3. What is an unnecessary regulatory burden?

This chapter discusses what constitutes an unnecessary regulatory burden, and how such burdens can be prevented. The content of this chapter is taken from the research report by the Productivity Commission of the Australian Government. [1]

3.1 Sources of potential unnecessary regulatory burdens

The potential for unnecessary regulatory burdens arises from a number of sources. However, they can typically be categorised under three broad headings:

(1) problems with regulations themselves;
(2) poor enforcement and administration; and
(3) unnecessary duplication and inconsistency.

3.1.1 Problems with regulations themselves

Regulations can unnecessarily increase regulatory burdens in several ways:

- **Unclear or questionable objectives**: a lack of clarity provides uncertainty about what is expected of both those being regulated and those regulating. Moreover, it increases the potential for regulators to use their own discretion in determining the intent and priorities of legislators and can lead to inconsistency between regulators interpreting the same piece of legislation. Regulatory uncertainty acts as a disincentive to invest, as well as potentially increasing compliance costs.

- **Conflicting objectives**: sometimes regulations (possibly enforced by different regulators) can have objectives that are conflicting. Examples might include safety considerations, that suggest generous spacing, and environmental regulations that seek to minimise a facility's 'footprint' and hence its environmental impact.

- **Overly complex regulation**: complex laws are likely to require legal interpretation and therefore compliance is more costly and more time consuming. They also make it harder to determine the expectations of regulators.
- **Excessively prescriptive regulation**: prescriptive regulation is typically more complex and onerous than objective- or performance-based regulation, is less flexible, can stifle innovation, and may not allow businesses to deliver the policy outcome at least cost.
- **Redundant regulation**: regulation may remain in force despite being overtaken by changed circumstances. While providing no benefits, such regulation will still involve compliance costs and could overlap with more recent legislation, causing regulatory confusion.
- **Regulatory creep**: regulations that influence more areas and activities than were originally intended or warranted. This can stem from the use of subordinate legislation, and regulatory guidelines.

3.1.2 Poor enforcement and administration

Poor enforcement and administration of regulation can arise from a number of sources:

- **Excessive reporting or recording requirements**: requirements beyond the minimum required to enforce a regulation unnecessarily increase compliance costs.
- **Inadequate resourcing of regulators (including inexperience or lack of expertise):** can delay the time taken for approvals, and potentially lead to poor regulatory decisions. It can also prompt regulators to seek additional, and potentially spurious, information because of a lack of experience or expertise, or to circumvent statutory time limits (where such limits exist).

- **Overzealous regulation**: can increase compliance costs and represents a disincentive to investment. Inadequate resourcing of regulators can lead to problems, but over-resourcing can also, if it results in imposing excessive regulation or micro-management of regulated businesses.
- **Regulatory bias or capture**: regulators may be 'captured' by particular interests that they deal with on a regular basis, and therefore make decisions favourable to those interests. Such interests could include the businesses being regulated (or a particular business or businesses), or lobby groups such as environmental or community groups.

3.1.3 Unnecessary duplication and inconsistency

Regulatory duplication and inconsistency between jurisdictions is not inherently bad. It may stem from different circumstances between jurisdictions and, from a competitive federalism perspective, can lead to better overall outcomes. However, duplication and inconsistency can impose some costs:

- **Duplication of regulation:** the need to provide information to multiple regulators and go through multiple processes can add unnecessarily to compliance costs. The existence of multiple regulators also creates incentives for 'forum shopping', where participants may seek the forum in which they are most likely to obtain a favourable outcome. Further, it can create uncertainties regarding the boundaries of responsibility for each regulator. On the other hand, regulatory duplication can also be seen as a desirable outcome of intergovernmental competition.
- **Inconsistency of regulation:** regulatory inconsistencies can occur within or across jurisdictions, and increase regulatory burdens. Inconsistency is likely to present particular problems for businesses operating in multiple jurisdictions.
- **Variation in definitions and reporting requirements:** variation can occur between regulators within jurisdictions, although it is typically a more significant problem for businesses operating in multiple jurisdictions. Such variation can increase compliance costs.

3.2 What is best practice regulation?

The overarching objective of regulation should be to achieve desired outcomes more efficiently than would be achieved by alternatives, including no regulation (PC 2002). In promoting government objectives, most regulation will also impose costs. The focus of this study is on unnecessary burdens. Best practice regulation imposes the least burden necessary to achieve the underlying policy goals, bringing the greatest possible net benefit to the community.

Box 3.1 **Principles of good regulatory practice**

Six principles of good regulatory practice were:

- Governments should not act to address ‘problems’ through regulation unless a case for action has been clearly established. This should include evaluating and explaining why existing measures are not sufficient to deal with an issue.
- A range of feasible policy options — including self-regulatory and co-regulatory approaches — needs to be assessed within a benefit–cost framework, including analysis of compliance costs and, where relevant, risk.
- Only the option that generates the greatest net benefit for the community, taking into account all the effects, should be adopted.
- Effective guidance should be provided to regulators and regulated parties to ensure that the policy intent of the regulation is clear, as well as what is needed to be compliant.
- Mechanisms such as sunset clauses or periodic reviews need to be built in to legislation to ensure that regulation remains relevant and effective over time.
- There needs to be effective consultation with regulated parties at the key stages of regulation-making and administration.

Source: Regulation Taskforce (2006), Australia Productivity Commission

3.2.1 Good regulatory design

Good design of regulations is important to minimise unnecessary burdens on business and the community. Elements of good regulatory design relate to:

- clarifying objectives
- simplifying regulation
- reducing levels of prescription (unless this is necessary to clarify requirements or provide certainty about compliance, thereby potentially reducing unnecessary burdens)
- minimising reference to subordinate legislation
- minimising unnecessary inconsistencies between jurisdictions
- including review mechanisms
- completing regulatory impact statements (RISs)
- including sunset clauses — a sunset clause is likely to trigger a review or termination of a regulation, which may reduce unnecessary burdens.

3.2.2 Regulatory impact statements and ‘good’ process

The RIS process is designed to bring together key elements of good regulatory practice. The RIS should cover the problem or issue being dealt with, the objective of government in dealing with the issue, and a range of feasible options. There should be benefit–cost (box 3.2), impact and risk analyses for each option, together with justification for the preferred option. The RIS should also summarise the consultation process and feedback received, and address how the regulation will be implemented and what review mechanisms are in place (Regulatory Taskforce 2006).

Box 3.2 **Importance of benefit-cost analysis**

The use of benefit–cost analysis is an important part of the regulatory impact statement process. A proper benefit–cost analysis should account for all the effects of a regulatory proposal on the community and economy (not just direct or easily quantifiable effects). Benefit–cost analysis involves valuing the gains and losses relating to a regulatory proposal in monetary terms. Where the benefits exceed the costs, this suggests the regulatory proposal would bring net benefits to the community.

Benefit–cost analysis is an important part of the regulatory assessment process because it:

- provides decision makers with quantitative information about the likely effects of a regulatory proposal
- encourages decision makers to take account of all the positive and negative effects of a regulatory proposal, and discourages them from making decisions based only on the impact on a single group within the community
- quantifies the impact of regulatory proposals in a standard manner, thereby promoting comparability, and encouraging consistent decision making
- captures the various links between the regulatory proposal and other sectors of the economy
- helps discover cost-effective solutions to policy problems by identifying and measuring all costs
- makes clear and transparent the assumptions and judgments made in those instances where it is difficult to quantify some costs or benefits with precision

(Australian Government 2007).

Good regulatory design is important to minimise unnecessary burdens on business and the community. Unnecessary regulatory burdens can potentially arise from problems with regulations themselves, poor enforcement or administration, and unnecessary duplication and inconsistency. Best practice regulation imposes the *least burden necessary to achieve the policy goals underlying the regulation, bringing the greatest possible net benefit to the community.*

3.3 Costs of regulation

The major costs associated with regulation can be categorised as compliance costs (including the administrative costs to government); lobbying or 'gaming' costs; the costs of price distortions leading to consumption and production losses; and the related costs associated with potentially 'lost', delayed or suboptimal investment (figure 3.1).

3.3.1 Compliance costs

The costs of complying with (and administering) regulation are potentially significant. The compliance costs of regulation to businesses potentially include:

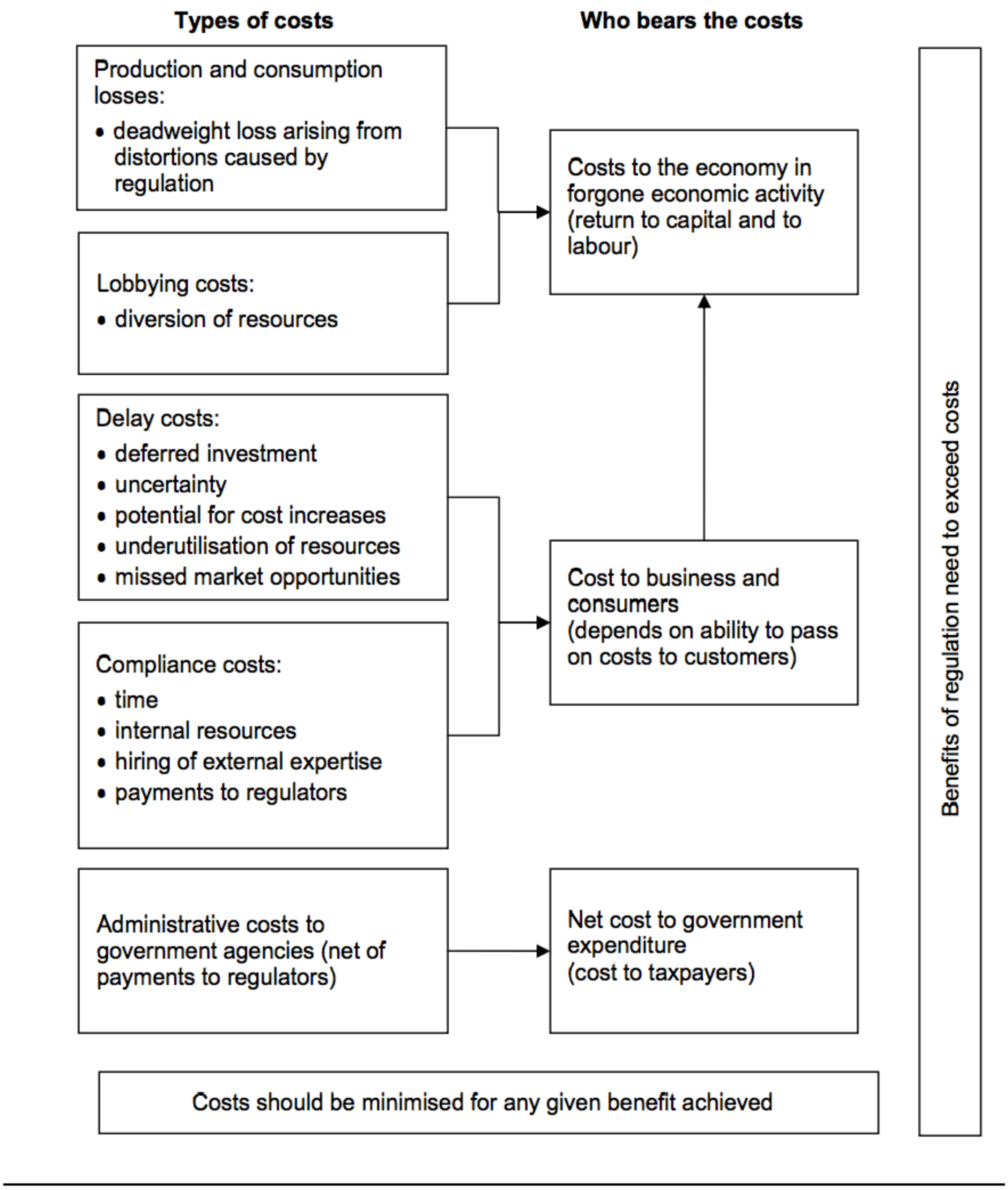
- management and staff time (including diversion of management attention from core business, and hiring of additional staff)
- payments to regulators
- purchase and maintenance of specially modified IT systems
- hiring of external expertise (such as consultants and lawyers)
- training costs.

The burden of these compliance costs falls initially on businesses, potentially reducing returns on investment and, therefore, possibly investment levels (in turn generating lower tax revenue). To the extent that higher costs are passed on to consumers in the form of higher prices or restricted consumer choice, the burden of increased compliance costs falls on consumers. Governments also incur significant costs in designing and enforcing regulation. Compliance costs are minimised when good regulatory practices are followed.

3.3.2 Lobbying costs

A further potential inefficiency stemming from regulation — particularly when regulatory outcomes are uncertain — is the diversion of resources into lobbying activity, both by businesses seeking to invest and other interested parties. The greater the discretion given to regulators, the greater the potential for lobbying activity to be employed in an effort to influence regulatory outcomes.

Figure 3.1 **Costs of regulation**



3.3.3 Production and consumption losses

Regulation can potentially lead to price distortions resulting in production or consumption levels deviating from those that would occur in the absence of regulation.

3.3.4 Delays and the potential for 'lost' investment

The compliance costs and regulatory uncertainty associated with prospective projects can reduce investor returns and increase risk, potentially threatening their commercial viability. Delays result in out-of-pocket expenses and implicit costs associated with deferred or cancelled projects, such as forgone earnings, lost market opportunitieS, the costs of standby financing facilities, and the costs of the funds already invested. These losses are compounded if capital costs are rapidly increasing.

Unnecessary compliance costs and delays can act as a deterrent to the entry of small- to medium-sized businesses, which already face high barriers to entry.

3.4 References

[1] Australian Government Productivity Commission, *Review of Regulatory Burden on the Upstream Petroleum (Oil and Gas) Sector*, December 2009