

## **BRIEFING PAPER ON REGULATORY IMPACT ASSESSMENT – WHAT, WHY AND HOW?**

### **Introduction**

Use of regulation<sup>1</sup> as an instrument to achieve economic and social policy objectives in emerging economies has expanded recently.<sup>2</sup> Yet globally most of the governments have witnessed regulatory failures majorly due to persistent and common patterns of overregulation and poorly designed or overly complicated regulations and faulty implementation<sup>3</sup>.

As excessive or cumbersome regulations can impose additional costs and inhibit actual objective, an effective, efficient and accountable regulation remains indispensable - for instance, to protect consumers, to incentivise investors, to promote financial sector, et al.<sup>4</sup> There is need, therefore to subject regulations to greater scrutiny than in the past. This briefing paper provides an introduction to Regulatory Impact Assessment (RIA), a tool that puts regulations under scrutiny by assessing the intended and unintended effects of regulations and presents the reasons for its adoption in emerging economies.

### **(WHAT) is Regulatory Impact Assessment?**

RIA is a systematic tool used to analyse the objectives of a regulatory proposal, the risks to be addressed by the regulation and the options for delivering the objectives. It is a formal method for assessing the costs and benefits, economic and non-economic, of regulatory proposals and the overall aim is to ensure greatest net public benefit.<sup>5</sup> It includes both regulatory appraisal of hypothetical alternatives (ex-ante) and regulatory evaluation of policies in force (ex-post).

RIA tool was first introduced in the United States (USA) in mid-1970s under the Regan administration. Following the neoliberal doctrine, he discerned that the legislators and government officials, when left to them, will produce statutes that do not concur with public interest.<sup>6</sup> Thus, in order to reduce the burden of existing and future regulations, provide for presidential oversight of the regulatory process, minimise duplication and conflict of regulations, and insure well-reasoned regulations, the Executive Order 12291 was issued in 1981.<sup>7</sup> Section 3 of the said order stated that each agency shall, in connection with every major rule, prepare, and to the extent permitted by law, consider undertaking a RIA.

In addition to the USA, OECD and European countries too joined suit and by the mid-90s, 20 out of the 28 OECD countries started to undertake RIA. Table 1 provides a brief snapshot of global spread of RIA.

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<sup>1</sup> For the purpose of this paper, the term 'regulation' means all regulatory instruments including policy, legislations, rules, guidelines, regulations etc.

<sup>2</sup> Better Regulation For Growth: Regulatory Governance in Developing Countries 2010, International Finance Corporation,

[http://www-wds.worldbank.org/external/default/WDSPContentServer/WDSP/IB/2010/07/13/000334955\\_20100713050729/Rendered/PDF/556450WP0Box0349461B0GovReg01PUBLIC1.pdf](http://www-wds.worldbank.org/external/default/WDSPContentServer/WDSP/IB/2010/07/13/000334955_20100713050729/Rendered/PDF/556450WP0Box0349461B0GovReg01PUBLIC1.pdf)

<sup>3</sup> Better Regulation Task Force: Principles of Good Regulation 2003

<http://webarchive.nationalarchives.gov.uk/20100407162704/http://archive.cabinetoffice.gov.uk/brc/upload/assets/www.brc.gov.uk/principlesleaflet.pdf>

<sup>4</sup> Kirkpatrick C, 2001, Regulatory Impact Assessment in Developing countries: Research Issues, Centre on Regulation and Competition working paper series, University of Manchester

<sup>5</sup> *ibid*

<sup>6</sup> Auby J B and Perroud T 2013, Regulatory Impact Assessment, Global Law Press, p. 21

<sup>7</sup> <http://www.archives.gov/federal-register/codification/executive-order/12291.html>, (accessed 13th May 2015)

**TABLE 1: GLOBAL SPREAD OF RIA**

Mid 1970's	1985	Mid 1990's	2000	2007	2008	2013	2014
US- Reagan administrati on introduced RIA	Mexico formed Economic Deregulati on Unit (UDE) for regulatory reform	20 out of 28 OECD countries implement ed RIA	Few non OECD countri es started adoptin g RIA	South Africa issued RIA guidelin es	Australi a adopte d RIA	Greece implement ed competitio n impact assessment	China launche d anti-trust review

**Rationale for RIA (WHY)**

Substantive and procedural matters which adversely impact the growth of businesses in most of the emerging economies can be attributed to a number of factors. Chief among them include multiplicity of authorities, plethora of regulations, lack of clarity and outdated regulations. These attributes of existing regulatory setup are well recognised now.<sup>8</sup> On number of occasions across various economic sectors, disconnect between the intent of a proposed legislation and the manner in which it is interpreted by the regulated entity has been noticed. Further, different authorities tend to draft often conflicting rules and regulations governing identical activities, thus creating confusion in the regulated space. These trends have led to a broader recognition of the need for regulatory reforms that enhances quality of regulations and process of forming the regulations. Thus, it produces a compelling case for introducing RIA, a tool to audit both the intended and unintended effects of regulation, and promote effective, efficient and accountable regulations.<sup>9</sup>

**Key Steps in RIA Process (HOW)**

OECD has penned down the guidelines for undertaking RIA. However, most of the countries, especially emerging economies, cannot follow them in entirety due to lack of expertise/capacity, resources and availability of data. However, the broad framework to undertake RIA is as shown in Table II.

**TABLE II: KEY STEPS IN UNDERTAKING RIA PROCESS**

Steps	Description
<b>Problem Identification and Initial Assessment</b>	<b>Understanding and Formulation of the Problem</b> The first step in performing RIA is to clearly formulate the problem that the proposed regulatory intervention/amendment to existing regulation is intended to address, since too many regulations are drafted without a clear statement of the problem and regulatory objective which leads to overregulation or ambiguity.
	<b>Specifying the Objectives</b> Objectives of regulations should be clearly specified with a clear link to the problem
	<b>Consider Alternative Options</b> The analyst should develop a list of alternatives actions that could be taken to address the problem. This list may include “doing nothing” and non-regulatory alternatives.
	<b>Choosing between Options</b> Some options can be excluded on the early stage on the grounds of feasibility, risks or limited benefits. In some case especially when an existing desirable law is being reformed, there may be few real options for reform.

<sup>8</sup> Ministry of Corporate Affairs, GOI, Report of the Committee for Reforming the Regulatory Environment for Doing Business in India, 2013

<sup>9</sup> Supra Note 6

	<b>The Consultation Plan</b> This step includes identifying the experts, key stakeholders, business and community groups to be consulted during the RIA process. The consultation plan should retain flexibility, to respond to new information needs, new findings, or changing public concerns.
<b>Stakeholder Consultations</b>	Stakeholder consultation is a key element of the RIA and should be an ongoing process. Nevertheless, this step puts primary focus on formal consultations aimed to ensure that interest groups are aware of all the policy options considered, and the costs and benefits of each option. Consultations provide stakeholders with opportunity to contribute towards policy development, and can thus help in achieving greater public support for regulatory reforms. The final RIA report must include details of those consulted, outlining key views expressed, and highlighting the major areas of agreement, as well as areas of difference.
<b>Data Collection, Analysis and Discussion of Findings</b>	This is the main analytical step of RIA. It includes analysis of potential/ existing benefits, costs and distributional impacts of each option- including the ‘doing nothing’ option. The key aim of this analysis is to help determine whether the benefits from the various policy options justify costs. Principally the assessment should include full economic costs and benefits, including social, environmental and health and safety costs and benefits. However, resource and data constraints make this process difficult and encompass to undertake target oriented RIA.
<b>Preparing the Full RIA Report</b>	Final step is to prepare full RIA report which assists the decision makers. A report must include following: <ul style="list-style-type: none"> <li>• Background and executive summary</li> <li>• Problem definition</li> <li>• Policy options</li> <li>• Recommendation</li> </ul>

## Types of RIA

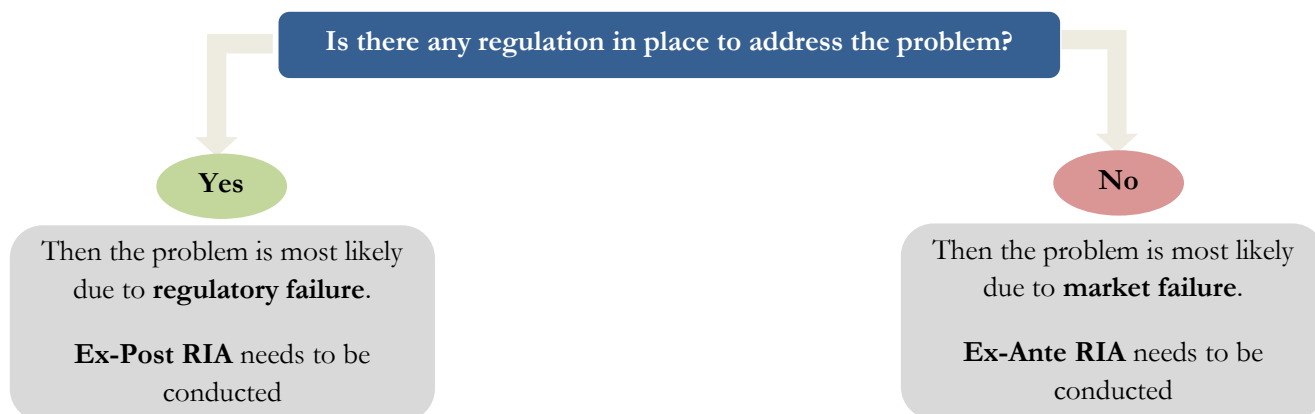
**Ex-ante:** This form of RIA is conducted prior to the regulation coming into force. It helps in the process of systematically selecting the most efficient and effective regulation from a set of options to meet the desired objectives<sup>10</sup>. It helps to achieve a sound understanding of the impact of the proposed regulation and evaluating which group of stakeholders will be impacted in what manner due to the regulation. A series of alternatives are evaluated and the costs/benefits associated with each alternative are identified to help decision makers arrive at the most beneficial solution.

**Ex-post:** Ex-post RIA is conducted after the regulation has come into effect to monitor and estimate the impact of the existing regulation. The results are assessed *vis-a-vis* the initial objectives of the regulation and whether it has met its desired purpose or not? It can then also provide recommendations for modifications to the regulation to correct any sub-optimal provision(s)<sup>11</sup>. Further, it can also be helpful to carry out any mid-course corrections to review any unsatisfactory provisions. In addition, it assists the governments in reviewing the effectiveness of the regulation and also evaluates more suitable alternatives. This process also increases the accountability of the governments as citizens can evaluate their performance specifically with respect to the benefits promised. Ex-post RIA can be extremely helpful for developing countries owing to the existence of multiple, archaic regulations, often prepared without having the clarity on objectives. This results in over-regulation or under-regulation, compelling the need for an ex-post impact assessment.

<sup>10</sup> Mapping of ex-ante Policy Impact Assessment Experiences and Tools in Europe, UNDP, BRC, 2007

<sup>11</sup> Ibid

**Figure I: Process to undertake RIA (Ex-Post & Ex-Ante)**



#### **PROCESS**

1. Understanding the baseline:
  - a. Identification and prioritisation of relevant regulations
  - b. Undertaking impact assessment of regulation through data collection and stakeholder validation
2. Development of regulatory alternatives
3. Undertake impact assessment of alternatives
4. Selection of optimal regulatory alternative

#### **PROCESS**

1. Understanding the baseline through data collection and stakeholder validation
2. Development of regulatory proposals
3. Undertake impact assessment of regulatory proposals
4. Selection of optimal regulatory proposal

#### **Benefits of RIA**

The most important objective and benefit of RIA is its ability to help design the most effective and efficient regulations to ensure that the costs are justified by the benefits to stakeholders.

- \* Primarily, RIA helps to design high quality regulations
- \* It provides clarity of objectives
- \* The tool helps to identify the appropriate tools to achieve the said objectives
- \* It helps to improve the decision making process by making it more systematic and scientific<sup>12</sup>
- \* It follows a comparative approach for selection of the alternative, thereby improving the process of identifying the most optimum option
- \* It guides the policy makers to ask relevant questions to ensure that the impact of the proposed or existing regulation is effectively evaluated<sup>13</sup>
- \* RIA involves extensive consultation with stakeholders, thus, making the process more participatory and transparent
- \* It also helps to improve government accountability as the process, objectives and selection is more transparent<sup>14</sup>

<sup>12</sup> Building an Institutional Framework for Regulatory Impact Analysis, OECD, 2008

<sup>13</sup> *Ibid*

<sup>14</sup> Regulatory Impact Analysis in OECD Countries - Challenges for developing countries, OECD, June 2005

### **BENEFIT OF RIA – EXAMPLE OF UK**

In 2013 a UK government campaign to cut EU red tape suggested to implement COMPETE principles: **C**ompetitiveness test, **O**ne-in and One-out, **M**easure impacts, **P**roportionate rules, **E**xemptions and lighter regimes, **T**arget for burden reduction, **E**valuate and **E**nforce - to enable business to COMPETE, grow, and create jobs. Just after applying these principles on ten regulations, UK businesses saved around £100 million a year, preventing additional costs of at least £100 million a year and banking one-off savings to firms of another £40 million.<sup>15</sup>

### **Challenges & Risks**

Undertaking RIA may face certain methodological and operations difficulties when it is applied to decision making in emerging economies. The data requirements for undertaking RIA can be demanding. In case of an ex-post RIA, stakeholder consultation could aid in bridging the data gap. However, in case of ex-ante RIA involves risk assessment, in which probabilities must be applied to possible outcomes. The valuation of these probabilities can be manipulated in the interest of vested parties to bring about the results initially desired by the policy maker to benefit few stakeholders over and above the others.<sup>16</sup> However, these challenges could be met if the body responsible to undertake RIA is provided with operational independence.

### **Way Forward**

Most of the emerging economies, struggling with staggering economic growth due to regulatory failure, are implementing reforms. However, sustainability of such reforms has been widely debated. The government's outlook requires focusing on reforms that would sustain an economy in the long-run. Therefore, there is a need to sensitise key stakeholders influencing government policy about the issue and its appropriate solution. RIA is a tool that will help in improving quality of regulations, consequently reducing the room for red tapism, which will ameliorate the investment sentiments and improve the country's social and economic condition. By a) making it easier for business it will add to government revenues also and not just the businesses and b) reduce the cost of oversight by government agencies. Care will need to be taken to ensure that cutting down all regulations perceived as redundant or inefficient may not be the best way forward.

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<sup>15</sup> Cut EU red tape: One year on November 2014, UK Government, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/371088/Cut-eu-red-tape\\_one-year-on.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/371088/Cut-eu-red-tape_one-year-on.pdf)

<sup>16</sup> Kirkpatrick C and Parker D, 2003, Regulatory Impact Assessment: Developing its Potential for use in Developing Countries, Centre on Regulation and Competition Institute for Development Policy and Management, University of Manchester