Regulatory Policy Committee

RPC short guidance note for departments on assessing Covid-19 restrictions-related impacts in regulatory impact assessments

Purpose and scope of the guidance

This short guidance note aims to assist departments in assessing the impacts of regulatory proposals that could be materially affected by the effects of Covid-19 and/or government measures to tackle the virus. The guidance does not cover regulatory measures aimed at stopping the spread of Covid-19 or mitigating its health impacts (such as lockdowns).[1]

The guidance does not introduce any new framework rules for departments or increase RPC scrutiny requirements. It aims to provide assistance to departments in assessing whether and, if so, how Covid-19 restrictions[2] have created significant economic and social uncertainty affecting their assessment of the impact of regulatory measures. A failure adequately to take Covid-19 restrictions into account in such IAs will potentially affect the RPC-rating of an IA where this is likely to significantly affect the EANDCB or the assessment of impacts on small and micro-businesses.

We expect this specific guidance to be relevant for a limited period, while the uncertainties created by Covid-19 and associated policies/restrictions remain. However, as indicated below, some impacts of Covid-19 restrictions can be expected to be long-lasting. Furthermore, some of the principles here will be relevant to future 'extreme events.'

This guidance considers how potential impacts of Covid-19 related policies and restrictions might affect the assessment of non-Covid related measures, specifically:

- Data availability and quality.
- Analytical uncertainty.
- Taking account of the short to medium term impact of Covid-19 restrictions.
- Taking account of possible long-term and structural impacts of Covid-19 restrictions.

Data availability and quality

Covid-19 restrictions may have constrained departments' stakeholder engagement and data gathering (e.g. through surveys), which may lower the quantity and quality of

[1] These measures are generally outside the scope of the framework, mainly because they are of a temporary (less than 12 months) nature. Should any such measures be extended so that they last longer than 12 months then they could become subject to framework requirements.

[2] "Restrictions" is used broadly and is intended to cover restrictions on economic and social activity arising from the virus, associated 'voluntary' social distancing and government measures. The latter would also potentially include economic support measures, such as the furlough scheme, on the basis that they affect the free operation of the labour market or economy.

evidence. Further, Covid-19 restrictions may have distorted existing data and affected its utility for IAs. (See national minimum wage example below). The RPC would expect departments to explain clearly in the IA:

- **Operational constraints:** and their impact on the quality and reliability of the evidence. Where data and evidence are particularly limited, the IA should set out how this has been addressed, for example by sensitivity analysis (see below); and

- **Timing:** Why it is appropriate to bring forward the proposal and IA at the present time rather than to wait for conditions more conducive for improved availability and validity of data (e.g. emergency measures for business/livelihood protection).

Departments should also demonstrate that they have sought creative ways to consult and gather evidence to overcome some of the operational constraints, for example hosting virtual meetings with stakeholders.

The RPC will take account of all these issues in judging whether the department's analysis is proportionate.[3]

Analytical uncertainty

The Covid-19 restrictions have introduced significant uncertainty to economic projections, social behaviour and reaction to policy. Such uncertainty is likely to affect both the counterfactual/baseline and projected regulation impacts; indeed, in many areas, a continuation of, or return to, the *status quo ante* is unrealistic. This uncertainty may also affect the ability to forecast – to the extent that new forecasts may be unstable. Outcomes are likely to be both less predictable and more divergent. It might also be the case that there are more than one 'extreme events' happening at the same time. These could interact, meaning that overall impacts would not be well-measured by adding the estimated impacts of each event.

In this circumstance, the RPC expects departments to:

- **Take account of Covid-19 restriction impacts:** where there is sufficient certainty to forecast counterfactual/ baselines and regulatory impacts, instead of continuing the *status quo*; or

- **Conduct sensitivity analysis:** where Covid-19 restrictions could have significant impacts on proposals but where there is too much uncertainty to build this into an IA's estimates, departments should still consider the stability of the counterfactual/baseline and regulatory impacts, against a credible range of future

[3] https://www.gov.uk/government/publications/proportionality-in-regulatory-submissions-guidance.

effects of the restrictions. In particular, departments should seek to demonstrate that the rationale for the proposed option is likely to be robust against a worst-case scenario for Covid-19 restrictions related impacts.

It should also be noted that even where there is too much uncertainty to estimate absolute levels of impact it might be possible to do assessments of likely *relative* impacts, for example, percentage changes.

<u>Taking account of the short to medium term impact of Covid-19 restrictions</u>

The spread of coronavirus and government restrictions have most obviously affected health outcomes, the economy and public finances (central and local government). Of these, the impact potentially most relevant to IAs is that on the economy. Economic growth has been highly volatile during 2020 and the economy is expected by the Office for Budgetary Responsibility (OBR), in its November 2020 report, to contract overall by around 11 per cent over the full year. [4] This volatility is expected to continue into 2021, with an expected sharp bounce-back in economic activity. Growth is not expected to settle (at just under 2 per cent) until 2023. Unemployment is expected by the OBR to increase sharply to a peak of around 7.5 per cent in summer 2021 before falling back.

Particularly where the impact of the proposed regulation is highly dependent upon the state of the economy, it is strongly recommended that the IA is informed by forecasts by bodies such as the OBR (as used by HMT for the Spending Review, Budget etc) and the Bank of England. These forecasts cover different scenarios; for example, the OBR's near-term economic outlook has upside and downside virus scenarios depending upon factors such as the effectiveness of test, trace & isolate and the availability of vaccines.

Departments may wish to proportionately consider developments since the OBR's November forecasts, such as economic outturn data (for example, the fall in GDP in November being lower than expected) and other key factors not known at the time of the forecasts. These will include the emergence of a new variant Covid-19 and third lockdown (perhaps more consistent with the OBR's 'downside' scenario), and the roll-out of vaccines (perhaps more consistent with the OBR's 'upside' scenario). The National Institute for Economic and Social Research's GDP tracker, for example, which estimates GDP slightly ahead of ONS releases, might also be informative about likely near-term economic growth ahead of the next OBR forecast. [5]

The impact of Covid-19 restrictions has varied significantly by sector. For example, the hospitality sector (pubs, eateries, hotels etc) has been particularly hard hit by social distancing and lockdowns. Where a proposed regulation is targeted at, or expected to particularly affect, a certain sector or type of economic activity, departments will need to

[4] Office for Budgetary Responsibility, 2020 Economic and Fiscal Outlook, November 2020.
[5] https://www.niesr.ac.uk/latest-gdp-tracker.

consider use of available sectoral data and forecasts. Departments will wish to make use of relevant available data, for example at sectoral and regional level, using the Office for National Statistics (ONS) as a principal resource. The ONS may be able to advise on any data difficulties resulting from Covid-19-related impacts, such as breaks in trend lines. Where international data sources are used, departments will wish to check that they provide reliable cross-country comparisons.

Example

Impact assessment on the annual upratings of the National Minimum Wage and National Living Wage (NMW/NLW)

Impact on data availability and quality
The IA for the annual uprating of the NMW and NLW uses the Annual Survey of Hours and Earnings (ASHE) for data on wages and to estimate the number of employees covered by the policies. Covid-19 restrictions presented particular problems for the IA this year because of the distorting impact of the government's furlough scheme on wage data and coverage of the NMW/NLW. This potentially presented a choice between using old data or trying to make adjustments to the latest data, both of which have implications for the robustness of the analysis. This is in addition to general constraints on stakeholder engagements etc.

Impact on the analysis
The analysis in the IA critically depends upon assumptions for earnings growth at the low end of the wage distribution in the counterfactual and assumptions on the extent to which the effects of the NMW/NLW 'ripple' or 'spillover' through the wage distribution. The sharp economic downturn and deterioration in labour market conditions associated with Covid-19 restrictions have significant potential implications for these assumptions.

Taking account of possible long-term and structural impacts of Covid-19 restrictions

Sharp and prolonged economic downturns can result in 'economic scarring'. For example, an increase in long-term unemployment can result in "hysteresis", whereby a proportion of people effectively cease to be active in the labour market. There can be persistent effects on investment, innovation and productivity. The Bank of England has estimated that the long-term effects of Covid-19 could reduce the supply capacity of the economy by about 1.75 per cent. In brief, short and long-term impacts can interact.
The Bank of England[6] has described how Covid-19 could affect the following in the long-term:

- **What we buy:** The pandemic has resulted in a shift in consumer patterns. Spending on travel, entertainment, hospitality and fuel have decreased, in particular. This has partly been offset by an increase in household goods and groceries. Much of this is likely to be temporary but there could be a persistent shift

[6] Speech by Dave Ramsden, Deputy Governor, Markets and Banking, at the University of Nottingham, 17 November 2020. https://www.bankofengland.co.uk/speech/2020/dave-ramsden-speech-public-lecture-for-university-of-nottingham

in the pattern of consumer behaviour. For example, consumers may continue to buy more online and consumer spending related to travelling to work could remain relatively subdued.

- **What we make:** Production patterns are likely to be affected by changing consumer patterns, although redeploying capital and labour is likely to take time. For example, if economic activity shifts from city centres, office buildings and surrounding restaurants, cafes etc may remain underutilised. These might be re-purposed to other uses, such as residential property, but this could be a slow process.

- **How we work:** It is possible that the shift towards working from home for many occupations might not be temporary and could be the start of a transformational change in work patterns.

This assessment ties in with a number of policy areas, some inter-linked, where the RPC sees regulatory impact assessments and where there has been discussion around whether Covid-19 might result in permanent, structural shifts in the economy and society. These include:

- Working arrangements (e.g. greater homeworking).
- Transport (e.g. reduced commuting).
- Real estate:
  - Residential (e.g. shift from inner-city to suburban dwellings; flats to houses etc).
  - Commercial (e.g. lower need for city-centre office accommodation).
  - Retail (e.g. shift from high street to online).

Example

The Town and Country Planning (Permitted Development and Miscellaneous Amendments) (England) (Coronavirus) Regulations 2020

This measure was introduced as part of a COVID-19 economic recovery policy and introduced a new permitted development right (PDR) for upward extensions on existing purpose-build freestanding blocks of flats.

The Department engaged with the RPC at the pre-submission stage to discuss issues relating to COVID-19 and the evidence base, and approaches to dealing with it. The IA included a section which covered both the impacts of the current sharp economic downturn ("…*there is most likely to be a loss of development at the margins, where the viability of site development is closer to the tipping point of becoming unviable")* and possible longer-term structural changes in the housing market, both in terms of type of accommodation and geographic location, from potential new ways of working.

All of these possible structural changes are, of course, subject to very great uncertainty. Departments will be expected to show that they have considered them where they are likely to be materially relevant to the proposal being appraised, and in a proportionate and usually qualitative way.