Regulation

For a few decades until 2007 there were concerted calls to cut 'red tape' in the interests of economic efficiency. There certainly are regulations that tie up resources but do not achieve their aim and from time to time there are regulations that are out of date. But good quality regulation is essential for the operation of effective markets and essential for the protection of consumers and the environment when those markets don't work. These calls have abated somewhat since the US subprime mortgage crisis – essentially a failure of regulation – led to the Global Financial Crisis.

When business lobby groups complain about regulation, the challenge is to sort out self-interest from genuine concerns about increased cost derived from the burden of compliance. Obviously regulation will impose a compliance burden of some sort but changes focused on reducing costs should not proceed where these will compromise the underlying aims of the regulation. "Streamlining" regulation can easily become an excuse for rolling back hard won consumer protections.

We want as little regulation as possible – but also as much as is needed. The idea that the size of the problem can be measured by the amount of regulation in the statute books – the "quantity theory of regulation" – is dangerously simplistic. Much of the increased quantity of regulation introduced over the past 20 years has been required by new developments (particularly the privatisation of government monopolies, emerging social and environmental issues and necessary responses to new technology).

The role of regulation

Regulation underlies and facilitates business, markets and everyday life

While some regulations restrict competition and harm consumers, much regulation is essential to the operation of markets and to creating and preserving consumer confidence in markets. Talk of regulation as being bad per se is simplistic nonsense. The recent Global Financial Crisis was in large part a failure of regulation of the mortgage market and the high risk derivatives market (trade in financial instruments often at high levels of borrowing rather than in the underlying asset itself, whether that be a property or share or the like). Furthermore, strong, clear and effective regulation can often give a country a competitive advantage.

As circumstances change, so too does the need for changes to old regulations or the introduction of new ones. The Uniform Consumer Credit Act is, for example, due for an overhaul in the light of changing technology and new business models. The rising mortgage broking sector currently contains few barriers to keep incompetent or crooked players out of the industry, harming consumers and reputable participants.

Regulation impinges on consumers too

Very many regulations are imposed on consumers, likely more than those that affect business. These include regulatory requirements that are widely supported (for example bans on drink-driving). They also include policies, such as compulsory superannuation, which are supported by significant business sectors despite the fact that these regulations are radically interventionist and burdensome for employers and consumers.

Anti-competitive and anti-consumer regulation

There is often need for the removal or amendment of regulations which harm consumers' interests. The Pharmacy Agreement is an example of anti-competitive regulation which protects pharmacists at consumers' expense, with no clear public interest purpose. Broadcast television has also been over-regulated to protect powerful media operators.

Regulation has an important role in helping to bring about desired social and environmental change

Many different types of actions are needed to bring about desired social and environmental change. They include such matters as education, market incentives, consumer pressure and risk assessment. Regulation also has a critical role. If Australian governments had not introduced regulations to require the wearing of seat belts and to set blood alcohol limits for drivers, the road toll in Australia would be much higher. The elimination of lead from petrol and the fitting of catalytic converters to car exhausts, thereby significantly reducing urban air pollution, would not have happened without regulation.

The importance of regulators

The performance of regulators is critical to the effectiveness of regulation. Ensuring that regulatory agencies are doing their job properly – targeting key risks and efficiently enforcing the law – will bring more benefits than continual tinkering with legal requirements. When business encounters a problem with regulation, there is a tendency to think that reviewing laws is the answer. Similarly, there is sometimes a tendency to think that new regulations should be introduced when previous regulations have not solved a market or social problem. Instead, the willingness and capacity of regulators to undertake well-targeted enforcement action to 'keep the market honest' is a key element of any strategy to avoid unnecessary regulation.

Other issues

The disclosure fetish

Treasury and business groups often promote regulations that are supposedly 'market friendly'. For example, they argue that market failure can be fixed by better disclosure (the making of information, or other material, public). Sometimes it can. But as behavioural economics illustrates through its demonstrations that people sometimes act in seemingly illogical and irrational ways, disclosure cannot fix all market problems and indeed can make some worse. In Australia, when disclosure doesn't work the response is often 'more disclosure' instead of alternative regulatory approaches, such as prohibiting irredeemable conflicts of interest. Furthermore, the 'anything goes so long as you disclose' approach inexorably adds to business cost without benefiting customers as the disclosure burdens pile on top of each other.

Industry self regulation

Many argue that self regulation is generally the preferred form of regulation. It is said to be more flexible and impose lower burdens on business. In fact there is little evidence that self regulation is cheaper for business or more effective for consumers. Self regulation is often introduced without being subject to the public policy development process or regulatory impact statements. Too often it is applied to industries that are manifestly unsuited to such an approach (for example industries with many small players). It frequently is only partial in coverage. Self regulation is often characterised by lack of effective enforcement mechanisms, which produces the worst of both worlds – it imposes a burden on compliant businesses while the non-compliant ignore it, or "free ride". Finally self regulation is supposed to be more flexible than government regulation but there is little evidence to support this assertion. In most circumstances rule-making and guidelines by regulators are not only more effective but can also be drafted or redrafted quickly to respond to changing circumstances.

This is not an argument against all self regulation, but rather a plea to judge it with the same rigour applied to other forms of regulation. There are of course cases where self regulation has proved effective. This is generally where it is situated within a clear policy framework laid down in legislation – financial services external dispute resolution schemes (such as the Banking and Financial Services Ombudsman) provided for by the Corporations Act is an example.

Reviewing regulation - What should be emphasized?

In October 2005 the then Prime Minister and Treasurer announced a task force to conduct a three month review of the impact of regulation on business efficiency, largely in response to business pressure. In particular, this review follows on from a 'Business Regulation Action Plan' released by the Business Council of Australia in May 2005. The task force report Rethinking Regulation was released in April 2006.

Much of the focus of the review was on the process for introducing new regulation – what kind of public benefit needs to be demonstrated? What bodies must be satisfied? Of course it is essential that the process for introducing new regulations and reviewing existing regulations be coherent and efficient. The process must also balance the needs of business, consumers and other affected parties. But it is important that such processes do not have a bias in favour of regulating or not regulating or in favour of a particular form or style of regulation. There is just as much to be gained by the speedy introduction of effective regulation as there is in preventing ineffective regulation. There is a danger that bureaucratic processes, or a too burdensome regulatory impact statement requirement, can slow down the implementation of new regulation agreed by all to be essential and urgent. And sometimes the processes – which are supposed to promote the efficient development of public policy – enable those likely to lose out under the regulatory proposal to have a second or third attempt at protecting their interests.

What is needed for a high quality regulatory regime?

In order to develop good quality regulation and to make regulation more effective the key questions are:

- What sort of regulation is required for a particular market to work most efficiently?
- When should regulation be used to bring about a needed social or environmental change?
- What is the effect of the regulation on consumers, the society or the environment?
- Is the regulation effective or not?
- What is needed to improve the effectiveness of the regulation?
- How effective is the regulator?

The process of regulation should not be limited by arbitrary rules such as requiring the repeal of one regulation before another can be introduced, nor should new laws automatically be subject to sunset clauses as this may simply lead to the reopening of disputes between different interests that are very difficult to deal with. On the other hand, it is good public policy to look at how existing regulations will interact with any proposed new regulation and ensure that overall regulation is coherent. There may also be circumstances where sunset clauses are desirable.

Useful sources

CHOICE
www.choice.com.au/campaigns
CHOICE campaigns for improved outcomes for consumers in a wide array of fields, including health care, financial services, communications, food and product safety. CHOICE often works with government and industry to refine regulation for the benefit of all.
See also: **http://www.choice.com.au/consumer-action/past-campaigns/consumer-protection/consumer-protection-enforcement.aspx**

'Business Regulation Action Plan', Business Council of Australia, May 2005,
http://www.bca.com.au/Content/101268.aspx
The Business Council's reform agenda for Australia's economic future, including its views on regulation, are available from this site.

Regulation Task Force
http://www.regulationtaskforce.gov.au
The task force on regulation and its report Rethinking Regulation is able to be downloaded from this site.

Council of Australian Governments, March 2008, Business Regulation and Competition Working Group Implementation Plan
http://www.coag.gov.au/coag_meeting_outcomes/2008-03-26/docs/brcwg_implementation_plan.pdf

Authors

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