse that key proposition). Some guidance material is provided in *A Guide to Regulation*, though improved and explicitly defined methods of estimating compliance costs would be of greater benefit.

(6) Target RIS efforts. Regulators should worry most about the regulations with the largest potential impacts (whether they be deadweight losses, compliance or administration costs). The ORR devotes more resources to proposals of high significance where a higher level of analysis is expected. In the US, Korea, and the UK, monetary tests (or a combination of monetary and other tests) are used as a 'rule of thumb' for determining those regulations that meet threshold significance requirements. In the Netherlands, the regulatory review office help desk assists ministries with the design of analyses, data collection, the analysis and interpretation of data, access to a statistician and funding for necessary research. However, in Australia the separation between significant and non-significant proposals is less clear cut.

(7) Integrate RIS with the policymaking process as early as possible. Regulators should see RIS insights as integral to policy decisions, rather than as a nuisance to be avoided. Though departments and agencies are required to consult the ORR at an early stage in the policy development process, current Australian practice appears to suggest that a RIS is compiled more as an add-on than an integral part in the process.

(8) Communicate the results. Policymakers are rarely analysts. RIS results must be communicated clearly, using a common format. In New Zealand, RISs are required to incorporate an executive summary and have an upper page limit. Such measures can facilitate decision-making by streamlining information into a digestible format. Also in NZ, the RIS must be attached to a press statement announcing any new policy and published on the web, thereby ensuring effective and widespread communication of regulation reviews to

interested parties. It is always difficult to keep track of the latest round of potential regulation coming out of government, and there are myriad government websites to review. Publishing on the web is a necessary part of disseminating proposals but, where possible, the existence of proposals needs to be directly communicated to affected parties. In Australia, the RIS is required to contain seven key elements, which enhances the readability of the document. However, there is no requirement for a RIS to include an executive summary or an upper page limit. Both measures would facilitate reader-friendliness.

(9) Involve the public extensively. The OECD indicates that interest groups should be consulted widely and within an appropriate timeframe – hence the consultation process is likely to contain several steps. The RIS must incorporate a consultation statement, summarising views or reasons why consultation was inappropriate. A final RIS for bills and disallowable instruments must be tabled. It is recommended that RISs for other instruments should be otherwise made public (for example, on a website), but this is not a requirement. The release of 'draft' RIS for public consultation is encouraged but not required, although recent legislative changes (including the *Legislative Instruments Act 2003)*[40] attempt to enshrine the consultation process.

(10) Apply RIS to existing as well as new regulation. RIS disciplines should also apply to reviews of existing regulation, given the risk that past regulation has become bad regulation. Preparation of a RIS is required for all reviews of existing regulation, except where proposed changes are minor or the scope of the original RIS was detailed and complex enough to encompass proposed changes. Nevertheless, monitoring is sometimes irregular and not particularly systematic.

3.4 SUMMARY OF HOW STATES/TERRITORIES COMPARE TO COMMONWEALTH

The ORR surveyed jurisdictions in 2002 to gauge the degree to which regulation development, implementation and review varied among the States, Territories and Commonwealth. This survey provides useful insight as to which governments are achieving best regulatory practice, highlighting those areas where improvements are possible.

Again using the OECD guidelines, it is informative to note where some States and Territories have implemented different procedures from the matching ones at the Commonwealth level.

Maximise political commitment to RIS

- In the ACT, the Cabinet Office may reject submissions which have an inadequate RIS.

Allocate responsibilities for RIS program elements carefully

- Senior officials in Tasmania and Queensland must sign off or certify RISs.
- In several States Parliament has specific responsibilities to ensure RIS requirements are met.

[40] See page 6 of *Regulation and its Review* – All legislative instruments must be recorded on a Federal Register. The electronic register allows individuals/businesses to access all Commonwealth instruments and related material in a single place via the internet. Under this Act, legislative instruments will sunset after 10 years in operation. The Act also requires regulators to consult with the community before making a legislative instrument, particularly in instances where the regulation will affect businesses or restrict competition.

Train the regulators

- Queensland provides software aids to the completion of RISs.

Target RIS efforts

- In Victoria, the responsible minister must ensure that independent advice is sought to confirm adequacy of RIS – either from a consultant, the Victorian Office of Regulation Reform or other units within Government with suitable expertise and independence.
- Queensland uses monetary tests (or a mix of monetary and other tests) as a 'rule of thumb' for determining which regulatory proposals meet threshold significance requirements.

Involve the public extensively

- A minimum period must be allowed for comments in NSW, Victoria and Tasmania. For example, in Tasmania, consultation is mandatory for both primary and subordinate legislation where a RIS is considered necessary. Once the RIS and the overall public consultation program is approved by the State's Competition policy unit, ads need to be placed in relevant local newspapers or other publications inviting submissions on the RIS. A minimum of 21 days must be allowed for receipt of submissions. In most instances, particular interest groups are directly provided with a copy of the RIS.

That said, while individual elements of each State's regulatory review practice may be better (in some respects) than those at the Commonwealth level, on the whole the Commonwealth guidelines are broader and more comprehensive than those of any individual State.

Table 3.1 and Table 3.2 below provide a comparison of key aspects of RIS requirements and processes at the Commonwealth, COAG and State/Territory levels.

TABLE 3.1: RIS REQUIREMENTS IN AUSTRALIAN JURISDICTIONS

Jurisdiction	Bills	Subordinate instruments	Quasi-regulation	RIS required for consultation	RIS for decision maker
COAG	✓	✓	✓	✓	✓
Aust. Govt	✓	✓	✓	-	✓
NSW	- [a]	✓	- [b]	✓	✓
Vic	✓ [c]	✓ [d]	-	✓	✓ [e]
Qld	-	✓ [f]	✓ [g]	✓	✓
SA	✓ [h]	✓ [h]	✓ [h]	-	✓
WA	- [i]	- [i]	- [i]	-	- [j]
Tas	✓	✓	✓	✓	✓
ACT	✓	✓ [f]	- [b]	- [k]	✓
NT	✓	✓	-	- [l]	✓

a) Cabinet submissions for new Bills must meet best practice requirements. Rural Community Impact Statements are required where rural and regional communities are affected by the proposal.

b) Not a formal requirement, but agencies proposing quasi-regulation are expected to comply with best practice for regulatory impact assessment.

c) As of 1 July 2004 for all new legislation with potentially significant effects for business and competition.

d) For proposals that impose an appreciable economic or social burden.

e) The consultation RIS and supporting documentation is given to the decision maker.

f) For proposals likely to impose an appreciable cost on the community or part thereof.

g) The RIS requirements apply if these instruments are called up or referenced in subordinate legislation.

h) Every cabinet submission is to consider community impacts – which include regulatory, small business, regional, environmental, families and society

i) A Small Business Impact Statement (SBIS) is required to accompany any cabinet submission seeking endorsement of a regulatory, legislative or policy initiative that will significantly impact on small business. A Regional Impact Statement (RIS) must also accompany all cabinet submissions.

j) The SBIS and Regional Impact Statement are considered by Cabinet before making its decision.

k) Consultation is required, but not via a RIS.

l) At agency discretion whether draft RIS made public, but a consultation statement is required as part of the CIA.

TABLE 3.2: RIS PROCESSES IN AUSTRALIAN JURISDICTIONS

Jurisdiction	RIS Guidelines	Cost-Benefit Assessment	Report On RIS Compliance	Regulatory Plans	Sunset Clauses	RISs – Local Government
COAG	✓	✓	✓	..	✓	..
Aust. Govt	✓	✓	✓	✓	-	..
NSW	✓	✓	✓	-	✓ [a]	-
Vic	✓	✓	✓	✓	✓	-
Qld	✓	✓	✓	✓	✓	✓ [b]
SA	✓ [c]	✓ [d]	✓ [e]	-	✓ [f]	✓ [g]
WA	- [h]	- [i]	-	-	✓ [j]	-
Tas	✓	✓ [k]	-	-	✓ [l]	✓ [m]
ACT	✓	✓	-	- [n]	- [o]	✓ [p]
NT	✓	✓	✓ [q]	-	- [r]	-

..not applicable.

a) A five year automatic repeal process under the Subordinate Legislation Act 1989 (NSW).

b) The Business Regulation Reform Unit worked with local government to produce guidelines (Department of State Development 2003) to enhance best practice development of local laws.

c) RIS guidelines endorsed by Cabinet in 2003.

d) Assessment of all costs and benefits across jurisdiction.

e) Not to departments and agencies. Results sent to the Premier and Parliament as requested. It is intended to report compliance in the annual report of the Department of Premier and Cabinet.

f) Regulations within the scope of the Subordinate Legislation Act 1978 (SA) expire on 1 September in the year following their tenth anniversary.

g) The Subordinate Legislation Act 1978 (SA) applies to all regulations under the Local Government Act 1999 (SA).

h) Guidelines on the preparation of the Small Business Impact Statement and Regional Impact Statement are contained in the Cabinet Handbook.

i) Specific to small business sector and regional communities.

j) At the direction of Cabinet, the Parliament or discretion of Ministers.

k) Coverage depends on the issue and may be state-wide or regional.

l) All regulations are automatically repealed after ten years under the Subordinate Legislation Act 1992 (Tas).

m) Under the Local Government Act 1993 (Tas), the Director of Local Government must issue a certificate of adequacy of the RIS process undertaken by Council before a proposal may progress to full public consultation. (The Regulation Review Unit was involved in developing this process.)

n) The legislative program provides the basis for all detailed public consultation on the Government's legislative intentions.

o) A review clause may be inserted into legislation, particularly in a dynamic environment which may necessitate frequent review.

p) Responsible for both State and local government.

q) Reports are provided to the NT Government biannually.

r) Contained in some legislation.

3.5 IMPROVING THE REGULATORY PROCESS

There may be a natural tendency in government to ignore the non-government costs of regulation if there are not devices to keep consideration of such costs in mind. So there are several key messages here:

- Better processes can give better regulation (or reduce the risk of bad regulation).
- But processes are useless without capacity and will of policymakers to adhere to them in practice and in spirit.
- Despite the rising flow of new regulation, scrutiny of it by the ORR is falling – just 7% of new Federal regulations were assessed in 2003-04. More than 90% of all such assessments are deemed 'adequate', and on only 9 (of 105) occasions in 2003-04 did the preparation of a RIS (RIS) affect the nature of the subsequent regulation.[41]
- And the frequency with which ORR says a regulatory risk assessment is required has been steadily falling, halving in the past five years.
- The Federal system is flawed because the bureaucrat in favour of a regulation also assesses its impact, albeit 'in consultation with the ORR'. Partly as a result, bureaucrats and politicians routinely ignore or side step processes in place to prevent bad regulation.
- The RIS must be an integral part of policymaking, rather than an afterthought.
- And governments must allow meaningful consultation time with affected parties.
- In particular, these parties should have adequate access to information regarding the costs, benefits and alternatives to the proposal.

[41] That only 9 out of 105 RISs affected the determination of subsequent regulation either indicates that regulators are getting regulation creation spot-on first time around or, more plausibly, that the process of RISs informing the development of regulation is not working.

4. WHAT ARE OUR REGULATORS DOING WRONG?

Australian regulators often get it wrong. In particular, they suffer from:

- **Regulatory over-reach** – Regulators and regulations often aim at achieving more than the achievable, thereby ending up with worse outcomes than deregulated markets would give. That can arise where regulators:
  1. Overestimate their ability to get better outcomes than the market.
  2. Are overly-prescriptive in regulation.
  3. Overreact to current hot issues.
  4. Cannot enforce their rules.

- **The Financial Services Reform Act and Uniform Credit Code are good examples. And regulators often regulate symptoms rather than causes, or try to fix one problem by regulating another area** (an almost always guaranteed disaster, such as the nightmare compliance issues spawned by exempting fresh food from the GST – the aim was to help the poor, but that should have been done directly via welfare and taxes, not via bad regulation).

- **Letting regulations overlap** – Overlapping or conflicting regulation can occur between different regulatory bodies at the same level of government, or different governments, or between public and private oversight bodies. Such 'regulatory cocktails' create adverse and unintended interactions – which regulators then let lie in the lap of consumers and businesses. For example, **workers compensation and OH&S laws differ between States, despite their almost identical objectives. That generates considerable extra compliance costs for national firms, with zero benefits for Australians.**

- **Not listening** – Regulators sometimes meet with business but do not listen: again the Financial Services Reform Act is a good example. That's a mistake: industry has an incentive to ensure regulation has a low compliance cost, and enforcing compliance is easier where the regulator has consulted with industry.

- **Not looking back** – The economy is not static. Regulations can become outdated or less cost-effective than alternatives (or deregulation). And as we learn more about the economy and markets, new and more effective ways of regulating are developed. A large part of the success of National Competition Policy was its requirement to review the anti-competitive parts of existing legislation to check they made sense.

Even though it is nigh impossible to identify total numbers of current regulations or their associated cost burden, what is clear from previous studies and consultation with industry is that **certain factors raise the cost of regulation but do not benefit consumers**.

These underlying factors clearly suggest that the current burden and form of Australian regulation is excessive.

The factors identified are:

- regulatory over-reach;
- overlapping regulation;

- lack of consultation; and
- lack of ongoing review.

Often more than one of these factors can be identified in a particular regulation.

4.1 REGULATORY OVER-REACH

Regulatory over-reach occurs when regulation is not the least costly way of achieving the stated policy goal. In turn, that can arise where:

- Regulators overestimate their ability to create a better outcome than the market.
- Regulators are overly-prescriptive in regulation.
- Regulators overreact to current hot issues.
- Regulators cannot enforce their rules.

4.1.1 REGULATORS OVERESTIMATE THEIR ABILITY TO CREATE A BETTER OUTCOME THAN THE MARKET

As mentioned previously, the public interest theory of regulation suggests that government intervention may be necessary in cases of market failure. But what is market failure?

Every single market displays imperfections and distortions compared to the 'perfectly competitive' markets of economics textbooks. **The test for regulatory intervention is not just the existence of some market failure, but whether the regulator can create a better outcome than the market would do if left unregulated**. To be a better outcome, the regulator must deliver a greater net economic benefit (benefits minus the costs of regulation) to society than the unregulated market.

Recent Australian studies have found several examples of overly heavy-handed regulation to correct perceived market power in markets that are workably, if not perfectly, competitive. Examples include regulating wholesale access to mobile phone services and the direct price regulation of airports. [42]

Another example is the high compliance costs of the Financial Services Reform Act. These stem from an inability of regulators to realise, throughout the consultation, drafting and implementation process, that they will not be able to achieve perfect information flows between suppliers and consumers of financial products.

[42] Banks (2003) *The good, the bad and the ugly: economic perspectives on regulation in Australia*, Address to the Conference of Economists, Business Symposium, October.

The Financial Services Reform Act

The FSR Act aimed to provide greater protection for consumers through financial product disclosure and licensing.

But product disclosure requirements have involved considerable additional set-up costs and ongoing costs, particularly in training staff. And the FSR essentially imposes a 'one size fits all' model, with more detailed disclosure requirements on generic or everyday products now required than was previously the case.

The result is that the new regime provides little benefit to consumers, and often confuses consumers because the verbal product disclosure requirements tell them little more about the product but can leave them more anxious.

And there is no additional protection for consumers as product disclosure still occurred before FSR. Information was sent out following a phone inquiry, but customers could still cancel within a cooling off period.

So what went wrong? To begin with, the Act had an unachievable objective. As financial products become more sophisticated, so does the knowledge needed to interpret product disclosure statements. It also becomes more specialised, so that any attempt to impose a consistent framework across all product types is close to impossible anyway.

Consultation was not always acted upon. The consultations were long and detailed – but many comments from industry seem to have been ignored.

And there was little attempt (by Government or industry) **to estimate compliance costs.**

So where to from here? There are lessons to be learnt on process – the lack of effective consultation, the lack of depth in attempts to understand compliance costs, and the lack of realisation among policymakers that they were trying to do the impossible anyway.

A detailed case study on the *Financial Services Reform Act* is in Appendix B.

4.1.2 REGULATORS ARE OVERLY PRESCRIPTIVE

As Banks[43] notes, unduly prescriptive regulation which sets down subsidiary rather than fundamental objectives as requirements creates a risk that the subsidiary, not fundamental, objectives are met. **Regulators often regulate symptoms rather than causes**.

Perverse outcomes can occur when regulation is overly prescriptive. A 2002 amendment to the Uniform Consumer Credit Code ('the Code') requires credit providers to issue mandatory comparison rates for credit products. Consumer protection regulation, if poorly designed or indiscriminately applied, is more likely to harm than to help consumers. Despite detailed

[43] Banks (2003) *The good, the bad and the ugly: economic perspectives on regulation in Australia*, Address to the Conference of Economists, Business Symposium, October.

regulation including formulae for calculating the comparison rate, and regulating how the rate is presented to consumers **comparison rates are in fact incomparable** and do not achieve the Code's objective to "assist consumers to identify the true cost of credit".

Why? Because the complexity and variety of financial products prevents a simple comparison measure. In the case of the Code, New Zealand is dropping its equivalent regulation because loans can be very complex, while consumers can have poor financial literacy, meaning that mandated comparisons cannot cover the gap between complex products and bewildered investors. Certainly it seems the availability of comparison rates did not translate into increased understanding or change the products purchased (see Appendix C).

4.1.3 REGULATORS TARGET PROBLEMS BETTER SOLVED USING OTHER POLICY INSTRUMENTS

The World Bank and other studies show the greatest returns from regulation come from getting the basics right. Using regulation to favour particular interest groups or to meet social objectives often imposes greater costs than alternative policy instruments.

- That is particularly so when an existing regulation or law is modified to try to achieve a secondary objective. For example, the GST exemption for fresh food undoubtedly increased compliance costs for both government and businesses, compared with a flat rate on all products. It also artificially distorted the relative prices of different foods. The objective of the exemption, to provide tax relief to low-income earners who spend a higher share of their income on basic foods, could have been much more efficiently achieved through changes to income tax or welfare programmes. Such policy alternatives would not have imposed as great a compliance burden on business.
- Similarly, commentators have suggested the current anti-dumping legislation, because it is not limited to cases of unfair competition, operates more as an industry assistance program than a regulation to correct market failures. And it is true that more anti-dumping applications tend to be lodged when the $A appreciates and during downturns in the business cycle. From an economic efficiency standpoint, it would be preferable that the same principles that apply to domestic cases of price discrimination are extended to anti-dumping. A review in 1986 rejected the introduction of a 'national interest' clause as too complex and costly. **But comments from BCA members indicate the current procedures for anti-dumping investigations are already uncertain, complex and costly**.

4.1.4 REGULATORS OVERREACT TO CURRENT HOT ISSUES

There is a temptation to use regulation as the policy instrument of first resort – particularly to get an issue off the front page fast. As government administration costs tend to be the smallest component of regulatory costs, the government is able to regulate away the immediate symptoms of a problem at high, dispersed and, possibly, disguised cost to business and, ultimately, to consumers.

4.1.5 REGULATORS CANNOT ENFORCE THEIR RULES

Regulation that is unenforceable is not effective. There are at least two reasons why regulation may be unenforceable. First, there are some desired outcomes that are unenforceable because the required behaviour is unobserved or very costly to observe. (For example, Singapore has legislated that children must take care of their elderly parents.)

Second, regulation may not be enforceable because the regulator does not have sufficient resources to follow up those instances of breaches that are known or suspected to occur. Regulators may consequently spend their time pursuing 'soft' targets – such as high profile businesses with good records that may have incurred minor breaches of regulations – at the expense of more serious violations by firms that are more costly and difficult to prosecute.

This can create industries with two levels – compliant and non-compliant businesses. That distorts resource allocation, encourages other non-compliant and illegal activity and generates deep dissatisfaction with regulations and disrespect for the regulator.

4.2 OVERLAPPING REGULATION

Productivity Commission Chairman Gary Banks calls this the danger of 'regulatory cocktails' creating adverse and unintended interactions. In Australia overlapping or conflicting regulation can occur:

- **Between different regulatory bodies at the same level of government**. For example, Federal agencies APRA, ASIC, the Reserve Bank and the ACCC share regulatory oversight of banking and financial markets. And these different regulatory bodies can have conflicting objectives.

  For example, Australian Government agencies appear to have conflicting goals and attitudes toward foreign investment:

  - On the one hand, the *InvestAustralia* agency, operating through the Department of Industry, Tourism and Resources, aims to attract and facilitate foreign investment to Australia.
  - On the other hand, the *Foreign Investment Review Board (FIRB)*, operating through the Department of Treasury, adds a regulatory process, stops some foreign investment to Australia from proceeding, and by its mere presence may discourage other investment.

  This would appear to be one area where inconsistent objectives from the same level of government impose both a regulatory burden on business and efficiency costs on the wider economy (see Appendix D).

- **Between levels of government**. For example, new developments may need to comply with planning laws at the Federal, State and local level. A review of Australia's building regulations found "Local Governments usually do not conduct an adequate level of impact analysis of their regulations. New regulations may be introduced that contain extra requirements on business, with increased costs, for uncertain benefit". [44]

- **Between jurisdictions**. For example, workers compensation or OH&S laws differ between States, despite almost identical objectives. This generates extra compliance costs for national firms with no benefits to the community. The Productivity Commission has consistently found benefit in mutual recognition regimes (both domestically and internationally) to harmonise standards and reduce the potential for duplication or inconsistency (see box below and Appendix E).

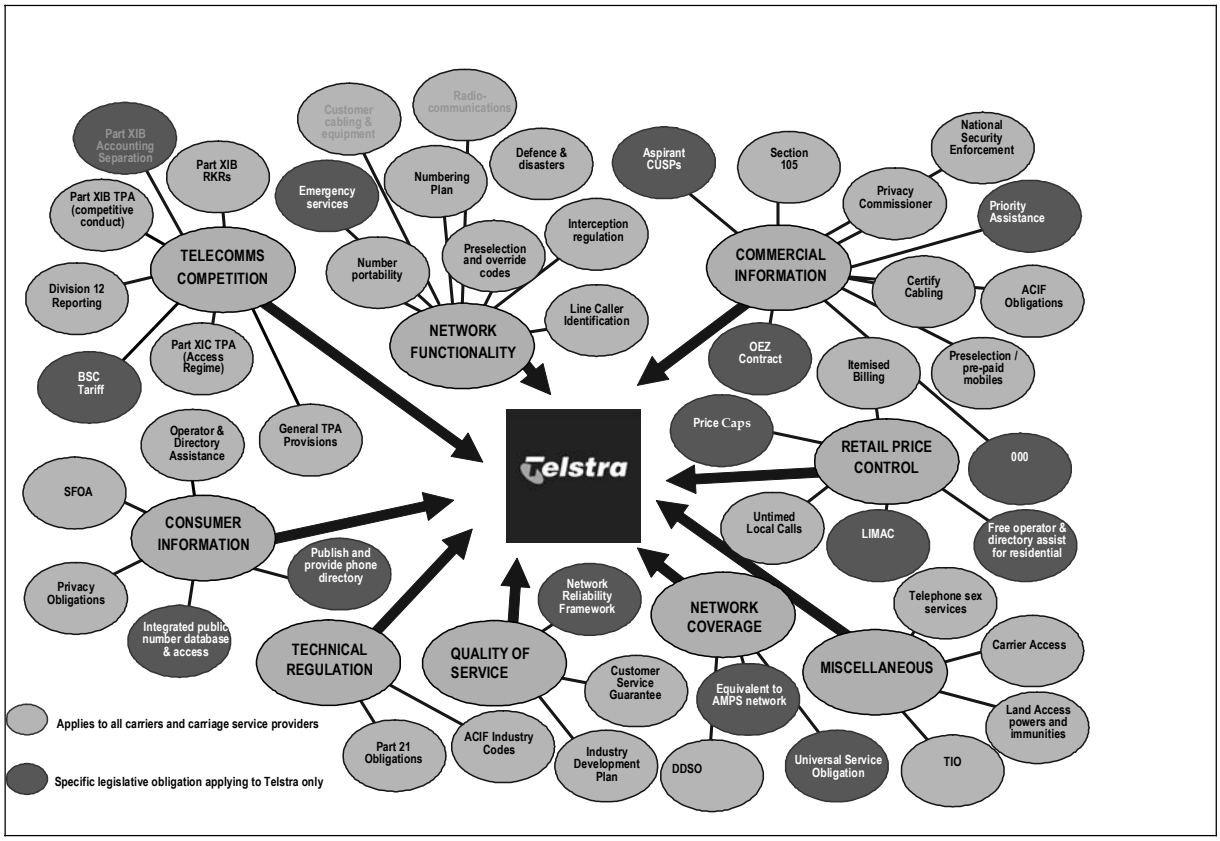
- **Between public and private oversight bodies**. Many industry bodies have a role, formally or informally, in regulating the conduct of their members. Yet the Australian

[44] Productivity Commission (2004) *Reform of Building Regulation* Research Report, Productivity Commission, Canberra, November 2004, p.xxxvii.

Stock Exchange's listing rules sometimes place more onerous corporate disclosure obligations on listed companies that those contained in the Corporations Act. Why so?

Just how bad can the resultant 'regulatory cocktails' get? Take a look at the following chart, which sets out the regulators and regulations Telstra faces.

FIGURE 4.1: SPAGHETTI, ANYONE?



And Telstra is by no means a special case. Many firms have to navigate the compliance nightmare that overlapping regulation creates. Imposing additional costs on business without a commensurate benefit to consumers and society is bad policy and bad regulation, as the Productivity Commission's inquiry in into National Workers' Compensation and Occupational Health & Safety Frameworks showed.

Same Policy, Multiple Versions, Zero Benefit – Australia's overlapping OH&S and Workers Compensation Schemes

There are ten principal Occupational Health & Safety (OH&S) statutes across Australia – one for each State and Territory and two Federal laws dealing with employees in the Federal Government and the maritime industry, respectively.

There are even more workers' compensation schemes, as some States have industry-specific as well as State-wide schemes.

Industry surveys identify the lack of nationally consistent Workers' Compensation and OH&S regulations as a key concern of business. In 2003-04 the Productivity Commission's inquiry into National Workers' Compensation and Occupational Health & Safety Frameworks attracted many

submissions from firms and industry associations canvassing the inefficient effects of nationally inconsistent regimes.

The objectives which underlie OH&S and workers' compensation regimes in each jurisdiction are essentially identical. Differences arise in how each jurisdiction implements these policies. The Productivity Commission found these differences to be substantial, and not merely superficial drafting differences. [45] As well as what is written in the detailed regulations and codes which set out the scheme, there are also differences in how the responsible body exercises its discretion, particularly in relation to enforcement.

Even where principles and policies are consistent, multiple arrangements create extra premium and reporting requirements for national firms, which in itself raises business compliance costs. CSR, a national firm eligible to self-insure for workers' compensation, still needs to obtain a licence to do so in each of the five States and Territories which it operates. It estimated that the ongoing cost of renewing these licences would fall by $500,000 a year (from $700,000 to $200,000) if it had to only maintain and review one 'national' licence. These savings would come from a reduction in administration staff, administration fees and reporting costs. The requirement to report to five different regulators at different times of the year and in different formats was estimated to add $60,000 alone to CSR's total reporting costs. [46]

Other organisations provided estimates of potential cost savings from a national scheme ranging from 5 to 15% of their annual compliance costs. They also identified areas of lost efficiency to the economy, the value of which could not be quantified in dollar terms.

While there are potential benefits from multiple arrangements, including tailoring arrangements to local preferences, or competing and learning between jurisdictions, the Productivity Commission does not appear to have found these benefits to be notable, or that they could only be obtained through the current fragmented system.

4.3 LACK OF CONSULTATION

Those affected are more likely to be aware of the probable costs of compliance and the wider impact of regulations on economic efficiency than legislators or regulators.

The problem with tapping into this expertise is that the affected firms often also have an interest in minimising the impact of the regulations and may overstate the costs. While this is reason to treat claims of high compliance costs with some scepticism, industry will nevertheless have incentives to present relatively unbiased assessments of the relative impacts of alternative means of solving problems, including non-regulatory approaches.

That is, if it is accepted that a particular problem needs to be addressed, industry will have an incentive to ensure that happens with the least compliance cost. While Governments

[45] The Productivity Commission, at p16.

[46] The Productivity Commission, at p20.

should not abrogate their role in assessing the most appropriate form of regulation to those who will be regulated, it should equally not be dismissive of the firms' submissions regarding the practical impacts of various options. Enforcing compliance is easier where the regulator has consulted with industry.

4.4 A LACK OF ONGOING REVIEW

The economy is not static. Regulations can become outdated or less cost-effective than alternative interventions (or deregulation) over time. And as we learn more about the economy and how markets work, new and more effective ways of regulating are developed.

A large part of the success of Australia's National Competition Policy was the requirement to review the anti-competitive elements of existing legislation to identify whether it is still the least-restrictive way to meet public interest objectives. While that was a substantial (and still incomplete) task, the benefits it produced (and is still producing) [47] show the potential gains to be had from careful review of existing regulations.

Review of legislation is not merely an exercise in bureaucratic navel-gazing. There are examples in Australia of regulation which has not been regularly reviewed and updated, to the detriment of the industry and economic growth more widely.

And even where reviews are been undertaken, political will is needed to act on suggested changes. Once regulation is in place, it can be very difficult to generate sufficient momentum and agreement to remove it, despite evidence that the regulation is not meeting its objectives.

Indeed, that is part of the reason why sunset clauses or compulsory review mechanisms can make sense – even though they reduce certainty to business. Once in place, it is much more difficult to remove legislation or regulation, even if a number of independent bodies have criticised its existence.

Consider the case of petrol retailing. For 25 years there have been restrictions on the ability of some large domestic oil refiners to participate in the downstream market for petrol retailing. Under the *Petroleum Retail Market Sites Act 1980* ('Sites Act') a quota is placed on the number of sites a refiner-marketer can operate itself. This quota is based on the refiner-marketer's average wholesale market share. Currently, the four major refiner-marketers (Caltex, BP, Mobil and Shell) can only operate 424 stores between them, out of around 8,370 retail petrol outlets spread across Australia.

The initial rationale for the legislation was to protect small independent petrol station owners from big oil companies. There had been complaints that the large oil companies were abusing their position in the industry through practices such as price discrimination.

In particular, it was argued that the large refineries charged higher wholesale prices to sites owned by lessees and franchisees than to their own company-run stores. The Government of the day feared that greater vertical integration of the industry would have long term, anti-

[47] See Productivity Commission (2005) *Review of National Competition Policy Reforms*, Productivity Commission Inquiry Report No. 33, Canberra, February, p.73-77.

competitive effects.[48] The Sites and Franchise Acts were therefore introduced to limit vertical integration in the industry.

But since 1980 there have been large changes to the petrol retailing industry, and the economy more generally. A review of the industry in 2002 noted the strong tendency towards consolidation in the industry, through mergers, exit of small players, entry of new supermarket chains and an increase in multi-site franchisees.[49]

Economy-wide approaches to dealing with possible sources of market power have also changed over the past two decades. The reach of the Trade Practices Act and the resources devoted to its enforcement have greatly increased. New sections have been added to deal with unconscionable conduct and industry codes. The likelihood of competitors merging has been reduced, with the threshold test of an anti-competitive merger changing from market dominance to that of substantially lessening competition.

These changes have arguably removed the need for the original regulation. And, as a result of these developments, it is possible that the Sites and Franchises Acts may now impede, rather than promote, competition in petrol retailing. The legislation also discriminates in its application, as vertically-integrated firms with refining operations overseas do not face the same restrictions as domestic refiners.

A bill to repeal the Acts was placed before Federal Parliament in 1998, but lapsed. A new bill is expected to be introduced during 2005, but this has only been possible after an intense two year period of negotiation and consultation between the affected parties.

Access Economics
May 2005

[48] Hansard 1980 p.1025 cited in Industry Commission (1994) *Petroleum Products Report No. 40* Australian Government Printing Service, Melbourne, July 1994, p.152 downloadable at http://www.pc.gov.au/ic/inquiry/40petrol/finalreport/index.html

[49] Department of Industry, Tourism and Resources (2002) *Downstream Petroleum Industry Framework 2002* Commonwealth of Australia.

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APPENDIX A: COMPARING AUSTRALIA'S REGULATORY PERFORMANCE

How good are Australia's regulatory practices?

Apart from some partial studies over the years, until recently it would have been impossible to assess Australia against world's best practice with any degree of rigour.

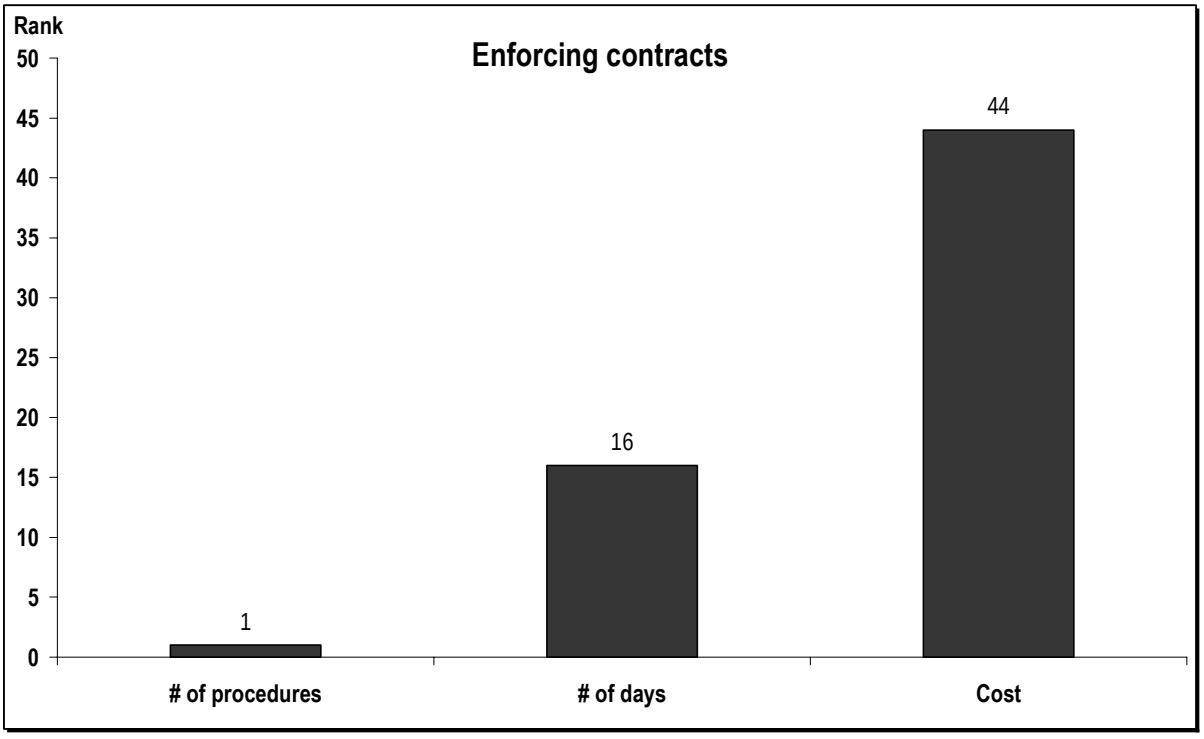
But that is no longer true. The World Bank is now releasing results from a large and on-going study of its membership and the manner in which nations are regulating themselves.

The study considers the regulatory practices of 137 countries.

The following sections consider the specific findings of the Bank, and Australia's global rankings by type of regulation.

A.1 ENFORCING CONTRACTS

Efficiency of the judicial process and courts system encourages investments and business transactions to take place. Too complex a dispute resolution process can influence business perceptions about the fairness of the judicial system in a country and hinder trade. Simplifying debt collection is a key part of reducing costs for businesses and thus more than 18 countries reformed their courts during 2003. Confidence in dispute resolution in a country encourages entrepreneurs to start businesses, and to go to court when things go wrong. A streamlined, simple dispute resolution process reduces costs for businesses and leads to more widely spread efficiencies in the economy as a whole.



In Australia it takes 11 procedures, 157 days and 14.4% of the debt in terms of costs to enforce a contract. Although Australia ranks number 1 in terms of the number of procedures it takes to enforce a contract, the number of days taken ranks poorly (16th) against countries such as France (75 days), Japan (60 days), New Zealand (50 days) and Norway (87 days).

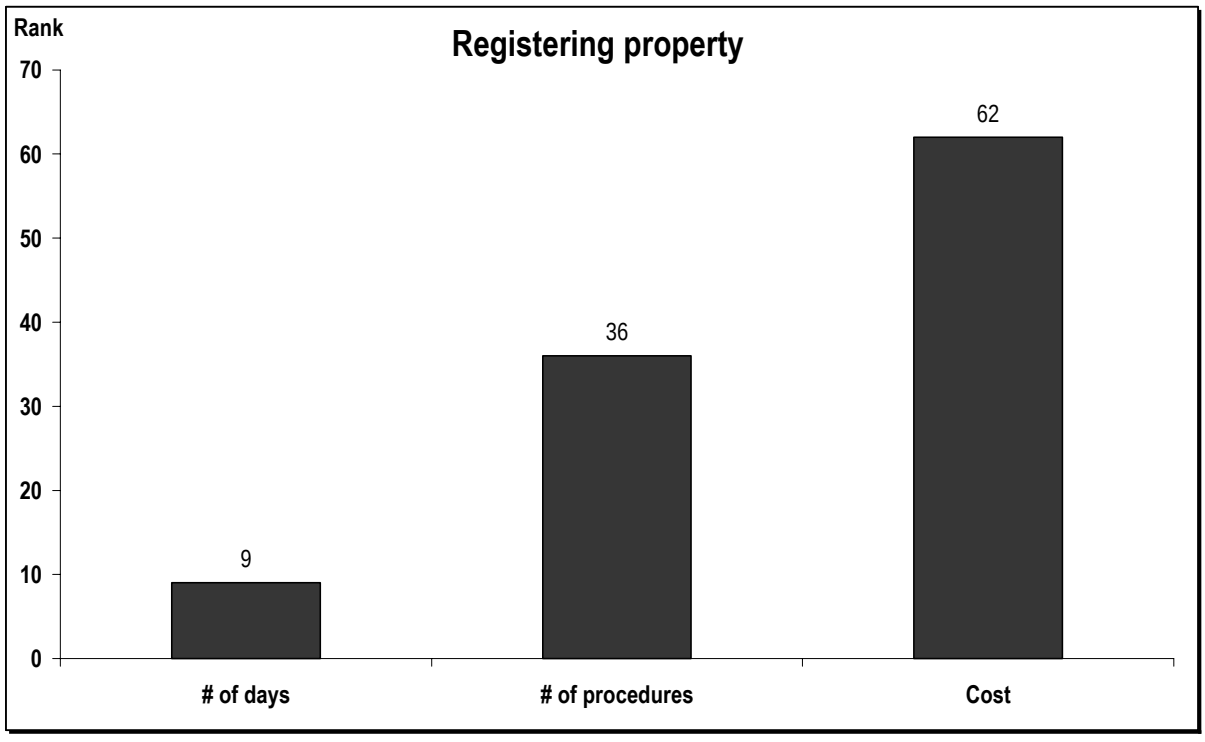
The costs of enforcing a contract in Australia are also relatively high (with a ranking of 44th) when compared with Japan, New Zealand, Norway, Sweden and the US, which all have costs under 10% of the debt.

A.2 REGISTERING PROPERTY

The World Bank finds that "Productive businesses thrive where government focuses on the definition and protection of property rights" – but not via the heavy handed regulation of those rights. Too complex a system of property rights can burden business unnecessarily. A system that is too stringent can create uncertainty, increase corruption and fraud and place undue transaction cost pressures on businesses.

Although Australia generally performs well in defining property rights, several countries have fewer procedures to register a property than the five that it takes here. In Germany registering a property takes four procedures, in the UK it takes four, in New Zealand and the US it takes two, and in Norway and Sweden, just one procedure.

The time take to register property in Australia is seven days, while in NZ and Sweden it takes only two, and in Norway it takes just a single day. In Australia the process of registering a property costs some 4.5% of the value of the property, leading us to be ranked 62nd in the world on this indicator. The likes of Germany (4.2%), Japan (4.1%), NZ (0.2%), Norway (2.5%), Sweden (3%), US (0.5%) and the UK (4.1%) all have lower costing procedures.



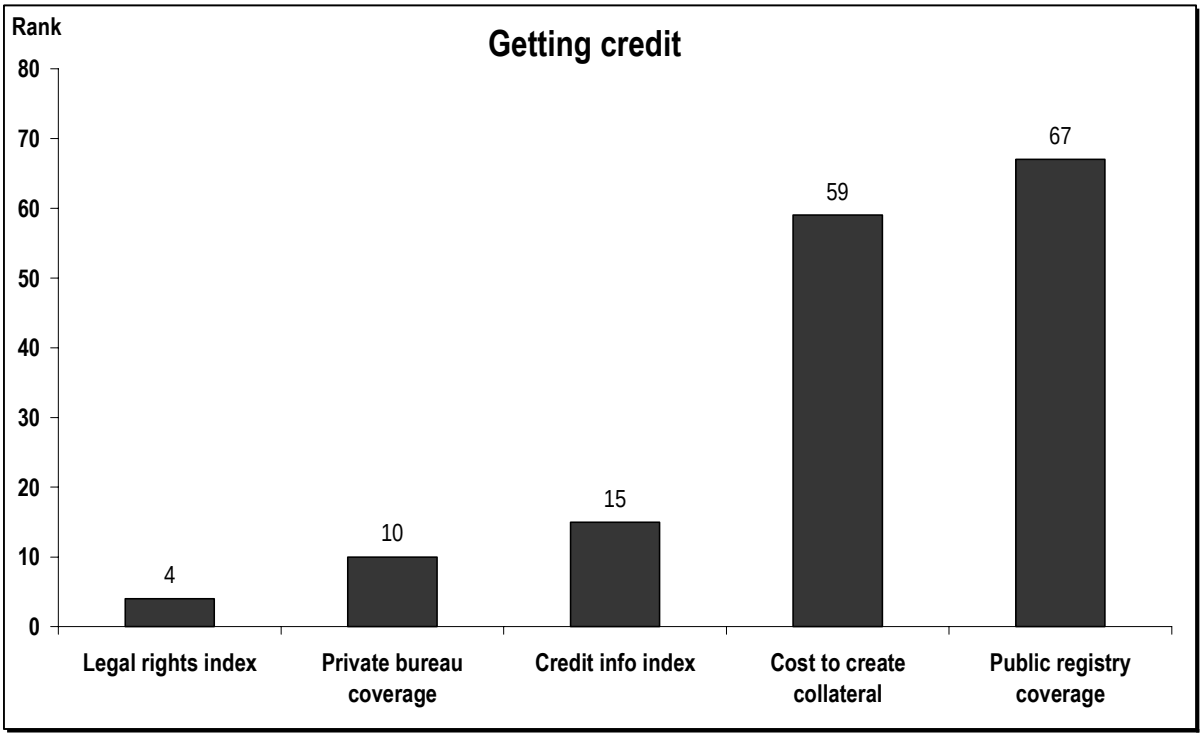
A.3 GETTING CREDIT

An essential building block of businesses today is access to credit. Without a formal register of credit information, appropriate legal rights of borrowers and lenders and a sufficiently low cost basis on which to create collateral, businesses will suffer. Improving the level of credit information available in a given country aids debtors as well as creditors and ensures that finance goes to the most productive and efficient businesses.

The World Bank found that those countries which have stronger legal rights have a smaller number of loan defaults, while businesses are less likely to report credit constraints, and loans tend to come with cheaper lending rates.

Australia performs well on the Legal Rights and Credit Information indexes (4th and 15th respectively) although countries such as Hong Kong, Singapore and the UK all achieve 10/10 on the former index and Germany, Japan, the UK and the US score 6/6 on the latter.

The cost to create collateral in Australia is 5.5% of income per capita. That is by no means the highest cost of any country, but does leave us ranked 59th in the world. Our cost to create collateral is bettered by most developed nations (such as France at 0.5%, Germany at 0%, Japan at 2.7%, NZ at 0.8%, Norway at 0.5%, the UK at 0.1% and the US at 0.1%).



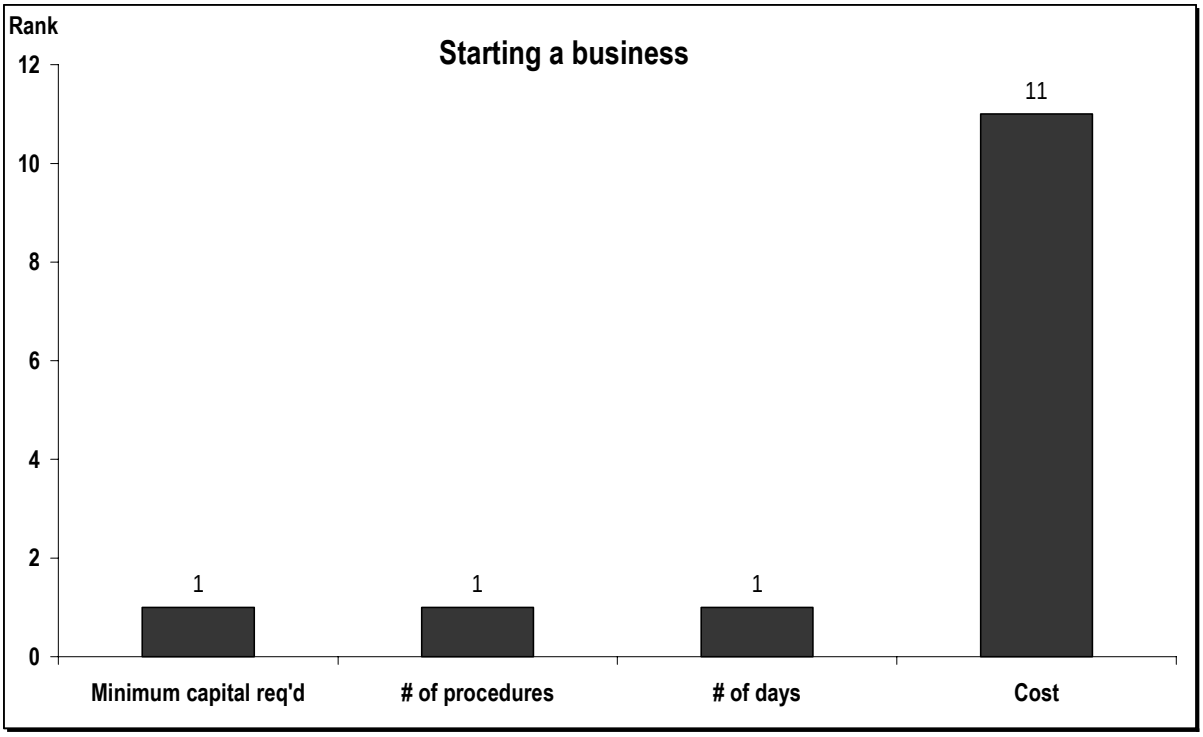
A.4 STARTING A BUSINESS

There are four measures in this category of regulation, and Australia has world's best practice on three of them – time taken (two days), number of procedures (two) and minimum capital required (0% of income per capita).

That's great. But there is room for improvement on the costs of starting a business, with 2.1% of income per capita required in Australia to start a business here. That can be compared with the many countries which charge significantly less than this (such as New

Zealand with a cost of 0.2% of income per capita, France at 1.1%, Sweden at 0.7%, the UK at 0.9%, and the US at 0.6%).

If starting a business proves too difficult, costly or time consuming, there is strong incentive for would-be entrepreneurs to operate in the black economy. And if that happens, then taxes aren't paid, credit is hard to get, products are not subject to quality controls, and corruption thrives. In short, many of the potential benefits that good regulation can provide are lost.



A.5 CLOSING A BUSINESS

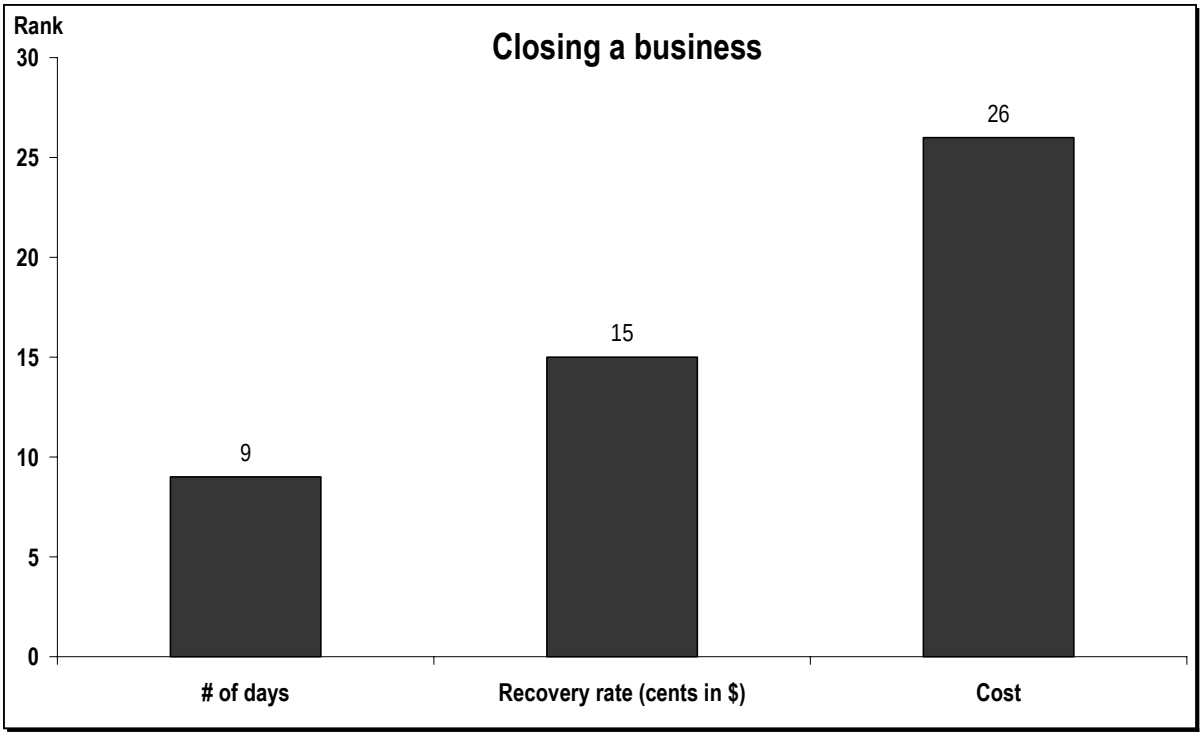
There are a variety of incentives to make closing a business easier. Efficient insolvency procedures lead to higher recovery rates in the event of closure – which means banks are more willing to lend and thus entrepreneurs are more likely to engage in business start ups. This link between closure and start up of business is not as illogical as it may seem on first glance. Indeed, it is the true enactment of Schumpeter's notion of creative destruction at work whereby new businesses replace the older, less efficient and less productive ones.

Reforms that have been seen to work in developed and developing countries alike include reducing the appeals that suspend the bankruptcy process, introducing or tightening time limits of procedures, establishing specialisation in dealing with bankruptcy cases and setting incentives for the administrator to get the most from the estate. In Australia the most prevalent mechanism to close a business is foreclosure, but a spectrum of exit options exist. Recently, Australia has instituted streamlined procedures for the liquidation of companies which lack sufficient assets to complete a regular procedure. But there is still more that can be done.

Relevant indicators to measure the ease of closing a business include the time taken, the cost as a share of the estate and the recovery rate (expressed as cents in the dollar) of a debt. Australia scores reasonable well on the time taken (1 year) being bettered by only eight countries including Japan (0.5 years), Norway (0.9 years) and Canada (0.8 years).

The associated costs of closing a business in Australia amount to 8% of the estate – a figure which is high when compared with the UK at 6%, New Zealand and Japan at 4% and Norway at just 1%. Australia's ranking on this indicator is 26th.

Finally the recovery rate in Australia (ranking 15th) is higher than that in the US (68.2 cents) and New Zealand (71.4 cents) but lower than the UK (85.8 cents), Norway (87.9 cents) and the very high rate in Japan of 92.4 cents in the dollar.



A.6 HIRING AND FIRING

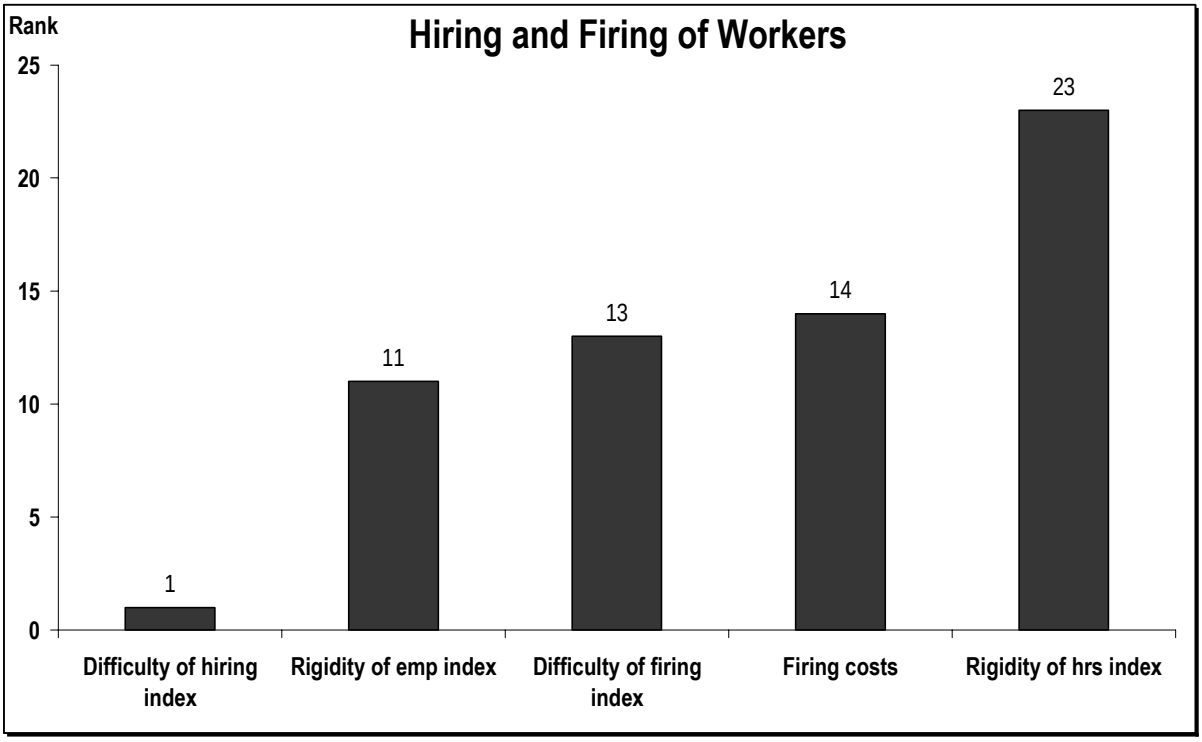
The ease with which companies can hire or fire workers affects (1) employment decisions, (2) the degree to which employees are hired through the informal economy and therefore (3) the growth and productivity prospects for the wider economy.

So there are benefits to be had from reforming hiring and firing regulation. Among other things, foreign investment has been found to suffer under too restrictive job regulations. AT Kearney (2004) found restrictive job markets were the third most commonly cited reason against foreign direct investment after high corporate taxes and corruption.[50] Restrictive regulation also prevents firms from changing with broader economic shocks and changed global conditions. As a country liberalises, enterprises must be flexible in hiring and firing in order to remain competitive on a global scale and thereby reap the rewards of globalisation.

Australia has world's best practice in terms of difficulty of hiring of workers. However, our overall rank of 13th in the world on the difficulty of firing index leaves room for improvement because 'barriers to firing are barriers to hiring'. In Australia, firing costs amount to 17 weeks worth of pay. In New Zealand, this cost is zero, in Norway it is equivalent to 12 weeks, in the

[50] AT Kearney (2004), *Measuring Globalisation,* Arlington Virginia.

US, 8 weeks. The rigidity of hours index shows Australia ranked 23 in the world with a score of 40 (the highest score being 100). Several countries, including Canada, the US and New Zealand, scored zero for this indicator.



A.7 PROTECTING INVESTORS

The World Bank notes four types of disclosure that protect investors: information on family, indirect and beneficial ownership, and on voting agreements between shareholders.

Further, two types of financial disclosure help investors: the business can have an audit committee to review and certify financial data, and the law may require an external auditor.

Finally, to be most effective, financial and ownership information should be available to all current and potential investors. These factors sum to give the disclosure index.

Protection of investors is important to encourage business growth and productivity while discouraging expropriation. The World Bank has found that in countries with a higher risk of expropriation the size of investment is half that in countries with good investor protections.

So making Australia's investor protection regulation the most efficient and effective possible will enhance investment here, and therefore output growth and economic efficiencies.

Australia scored a high 6 on this index. However, the UK, the US, Spain and Israel topped the list with a score of 7. So, overall Australia's ranking on the world scale is not too bad – but there remains some room for improvement.

APPENDIX B: THE FINANCIAL SERVICES REFORM ACT: WHAT WENT WRONG?

This section presents a short analysis of the *Financial Services Reform (FSR) Act 2001*. It examines problems with the Act in practice and the process of generating the FSR Act to provide lessons for the future.

The objective

The *Financial Services Reform (FSR) Act 2001* was introduced with the aim of improving the integrity and efficiency of the Australian financial system, and providing greater protection for consumers. The Act sought to address the findings of the 1997 Financial System (Wallis) Inquiry that, in some cases, inadequate disclosure was preventing consumers from making well-informed and efficient investment choices. Key elements of the Bill were:

- Financial product disclosure – standardising information disclosure rules across financial products and services as a protection for consumers (also meant to benefit industry from consistent standards).
- Licensing – establishing a single licensing regime of minimum standards for financial services providers (also meant to benefit industry by having one licence rather than multiple licences for different financial services).

Problems in practice

The problems of the Act in practice were noted by various financial service providers whom Access Economics interviewed. They reflect general industry discontent of significant additional costs for dubious benefit to either industry or consumers. Key issues include:

- Product disclosure requirements have involved considerable additional set-up costs and ongoing costs, particularly in training staff to adhere to imposed requirements.
  - At one institution new call centre operators and bank tellers get 12 hours training on their obligations under the FSR Act in the first 3 to 4 months of work, and then another 4 hours a year in recurrent training. This is atop compliance training required to meet other regulation, and employees who give more detailed financial planning advice will have a much larger FSR training load as well.
- FSR essentially imposes 'one size fits all' requirements. It does so by imposing more detailed disclosure requirements on generic or everyday products than was previously the case. A more flexible approach could achieve better outcomes as financial products and services are not uniform.
- The result is that more detailed product disclosure explanations are now required for some basic deposit products and all basic insurance products, such as home, contents and motor vehicle policies, which tend to be reasonably well understood by consumers and involve relatively low levels of financial risk. And large companies in particular want to make sure that they dot every 'i' and cross every 't' – the resultant conservative interpretation of the requirements of the Act therefore sees financial institutions reissuing complete sets of documentation for minor changes to products such as increases in insured values in existing policies or reinvestment of term deposits because these are classed as 'new' products.
- Whole forests of trees are dying to little purpose here.

- For insurance, the FSR requirements suggest that insurance companies are providing financial advice. However, major insurance companies have a 'no advice' model for their sales people (that is, company policy is to offer no personal financial advice) as the cost implications of providing personal advice are prohibitive. It could be argued that consumers are now in fact receiving lower standards of service from financial institutions, as they must wade through detailed product disclosure statements, and draw their own conclusions about interpretation, rather than obtain clarification from a sales person about the product.
- "Advice" such as insurers asking "have you considered sufficient cover for jewellery, replacement cover?" should not be subject to the same kind of training obligations and accreditation as "advice" where the customer is putting life savings at risk in a managed fund (again, a lack of flexibility is evident).
- The new regime appears to provide little benefit to consumers, and often confuses them as verbal product disclosure requirements tell them little more about the product yet can leave them more anxious.
- There is no additional protection for consumers. Product disclosure still occurred before FSR. Information was sent out following a phone inquiry, but customers could still cancel within a cooling off period.
- Some companies who sell insurance as incidental to their main business (car dealers, transport companies, travel agents) also have to fulfil detailed licensing requirements to be authorised representatives. Such requirements can be a significant cost and could be avoided by having a standard Financial Services Guide from the insurer which sets out general details.
- The industry has noticed that some financial service providers are increasing minimum investment levels as a result of the increased compliance costs and time needed per transaction to fulfil disclosure requirements. Smaller investors may now have a reduced choice of financial products because these higher fixed costs cannot profitably be recovered without higher up-front fees or lower on-going rates of returns.
- FSR has failed to do away with multiple licenses. FSR was designed to provide a single set of licensing requirements, but a number of other Acts (such as the Insurance Conducts Act and the Banking Act) remain in force and impose different requirements. The industry still needs to answer to both APRA and ASIC on a number of issues, while State regulatory bodies are also involved in a number of areas.
- One financial service provider has estimated FSR licensing requirement imposed an initial cost of $30 million and an ongoing cost of $10 million a year on it. Suncorp-Metway's experience of the financial services licensing requirement was that it involved five staff full time for several months to prepare and provide necessary documentation. They have seen no evidence of other licensing requirements having been streamlined.

What went wrong? To begin, the Act had an unachievable objective

The faster-paced the industry, and the more complex the products it sells, the greater the risk that regulation dates (and goes bad) – so the greater the caution with which regulators should proceed.

The requirements of the FSR Act came into force in March 2004 – seven years after the release of the Wallis Inquiry and five years since the CLERP 6 consultation process began. During these years there was growing product differentiation. At the same time, Australians amassed larger superannuation savings. And interest in the sharemarket among 'retail'

investors leapt amid the privatisation, demutualisation and listing of large companies such as Telstra and NRMA Insurance and high returns to equity over the 1990s.

With more products and consumers, regulators turned to greater disclosure requirements, seeing them as necessary to protect those consumers.

But it is unlikely that disclosure requirements, however prescriptive, can of themselves help consumers make effective investment choices. As financial products become more sophisticated, so does the knowledge needed to interpret product disclosure statements. It also becomes more specialised, so that an attempt to impose a consistent framework across all product types is inappropriate. This aligns with industry complaints that *the drive for consistency at the expense of flexibility has led to large amounts of unnecessary and confusing documentation* being issued with simple financial products.

Consultation was not always acted upon

The FSR Bill was tabled with a Regulation Impact Statement (RIS). That Statement notes:

> *Following the release in March 1999 of the CLERP 6 Consultation Paper, an extensive public consultation process took place. The Minister for Financial Services and Regulation met with key stakeholders representing the interests of consumers, financial service providers and financial markets. In addition, Treasury and the Minister's office held public consultations in Sydney, Melbourne, Brisbane, Adelaide, Perth and Darwin, with over 400 interested parties. More than 120 submissions were received in response to the Paper, and officers of the Treasury have participated in over 80 meetings with stakeholders.*
>
> *The consultation process in relation to the draft FSR Bill commenced upon the release of the Bill to the public on 11 February 2000. Treasury received over 100 submissions in response. Targeted consultation sessions with stakeholders were conducted in April 2000, and representatives from approximately 30 interest groups attended these sessions. Feedback from stakeholders represented at the round-table consultations was largely positive, although a number of refinements to the draft legislation were suggested. These suggestions have been taken into account in the final drafting of the FSR Bill.*

Critics of the Act cannot argue that it was rushed through or there was no opportunity to comment – effectively there was a two year consultation process before the Bill was tabled in 2001.

Yet there are clearly genuine concerns about the costs to business of the end result.

At issue is the willingness of regulators to make changes on the basis of consultations. Consultations where government and regulators are not prepared to listen and which cannot result in any change serve no useful purpose – they become a massive waste of resources in themselves.

It appears that some changes were made to the FSR Bill through the consultation stage, but the FSR Bill was politically driven to have some result achieved (the options of abandoning the Bill, or undertaking major re-working of it, were not feasible). Once a political decision has been made to introduce a policy, there may be a tendency to focus on legalistic issues of drafting rather than the practical effects of the law.

There was little attempt to estimate compliance costs

Another failure of the process before the Bill was implemented appears to be a lack of any examination of the issues in cost-benefit terms.

The RIS is rather scant in its discussion of the costs to business of the Bill. There is no attempt to quantify these so they can be compared with the expected broader benefits to be provided to consumers. Nor does there appear to have been material provided in the background papers which attempted to quantify the costs, even for a typical business.

By the same token, business doesn't appear to have made government acutely aware of the potential compliance costs of the Bill in quantitative terms through the consultation process. Some financial institutions claim many of the costly side-effects of the FSR Act were not foreseeable until it was implemented.

Such assessments are difficult, but an attempt by either government or stakeholders to quantify compliance costs may have focused attention on the scale of the potential costs, and a more sober assessment of those against the benefits. Assumptions necessary to generate a 'back of the envelope' calculation could have been set out clearly and debated.

Within government the ORR can offer guidance in making RIS cost-benefit assessments, though agencies still require their own skilled staff to perform them. These staff also need a firm understanding of the structure and practices of the industry they are regulating. *A criticism from banks is that bureaucrats and politicians often do not and are not willing to consider the processes necessary to implement a new regulation*. In the case of the FSR Act, business had to lobby intensely for a longer transition period. There was reluctance on the part of regulators to agree that investigation, implementation and documentation of the necessary systems and procurement changes would take a long time to occur.

Where to from here?

Regardless of the process to date (lack of consultation, lack of awareness of the consequences by stakeholders, or a change in the economic environment), a bad Bill (with notable costs against dubious benefits) is a bad outcome, and the economy could benefit from having a process in place to review such outcomes.

A process to review legislation where there is widespread discontent with the resulting impacts would make sense as part of regulatory reform. That may apply to legislation as a whole, or perhaps just some elements (which come to light as onerous after implemented). Such a review might also allow some of the costs and benefits stated in the RIS to be tested in fact.

A concerted lobbying effort from business may yet lead to some changes in the FSR Act. There were already amendments made during 2004 to deal with some of the more onerous or unclear provisions of the initial FSR Act. Further regulation and ASIC policy guidelines are expected to clarify other issues. However, such piecemeal amendments may alleviate particular pressure spots, but will not address the more fundamental question – does imposing detailed disclosure requirements on financial service providers lead to better informed consumers and a more efficient financial services market?

APPENDIX C: THE INCOMPARABILITY OF MANDATORY COMPARISON RATES

The Uniform Consumer Credit Code ('the Code') has been adopted into law by each of the eight States and Territories. In 2002 an amendment was made requiring credit providers to publish a mandatory comparison rate for any fixed term consumer credit product they offer. The explanatory paper which accompanying the amendment stated that:

> *Since the introduction of the Code in 1996, lenders have introduced a range of different fees and charges on consumer loan products. The combination of fees and charges and interest rates has made it increasingly difficult for consumers to compare the cost of credit between different lenders and different products.* [51]

The object of mandatory comparison rates is to "assist consumers to identify the true cost of credit offered by credit providers". [52] The Act, and associated regulations, contain detailed prescriptions about how the comparison rate must be calculated, and how it is communicated to consumers. The method of calculating is set down in regulation, and replicated below.

'(3) The comparison rate is given by the following formula—

$$i = n \times r \times 100\%$$

where—

"**n**" is the number of repayments per annum to be made under the credit contract (annualised if the term of the contract is less than 12 months), except that—

(i) if repayments are to be made weekly or fortnightly—n is to be 52.18 or 26.09, respectively; and

(ii) if the contract does not provide for a constant interval between repayments—n is to be derived from the interval selected for the purposes of the definition of j mentioned below.

[51] Consumer Credit (Queensland) Amendment Bill 2002 Explanatory Notes, p.2

[52] Consumer Credit (Queensland) Act 1994, section 146A(1)

"r" is the solution of the following—

$$\sum_{j=o}^{t} \frac{A_j}{(1+r)^j} = \sum_{j=o}^{t} \frac{R_j + C_j}{(1+r)^j}$$

where—

"j" is the time, measured as a multiple (not necessarily integral) of the interval between contractual repayments that will have elapsed since the first amount of credit is provided under the credit contract, except that if the contract does not provide for a constant interval between repayments an interval of any kind is to be selected by the credit provider as the unit of time.

"t" is the time, measured as a multiple of the interval between contractual repayments (or other interval so selected) that will elapse between the time when the first amount of credit is provided and the time when the last repayment is to be made under the contract.

"Aj" is the amount of credit to be provided under the contract at time j (the value of j for the provision of the first amount of credit is taken to be zero).

"Rj" is the repayment to be made at time j.

"Cj" is the fee or charge (if any) payable by the debtor at time j in addition to the repayments Rj, being a credit fee or charge (other than a government fee, charge or duty) that is ascertainable when the comparison rate is disclosed (whether or not the credit fee or charge is payable if the credit is not provided).

Source: Consumer Credit Regulation 1995 section 33F

The key features to note of this comparison rate formula are:

- the credit provider is only required to include fees and charges that are ascertainable when the comparison rate is disclosed;
- some fees, such as government fees and charges, are not included; and
- in some cases, the credit provider decides the time period over which it assumes repayments are made.

These features are presumably necessary to ensure the calculation of a comparison rate is feasible over a wide variety of possible loans, including honeymoon rates, early repayment options and variable/fixed rate combinations. It also means that the comparison rate really only shows the consumer the 'true' cost of credit in that lenders cannot artificially reduce the headline interest rate of a loan by including large establishment fees. However it does not allow consumers to readily compare loans with differing exit fees or interest rate schedules.

The positioning and prominence of a comparison rate is also regulated. A comparison rate must be no less prominent than any annual percentage rate or repayment amount stated in the advertisement. [53] In electronic media, the comparison rate and warning statement must generally be given in the same manner (text or speech) as the annual percentage rate. [54]

The comparison rate must also be accompanied by a warning advising the consumer that the comparison rate has been calculated on a specific example and may change if the terms of the loan change, including whether the loan is repaid earlier than anticipated.

[53] Consumer Credit (Queensland) Act 1994, section 146I(2).

[54] Ibid, section 1461(3).

The requirement to publish comparison rates began on 1 July 2003. The mandatory comparison rate requirement has a three year sunset clause. [55] It is not yet clear what form of review will be undertaken prior to that date to decide whether the regulation should continue. What is also unclear is whether mandatory comparison rates do indeed help consumers to compare different loan products.

A similar scheme of comparison rates will be repealed in New Zealand as of April 2005 because it was not meeting its objective. The 2001 NZ review concluded that effective consumer protection cannot rely on disclosure of comparison rates alone, due to the complexity of modern credit products and the poor financial literacy of consumers.

Many of the problems with comparison rate schemes identified in NZ are also seen here – the comparison rate is not suitable for flexible or complex lending products and the rate is produced on a nominal, rather than real basis, so the opportunity cost of interest paid is not included. Moreover, regulation cannot deal with all possible examples without becoming unwieldy, but where situations are not covered there is a lack of consistency among lenders.

Perhaps most damning of all is that there is little evidence that consumers understand how to use comparison rates. [56] Awareness of comparison rates did not translate into increased understanding of their objectives, nor did it alter transaction behaviour. This suggests the requirement to publish comparison rates in particular formats so as to increase consumer awareness of them, will not by itself allow consumers to understand its significance.

Research suggests that understanding of comparison rates depends on a person's level of education, their age and geographic location, as well as the extent of their information search. No Australian research has yet been undertaken, although Consumer Affairs Victoria is funding a study into the effectiveness of mandatory comparison rates under the Code. This study is expected to be completed at the end of 2005. [57]

A RIS was not produced to accompany the regulatory amendments introducing mandatory comparison rates. This was despite advice from the Office of Regulation Review that a RIS was required under COAG guidelines.[58] If a RIS had been prepared, it may have caused policymakers to consider the likely benefits and costs of the mandatory comparison rate model, as opposed to other options such as investor education.

[55] Consumer Credit (Queensland) Act 1994, section 146D.

[56] NZ p34-35.

[57] http://www.sisr.net/cag/projects/mandatory.htm.

[58] National Competition Council (2004) *2003 National Competition Policy Assessment* p.B.8.

APPENDIX D: THE INCONSISTENT OBJECTIVES OF FOREIGN INVESTMENT REGULATORS

Australia's financial sector has historically been characterised by heavy handed regulation, with interest rate controls and excessive prudential reserve requirements causing banks to ration finance, and spawning the growth of the non-bank lending sector. Gary Banks highlights some of the problems in tight government controls over the financial sector:

> *"Prior to financial deregulation, an interest rate cap was imposed as a measure to assist small business. However, the cap made lending to small business less attractive to banks, given the relative risks involved. The result was reduced credit availability for those groups, undermining the goal of the measure. Generally, price ceilings imposed on suppliers who are free to alter supply will have perverse, or at least unexpected, consequences."* [59]

Reforms through the 1980s and 1990s opened up the sector and reduced business costs in obtaining finance. The results of that process included strong productivity growth over the past decade in the finance and insurance industry itself, and a contribution to Australia's overall strong productivity growth performance.

The operation of the Australian financial sector is a success story in reducing regulation.

Of course, prudential controls over financial institutions still need to be maintained.

But concern appears to be building in the Australian business community about the risk of **creeping re-regulation of the financial services sector**. Financial sector participants in the Commonwealth Treasury Business Liaison Program report that the cost of meeting financial sector requirements had increased three- or four-fold over the past three years. [60]

Given these recent additional regulatory burdens on the financial services sector, there appears to have been relatively little documented on the compliance costs to business.

A related important component of finance and investment is the **attraction of foreign investment** to Australia. The standalone benefits of foreign direct investment are easily exaggerated. That said, a key component of the benefits associated the Australia-United States Free Trade Agreement, as modelled by CIE, stemmed from investment liberalisation. While the degree of response is open to debate, the report notes:

> *"By lowering the barriers to foreign direct investment, the equity risk premium associated with investing in Australia is likely to fall, thereby lowering the cost of capital in Australia and boosting investment."* [61]

[59] Banks, G (2003), *The good, the bad and the ugly: economic perspectives on regulation in Australia*, p.7.

[60] Treasury (2004) *Key themes from the Treasury Business Liaison Program – April 2004*, Treasury, Canberra, April.

[61] Centre for International Economics (CIE) (2004), *Economic analysis of AUSFTA*, p.ix.

So there are clear benefits to the free flow of financial and investment capital. Economic modelling conducted in McKibbin [62] examined a scenario of restricted foreign investment, stylised by an increase of 1 percentage point per annum in the real return required by foreign investors in Australia. This modelling suggested a corresponding reduction in the level of Australia's GDP over the long term of around 1%.

Such losses can arise because foreign investment flows are mobile and responsive to the economic and regulatory environment. The Productivity Commission [63] found that foreign investment responds significantly to the non-trade provisions of preferential trading arrangements, with net investment creation (though there was a lack of response of foreign investment to bilateral investment treaties).

Having foreigners wanting to invest in Australia is a vote of confidence in the Australian economy. However, foreign companies who do wish to invest can be faced with a series of regulatory hurdles, at all levels of government. These can be daunting for companies unfamiliar with the Australian business environment (even if they are familiar with bureaucratic process in their home countries).

Moreover, this is another example of regulating symptoms rather than causes. In brief, Australians spend more than they earn, and this nation runs a current account deficit as a result. Because we run a current account deficit, we by definition run a capital account surplus – meaning that we rely on financing from the rest of the world.

The latter means one of two things – either net foreign debt goes up, or net foreign ownership of Australian assets (land or buildings or mines or shopping malls or tollways or shares in previously Australian-owned corporations) goes up. Therefore, when we regulate foreign investment in Australia, we are regulating a symptom (the financing of Australia's capital account surplus) rather than understanding the cause (our current account deficit).

Regulating foreign investment in Australia can only reduce that investment (and mean either extra foreign debt – the mathematical equivalent – or weaker Australian economic growth).

Have regulators ever explained that to ordinary Australians? Confusion may be heightened by an apparent ambivalent attitude of the Australian Government towards foreign investment:

- On the one hand, *InvestAustralia* operating through the Department of Industry, Tourism and Resources, aims to attract and facilitate foreign investment to Australia.
- On the other hand, the *Foreign Investment Review Board (FIRB)*, operating through the Department of Treasury, adds a regulatory process, stops some foreign investment to Australia from proceeding, and by its mere presence may discourage other investment.

This is one area where inconsistent objectives from the same level of government impose regulatory burdens on business and efficiency costs on the wider economy.

[62] McKibbin (1996) *Quantifying APEC Trade Liberalization: A Dynamic Analysis,* Australian National University and the Brookings Institution, March 1996.

[63] Productivity Commission (2003) *The Trade and Investment Effects of Preferential Trading Arrangements – Old and New Evidence*, Staff Working Paper, Productivity Commission, May 2003.

APPENDIX E: A LACK OF CONSISTENCY IN WORKERS' COMPENSATION OR OH&S REGULATIONS

There are ten principal Occupational Health & Safety (OH&S) statutes across Australia – one for each State and Territory and two Federal laws dealing with employees in the Federal Government and the maritime industry, respectively.

There are even more workers' compensation schemes, as some States have industry-specific as well as State-wide schemes.

Industry surveys identify the lack of nationally consistent Workers' Compensation and OH&S regulations as a key concern of business. Commonwealth Treasury notes [64] many comments from national firms that the diversity of OH&S regulation and workers' compensation schemes across States notably raised compliance costs. Workers' compensation costs were also the dominant workplace relations concern for employers responding to a 2004 survey.[65]

In 2003-04 the Productivity Commission's inquiry into National Workers' Compensation and Occupational Health & Safety Frameworks attracted many submissions from firms and industry associations canvassing the inefficient effects of nationally inconsistent regimes.

The objectives which underlie OH&S and workers' compensation regimes in each jurisdiction are essentially identical. The schemes also include many common elements and policies, especially at a higher level. Differences arise in how each jurisdiction implements these policies. For example, all jurisdictions operate a compulsory, no-fault workers' compensation scheme, yet each has different rules on access and coverage, benefit structures, injury management processes and the like. [66] The Productivity Commission found these differences to be substantial, and not merely superficial drafting differences. [67] As well as what is written in the detailed regulations and codes which set out the scheme, there are also differences in how the responsible body exercises its discretion, particularly in relation to enforcement.

Even where principles and policies are consistent, multiple arrangements create extra premium and reporting requirements for national firms, which in itself raises business compliance costs. CSR, a national firm eligible to self-insure for workers' compensation, still needs to obtain a licence to do so in each of the five States and Territories which it operates. It estimated that the ongoing cost of renewing these licences would fall by $500,000 a year (from $700,000 to $200,000) if it had to only maintain and review one 'national' licence. These savings would come from a reduction in administration staff, administration fees and reporting costs. The requirement to report to five different regulators at different times of the year and in different formats was estimated to add $60,000 alone to CSR's total reporting costs. [68]

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[64] Treasury (2004) *Key themes from the Treasury Business Liaison Program – April 2004*, Canberra, April.

[65] Australian Chamber of Commerce and Industry (2004) *ACCI Review No. 112* ACCI, Canberra, June, p.7.

[66] The Productivity Commission, at p xxxi.

[67] The Productivity Commission, at p16.

[68] The Productivity Commission, at p20.

Submissions to the Productivity Commission inquiry into National Workers' Compensation and OH&S Frameworks could not identify the total cost increment due to inconsistent State-based regimes, but many firms could quantify the impact of duplication and inconsistency on particular aspects of their compliance program. For example, Insurance Australia Group estimated the systems costs were the largest direct cost of multiple arrangements. These added $10.1 million to the initial cost of setting up a national IT platform and around $1.7 million a year in recurrent IT costs.[69] These recurrent costs are incurred because IAG assumes that the frequency of changes to a national regulatory framework would be significantly less than the total number of changes made by the State-based schemes.

Other organisations provided estimates of potential cost savings from a national scheme ranging from 5 to 15% of their annual compliance costs.

They also identified areas of lost efficiency to the economy, the value of which could not be quantified in dollar terms. The opportunity cost of internal safety management staff time spent on training and researching jurisdictional differences in law may be that less time spent on other areas of their job which generate greater benefits in terms of preventing injuries. Alternatively, firms could redirect these labour resources to other areas of the organisation and increase production and profitability without any reduction in safety standards.

Compliance costs of multiple arrangements are borne unequally between firms. Most firms and their employees are located in a single jurisdiction, so multiple arrangements do not affect compliance costs. Firms which operate in more than one jurisdiction represent less than 1% of all businesses, yet account for around 30% of jobs. [70]

There are potential benefits from multiple arrangements, including:

- a greater ability to tailor arrangements to the preferences of local residents, workers and firms;
- an ability to learn from 'best practice' innovations designed in other jurisdictions; and
- an incentive for jurisdictions to have the 'best' set of regulations, to attract businesses from other jurisdictions (competitive federalism).

However, the Productivity Commission has not found these benefits to be notable, or only obtainable through the current fragmented system.

[69] The Productivity Commission, at p19.

[70] The Productivity Commission, at p18.

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