

Regulatory impact assessment

The idea of using regulation to promote development in low-income countries has a long and chequered history. Since regulation is used by governments to try and change people's behaviour it is not surprising that it has been labelled 'good' or 'bad' according to whether the state or the market has been the politically preferred agent of economic management and development at any given time.

The current position represents a retreat from the strong preference for the market demonstrated in the '80s and '90s. Although markets are still regarded as important agents of development it is now generally accepted that they can be imperfect, incomplete or missing. This then allows governments and other institutions a role in helping markets to function efficiently. Regulation is thus rehabilitated as an instrument for assisting private sector development and economic growth.

Governments in most developing countries recognise the private sector as the most important contributor to economic growth and acknowledge the need for regulation to enable markets to function efficiently. But successful market development is not necessarily pro-poor. Therefore regulation may also be needed to guarantee that market-led development contributes to the objective of poverty reduction in low-income countries.

Regulation can help ensure that markets are not only economically efficient, but work so as to improve access by the poor. Also, the broader goals of sustainable development imply a much wider range of objectives for regulation policy, including, for example, protecting consumers, employees and vulnerable groups from abuse and protecting the environment.

So regulation is now considered a key instrument for achieving development goals. But comparatively little attention has been given, so far, to finding out how successful it has been. And this is despite donors' heavy emphasis on privatisation, market liberalisation and broader institutional reform including setting up regulatory agencies.

Regulation needs to be both effective and

efficient. It needs to meet its goals and to do so as cheaply as possible, in terms of both administration costs and the cost to the wider economy. Economic, social and environmental regulation can all affect each other so the linkages between them must be taken into account when proposing changes in any one. Sometimes a change in a regulation may be accompanied by economic, environmental and social gains – a win-win-win outcome. More likely are trade-offs where gains in one sphere lead to losses in another. There is therefore a compelling case for the systematic appraisal of the positive and negative impacts – economic, social and environmental – of any proposed change to an existing regulatory framework.

Principles of RIA

Regulatory impact assessment (RIA) is a method for assessing the positive and negative impacts of existing or proposed regulatory changes. It can be used either in advance of a regulatory change (to assess the predicted impacts) or after the regulation has been implemented (to assess what the impacts actually were).

Making decisions

RIA is not a tool that substitutes for decision-making, rather it is an aid to raising the quality of debate and understanding in the decision-making process. The ways policymakers make decisions on regulations can be classified as *expert*, where the decision is made by a trusted expert, *consensus*, where a group of stakeholders agree a common position, *political*, where political representatives make the decisions based on political priorities, *benchmarking*, where the decision is based on an outside model, and *empirical*, where the decision is based on fact-finding and analysis that

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defines the parameters of action according to established criteria.

RIA is part of the empirical approach to decision-making. Strengthening the empirical basis for policymaking is increasingly recognised as an essential condition for improving its quality. RIA does this by systematically and consistently examining the potential impacts (positive and negative) that arise from government action and how these are distributed among the various stakeholders. It communicates this information to decision makers in a way that allows them to consider the full range of positive and negative impacts that would be associated with the proposed regulatory change.

Good practice

RIA can be used as an integrating framework to identify and compare the linkages and impacts between economic, social and environmental regulatory changes. In this way it can help integrate multiple policy objectives. Public consultation, which is an integral part of RIA, enhances the transparency of the decision-making process and improves the information provided to policy makers. And government accountability can be improved because the RIA process involves reporting on the information used in decision-making and demonstrating how the decision impacts on society. RIA needs to be based on sound professional judgment. Regulations which may have significant impacts will have to be assessed particularly carefully. In other words there will often be a need for preliminary or screening RIA to establish the need for a full RIA and the appropriate level of detail, cost and complexity.

The RIA report should also specify how the *actual* impacts of any regulation (rather than the anticipated impacts) will be monitored and evaluated. This should then enable remedial action to be taken if necessary. Also the lessons learned from studying these actual impacts should be an important part of subsequent regulatory decision-making. Unfortunately it is much more common to find this being encouraged rather than actually practised.

Some regulatory proposals deal with risk,

whether to the environment or to consumers or to workers' health and safety. Risk assessment is part of RIA and involves identifying which outcomes lead to harm and estimating the probabilities of such outcomes occurring. If the risk is considered significant then controls or mitigation measures may be required.

RIA involves establishing a limited number of economic, social and environmental indicators which can be measured in quantitative or qualitative terms. Changes in the indicators then suggest possible impacts of the regulatory reform. Choosing indicators should be an open process involving a wide range of stakeholders because there will be different views on which indicators should be chosen.

Causal chain analysis is an integral part of impact assessment. For RIA this requires looking at the various options for regulatory change, including the 'do nothing' option, and clarifying the 'cause and effect' links that lead from each option to the economic, social or environmental outcomes.

Because RIA has to be applied on a case by case basis there can be no simple blueprint for 'best practice'. There will be differences in how quickly governments can adopt and implement their own RIA processes. First the appropriate skills will have to be developed. In general, assessing qualitative data requires the ability to make fine judgments while interpreting quantitative RIA data involves many problems of aggregation. A range of techniques will have to be used in assessing the magnitude and significance of the impacts.

Secondly, RIA depends on extensive consultation to ensure that the necessary information is collected and analysed before identifying the likely impact. There may be little tradition of consulting widely before undertaking regulation. Also those who may have been consulted in the past may not have represented the relevant stakeholders. And of course consultation is time consuming and can be expensive. It is sensible therefore to first screen regulations to form a view on how significant its impacts are likely to be. Resources for RIA can then be allocated where they are likely to do most good.

Once it has been established that a proposed regulation should be subjected to a detailed RIA, the terms of reference for the assessment can be specified. These cover the options to be assessed, the impacts to be investigated and the methods that will be used. They also set out who will be responsible for carrying out the RIA.

The politics of RIA

RIA assumes policymaking is an objective and rational process which can be enhanced by fact finding and disinterested analysis of the evidence. In fact, in practice, regulation can be 'captured' by special interest groups which have the time, resources and motivation to influence the process. Governments face constant pressure to advance regulations that serve the interests of such groups. If RIA does succeed in promoting wider consultation and requiring that potential impacts (both positive and negative) are made public then this increased transparency and accountability may prevent the more powerful groups from influencing the outcome unduly. RIA can also be 'captured' by government, where the process is used to validate decisions they have already made.

RIA is not just a method of analysis which produces a predictable outcome and technical 'solution'. In fact it can contribute to open and accountable government decision-making. But this will depend a lot on the context. The pre-existing legal and administrative arrangements will obviously shape the process. So will the presence, or, more likely in developing countries, absence of civil society organisations which can effectively represent the interests of the less powerful in society. Local customs and behavioural norms will influence the process, as will the contending social interests in the country.

When regulatory instruments fail to take into account the limitations of the institutions that actually exist in a country the results can be contrary to expectations. For example, when privatisation has proceeded in developing countries where robust regulatory institutions have not previously been established, the results, in terms of economic and social performance have been disappointing.

Current practice in developing countries

What are developing countries currently doing in terms of regulatory impact assessment? There is very little published information on this so we devised a questionnaire and sent it to departments with regulatory responsibilities in 99 countries. We received 68 responses from 40 countries. Most of the responses (48) came from regulators of network utilities. The respondents ranged from middle management to director-general level or were consultants to senior management in regulatory bodies.

The questionnaire had three main parts. It covered RIA as an assessment method, RIA as a process and RIA as part of a more general strategy of regulatory reform. The main areas covered were:

Theories of regulatory change

Rational-synoptic and technocratic theories

These theories consider the policy process to be linear and starting with an identified regulatory problem but not enough information to deal with it. RIA produces the relevant information and analysis so the correct regulatory reform decision is made and an overall improvement in governance is achieved.

Behavioural theories

On the other hand these theories see organisations' behaviour as only partly rational, with switching goals and simplified and sometimes conflicting decision rules. RIA still plays the role of information provider but the process itself, and those who participate in it, is more significant. RIA is considered to have the potential to change the way society, public administration and the decision-makers interact.

Dominance theories

These emphasise the influence of the goals of the dominant stakeholders or political leaders and the way RIA can help these be achieved. In one situation, for example, RIA might focus on reducing the regulatory burden on business. In another it might prioritise poverty reduction. Alternatively it can be used to centralise decision-making by allowing the national administration to check all regulatory proposals against criteria which have previously been endorsed by some elite.

The OECD approach

The adoption of formal RIA arrangements has been most evident, so far, in countries which are members of the Organisation for Economic Cooperation and Development (OECD). More than half of all OECD countries had adopted RIA programmes by 1996 and 20 out of the 28 were using RIA in some form by 2001.

The OECD has established the following ten questions that policymakers should ask about any proposed regulation:

- *Is the problem to be addressed correctly defined?*
- *Is government action justified to deal with this problem?*
- *Is regulation the best form of government action?*
- *Is there a legal basis for regulation?*
- *What is/are the appropriate level(s) of government for this action?*
- *Do the benefits of regulation justify the costs?*
- *Is the distribution of effects across society transparent?*
- *Is the regulation clear, consistent, comprehensible and accessible to users?*
- *Have all interested parties had the opportunity to present their views?*
- *How will compliance be achieved?*

This regulatory quality checklist contributes to shaping RIA guidelines in OECD countries and should also be useful to those designing RIA systems in low-income countries. Unsurprisingly, given the importance of the social and institutional context in which RIA is practised, there is considerable variation among OECD countries in how they apply and implement RIA.

- familiarity with RIA as a concept and the OECD guidelines
- the existing use of RIA within the country
- legal requirements to use RIA and published governmental guidance
- the form of RIA used
- the processes used when doing RIA
- the openness of RIA, in terms of published documents
- public consultation and participation in RIA
- RIA and wider regulatory reform

The answers confirmed that there was some understanding of RIA and its principles among regulators in a number of developing and transitional economies. But this understanding seemed neither deep nor widespread. RIA was found to be a legal requirement in ten of the 40 countries – perhaps a surprisingly large proportion given the general perception that RIA is largely an OECD phenomenon.

Eight of the nine Asian countries that responded were using RIA, compared to 11 of the 16 African countries, six of the nine Latin American/Caribbean countries and five of the six transitional economies. But only one country (Tanzania) claimed that RIA was being systematically applied to all new state regulations.

There were marked regional differences in familiarity with RIA principles. Three fifths of the African replies reported little or no awareness whereas most Asian respondents claimed to be fully aware. However, only six were familiar with the OECD guidelines. None of the African respondents claimed their countries had developed their own guidelines for RIA.

It seemed that RIA was mostly being used to appraise proposed regulation rather than to evaluate that which already existed. This is also true in OECD countries. It is not difficult to understand that governments may be reluctant to dwell on whether their regulations have had the desired results. This use of RIA requires top-level political commitment.

The questionnaire also tried to find out how RIA was being applied across economic, social and environmental regulatory proposals. The answers indicated that it was being applied mostly to economic regulation. In the 30 countries using RIA, 28 were using it for this purpose while only 14 claimed some use in all three dimensions. This concentration on economic regulation probably reflects the traditional focus of government regulation on market failure and natural monopolies, especially utilities. It is also possible that the use of RIA in the broad sense in social and environmental policymaking was underreported due to terminological confusion. (There are a number of labels currently being applied to the impact assessment of social and environmental policymaking.)

Of the 30 countries using RIA, 18 claimed that both positive and negative impacts were considered. Another two said that they only considered positive impacts and the remaining ten seemed uncertain. The difficulty of putting a value on different types of impacts was reflected in the responses received. Only a minority of those considering both costs and benefits were quantifying them in both physical and value terms. And only eight of the 30 countries considered that RIA had provided a 'high level of detailed analysis of costs and benefits'.

It seems that most countries applying RIA to new regulations do consult the public. This is usually through notices and invitations to comment on proposals. Outside experts, government bodies and the private business sector all take part. But consumer groups and other civil society organisations are less commonly included. And few countries make the views of participants public. There seems to be an opportunity for more transparency in this respect.

RIA is likely to be more effective when it is part of a broader strategy of regulatory

governance reform. Of the 22 countries claiming to have such a strategy, ten were using RIA.

Overall the findings suggest that the level of awareness and application of RIA in developing and transition countries is perhaps higher than expected based on the limited information previously available. But sample bias cannot be ruled out. It may be that returns came mainly from countries where RIA is relatively well established. Perhaps the fact that no replies were received from 59 of the 99 countries contacted reflects their lack of any form of RIA.

Designing RIA in developing countries

Why has the use of RIA been relatively limited in developing countries so far? Perhaps the OECD proposed methodology does not transfer readily to countries with very different economies and a greater focus on sustainability and poverty reduction. Or perhaps the RIA is culturally, socially and historically embedded. Either way, an approach to RIA is needed which is appropriate to the context. While the OECD guidelines are useful, they focus on market efficiency rather than reflecting the overarching goals of regulation in low-income countries i.e. poverty reduction and development. And they do not take into account the frequent lack of regulatory skills and resources.

How has 'best practice' guidance in RIA been developed? Most published examples of RIA come from USA, Canada, UK, Australia and some northern European countries. Therefore it is likely that their experiences and thinking have been the dominant influence in shaping such guidance. Again, the fact that RIA has not made the same progress in other countries may suggest that this 'best practice' does not travel well.

In Mexico and South Korea, for example, the approaches to RIA are similar to those found in the developed countries and are consistent with OECD principles. However both countries seem to suffer from inappropriate policy transfer. In Korea the RIA system was introduced in 1998 as part of a broader programme of regulatory reform. It had support at the highest levels of government and was shaped significantly by OECD 'best practices'. Unsurprisingly, perhaps, OECD subsequently noted a significant implementation gap and remarked that most of the RIA work was being done at a low level of sophistication.

In Mexico, regulatory reform also had top-level government support. Here again an implementation gap could be accounted for partly by skill shortages. But also the quality of the data was so poor that quantitative analysis was virtually impossible. Regulatory agencies were not even asked to produce net benefit estimates for fear of creating additional incentives to distort already inadequate data.

A framework for RIA

The aim of regulation policy in developing countries should be to change private sector behaviour in ways that are consistent with the goal of raising the income levels of the poor. If the positive and negative impacts of regulation in terms of, for example, prices and job opportunities and access to credit are to be properly recognised, an RIA must specifically address the social effects of regulatory changes. It may be appropriate for RIAs to be 'pro-poor' by placing a heavier weighting on poverty reduction to favour changes that assist the poor.

So how could a suitable framework for RIA in developing countries be designed? The first essential would be an effective regulatory management system. This would need top-level political support and the establishment of explicit standards. Training for regulators and civil servants would be essential. Problems of data collection would have to be faced and minimum acceptable standards agreed. The RIA process itself would have to be monitored and its role in achieving poverty reduction and growth clarified.

The next step would be to improve the quality of new regulations. To achieve this, RIA must be applied at the earliest possible stage when designing an important new regulation. The views of the public must be taken into account – this will require systematic consultation procedures and the even-handed treatment of different interest groups. The various regulatory options (including doing nothing) will have to be assessed. Those that look more likely to have significant impacts should be examined more closely. Better regulation will require better coordination within government including peer review and perhaps a dedicated impact assessment bureau. RIA will have to be recognised as an integral part of the policymaking process – not something 'added on' for cosmetic purposes or to please donors.

Finally, regulations already in existence will need to be improved. RIA should be applied when these are reviewed and the results published. When all the options and their concrete implications are widely known, the need for change and the rationale behind it can be properly appreciated. It should also be possible then to reduce red tape and unnecessary government formalities.

RIA methods

A range of analytical methods can be used to identify the scale, probability and social distribution of all significant positive and negative effects of regulation. However it will always be necessary to include both qualitative and quantitative analysis – not all impacts can be expressed numerically, convenient though this would be. When

Assessing RIA quality

The case for using RIA is that it will improve regulatory decision-making. However, little systematic analysis of this has yet been done. How might the quality of RIA systems themselves be assessed?

First the criteria for assessment must be established. What are the goals of the RIA system in question? In a narrow sense the goals may be to provide relevant, good quality information in a suitable format for decision-makers and stakeholders. In this case the quality of the documentation could be assessed in terms of its content, relevance, clarity and user-friendliness of presentation.

The effectiveness of the RIA process could also be assessed. For example – did it start quickly enough? Does it provide information on time? How effective are its consultation procedures? How transparent is the process? How effective are the 'follow up' procedures of monitoring and evaluation?

Systematic detailed studies of RIA performance are in short supply and all relate to industrialised nations. Studies of RIA performance in the USA, UK and EC have all found significant deficiencies. These include failing to present the results clearly, not providing enough executive summaries and burying information in places where it was difficult to find.

Evidence of systematic studies of the quality of RIA processes is sparse and not particularly encouraging. There are examples of procedures not starting quickly enough, a lack of openness when making decisions, inadequate consultation of stakeholders and deficiencies in the monitoring and evaluation of regulations' effects after they are implemented.

Performance assessment of RIA in the broader sense is more complex. This involves considering how well the resulting regulatory reform has achieved its goals. It also seeks to find out how much the RIA contributed to the regulatory reform and therefore to its impacts.

impacts can be expressed in a common unit of measurement, such as money, this does make adding them up and comparing them easy. But this cannot always be done and, even when it is possible, it involves making estimates and judgments whose quality may vary. Therefore RIA will always require a very careful and open consideration and weighting of different types of information.

When developing a methodology for RIA, it may well be desirable to choose an approach that is fairly comprehensive and can be selectively applied and simplified. This may help to avoid many different methodologies being used within the same country. It is also, of course, important to choose a methodology that is capable of being applied both to new regulations and regulations already in force.

The development and application of RIA methodologies cannot be divorced from identifying and developing appropriate conditions of governance such as adequate provision of rule of law and administrative and appraisal capabilities. Introducing RIA may require governments to move towards more open policymaking in general. If RIA is to be used consistently and become a normal feature of regulatory policymaking it will require powerful political support within government.

Conclusion

It will take time to assimilate RIA into government decision-making in developing countries and progress is likely to be gradual. The problems that RIA seeks to tackle will vary and so will local needs and capacities. There is no one 'best way of doing things' that can be transferred from country to country. We urgently need to extend our knowledge of regulatory practice in developing and transition economies. As we learn more about the problems encountered, we can harness this knowledge to develop a RIA framework that is appropriate for these countries.

Although institutional reform, including regulatory capacity building, is inevitably a deeply political act, we have argued that effective development policy requires the promotion of appropriate methods to improve regulatory practice. If RIA is designed according to the principles set out above, the result should be better regulation and improved developmental outcomes.

CRC Policy Briefs are intended to provide those involved in development policy and practice with a clear understanding of the main issues and findings presented by CRC research and publication programmes on regulation, competition and development. They have been prepared by **Sarah Mosedale**, under the editorial direction of CRC staff, on the basis of CRC published outputs.

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No 30. Lee, N. *Developing and Applying Regulatory Impact Assessment in Low and Middle Income Countries*. 2002

No 34. Parker, D. and Kirkpatrick, C. *Researching Economic Regulation in Developing Countries: Developing a Methodology for Critical Analysis*. 2002

No 83. Kirkpatrick, C., Parker, D. and Zhang, Y. *Regulatory Impact Assessment in Developing and Transition Economies: A Survey of Current Practice and Recommendations for Further Development*. 2003

which are all available on the CRC web site at: <http://idpm.man.ac.uk/crc/public.html>