



# Better Regulation n...

*Is it better for business?*



*Written for the FSB by Robert Baldwin  
Professor of Law, the London School of Economics*

# About the FSB

The Federation of Small Businesses (FSB) is the UK's largest lobby organisation representing the self-employed and owners of small businesses. Founded in 1974, it now has over 185,000 members across all industries, trades and services. It is a non-party political lobby group that exists to promote and protect the interests of all those who own and manage their own businesses.

FSB members together employ 1.25 million people and turnover £10 billion a year. The FSB is a member of the European Small Business Alliance, (ESBA). This is a major independent free membership based organisation representing small business entrepreneurs and self-employed in Europe.

**Federation of Small Businesses  
Press and Parliamentary Office  
2 Catherine Place, Westminster, London SW1E 6HF**  
Telephone: 020 7592 8100  
Facsimile: 020 7233 7899  
E-Mail: [london.policy@fsb.org.uk](mailto:london.policy@fsb.org.uk)  
Website: <http://www.fsb.org.uk>

# About the Author

Robert Baldwin is a Professor of Law at the London School of Economics (LSE), where he teaches regulation and criminal law and is director of the LSE Short Course on Regulation. He is the author of numerous books and articles on regulation, including (with Martin Cave) *Understanding Regulation* (Oxford, 1999).

Since 2003 he has been a Director of Corporate Risk Group, the risk management consultancy, and he has extensive experience of working with private and public bodies on regulatory issues – including HM Treasury, the OECD, the European Commission, The National Audit Office and the Lord Chancellor's Department.

For assistance with this report the Author thanks Indianna Minto, Luke Finch, Amanda Tinnams, Claudio Radaelli, Angus Doran and Elizabeth Start.

# Foreword

---

The creation of the Better Regulation Task Force in 1997 marked a shift away from notions of 'Deregulation' in Government and principles of 'Better Regulation' were adopted. Since then we have, however, seen a record growth in regulations the costs of which disproportionately affect small businesses and the self-employed. Indeed small companies find themselves at a competitive disadvantage as they incur 35% higher compliance costs than large firms.

With this in mind we commissioned Professor Robert Baldwin to analyse the impact of 'Better Regulation' concepts on the Government's legislative programme, as it relates to small businesses. We wanted to evaluate whether the commitment to Better Regulations has made a positive difference or had the opposite affect.

His report highlights that 56% of the private sector workforce is employed in small and medium sized enterprises and that 97% of all businesses employ less than twenty employees. These statistics reveal that small businesses are a vibrant part of the UK economy. This should not, however, be misinterpreted to conclude that small businesses can adapt to regulatory change. It must be emphasised that small businesses cannot continue to absorb the ever increasing

number of regulations that emanate from the European Union and Westminster.

This report seeks to highlight that better regulations have grown considerably during the period since the establishment of the better regulation movement. The report refers to numerous initiatives of the last decade to tackle regulatory burdens all of which have been a disappointment.

The FSB feels there is still a long way to go to improve the regulatory climate for small businesses, but we are heartened that this is still an important commitment for Government and all political parties. In this way we actively support initiatives at the EU level to simplify the *acquis communautaire*, the Better Regulation Action Plan and HM Treasury's Hampton Review on Government Enforcement. Indeed greater use should be made of the Regulatory Reform Act 2001 to reduce legislative burdens and policy makers should carefully apply the Better Regulation Tool Kit. We are eager for these latest initiatives to make rapid progress and deliver the Better Regulation that meets small business expectations.

**Carol Undy**  
*National Chairman*

# Contents

---

<b>1.</b>	Executive Summary	6
<b>2.</b>	Small Businesses and Regulation	8
<b>3.</b>	What is ‘Better Regulation’?	10
<b>4.</b>	The Better Regulation Movement	13
<b>5.</b>	The Better Regulation Tool Kit	17
<b>6.</b>	Measuring the Effects of Better Regulation	27
<b>7.</b>	Conclusion	33
<b>8.</b>	Key References	35

# 1 Executive Summary

## Small Businesses and Regulation

1. Government efforts to improve regulation are coming into their twentieth year and it is time to ask whether regulation, as a result, is now better for small businesses.
2. Small businesses are vital to the UK economy but are disproportionately affected by regulatory requirements, red tape and burdens. Regulation can undermine their competitiveness, capacity to grow and viability.
3. There are identifiable reasons why regulation hits small businesses hard. They have higher compliance costs than large businesses; they are less resilient to regulatory shocks, miscalculations and uncertainties; they lack regulation specialists; their need to grow can be badly affected by regulation; they face large costs of administration (e.g. of taxes) as well as regulatory burdens; and they often need the assistance of government to comply with regulation.
4. What constitutes 'better' regulation may be seen in varying ways by different enterprises. Small businesses have a special vision of 'better' regulation - one that expects, for instance, that assessments of benefits and costs take on board the particular difficulties and expenses that small businesses experience in dealing with regulation; that considers issues of competitiveness, needs for growth and cumulative burdens; and that takes account of small business confidence.

## The Better Regulation Movement

5. The roots of the UK better regulation movement trace back to the deregulation initiatives of 1985. It was, however, 1997 that marked the move away from deregulation to a search for 'better' regulation.
6. The UK Government has pursued 'better' regulation with a number of institutional, political and strategic initiatives. It has set up bodies such as the Better Regulation Task Force, the Small Business Service and the Panel for Regulatory Accountability which all are tasked to consider small business concerns.

7. Legislation has been passed with the aim of reducing red tape, notably the Regulatory Reform Act 2001. Action plans for reducing burdens have been produced and the Prime Minister has shown personal leadership on red tape reductions. Periodically, reviews of business burdens and small business needs have been instigated.

8. Within Europe and the OECD there have also been initiatives on better regulation since the nineties. The European Commission produced an Action Plan for Better Regulation in 1992 and the OECD has led the way internationally in the drive to develop regulatory policies, regulatory improvement tools, and institutions for improving regulation.

## The Better Regulation Tool Kit

9. UK Governments have developed, especially during the last seven years, an extensive toolkit for improving regulation. Tools that have been introduced or refined have included: Regulatory Impact Assessments (RIAs); consultancy and transparency procedures; mechanisms for reducing burdens, removing red tape and simplifying regulation; strategies and guidance for making enforcement more business-friendly; processes for considering alternatives to regulation or to traditional ways of regulating; sunset provisions; and general regulatory improvement policies.

## Measuring the Effects of Better Regulation

10. The better regulation movement has produced a number of outcomes in the form of new governmental tools and strategies for improving regulation. The RIA tool lies at the centre of those outcomes but there is still work to be done to realise the full potential of RIAs so that considering alternatives is embedded within government; costs to small businesses are fully considered; cumulative burdens are taken into account; options for assisting small businesses are scrutinised fully; and quantification techniques are seen as sufficiently reliable to allow RIAs to play a full role in policymaking and legislative processes.

**11.** There is evidence that the better regulation movement has failed to convince small businesses that burdens have been reduced. Surveys reveal that as many as two thirds of small businesses consider that burdens have increased in recent years. Four out of five small businesses think burdens are excessive. Perceptions generally are of a deteriorating situation on burdens.

**12.** Some surveys have suggested that Britain offers entrepreneurs the lowest international levels of barriers to business but small business perceptions are far more pessimistic – more than one survey has revealed that small businesses see regulation as a serious, or even the most serious, obstacle to success.

**13.** Small businesses appear to be growing in satisfaction concerning one aspect of regulatory performance – the level of advice and support they receive. This contrasts with small business perceptions of deterioration in the care with which new regulations are considered; the timing and scheduling of compliance deadlines; and regulators' understandings of small businesses.

**14.** An examination of regulation-making processes reveals a number of reasons why the better regulation movement has not easily produced an increase in the impact of the small business voice.

**15.** Ministers and proponents of regulation may tend to under react to small business concerns due to a series of factors. They are often committed to regulate for ideological or manifesto-related reasons; the costs and benefits of regulation are difficult to quantify and RIAs are commonly not prepared on the basis of representative samples or manageable assumptions and predictions – they are, accordingly, not always treated as convincing. 'Pre-better regulation' attitudes can also reappear so that concerns about burdens are dismissed as objections to regulation per se; the use of enabling legislation reduces opportunities to debate small business fears; legislative timescales may prevent full consideration of burdens; the big business voice often dominates the regulation-making process; and governments have incentives to sustain the constant flow of new regulations.

## Conclusions and Recommendations

**16.** The better regulation movement has produced a large number of initiatives but it has yet to deliver the better regulation that small businesses want.

**17.** Work needs to be done especially to improve performance in using the RIA process and in reducing unnecessary burdens. A full scale cultural change in favour of 'better' regulation still has to be made by many departments and agencies.

**18.** The Cabinet Office Guide to RIAs should demand that all RIAs expressly set out and discuss an array of options for reducing potential regulatory impacts on small businesses.

**19.** When signing-off RIAs, ministers should certify that they meet the requirements of the Cabinet Office Guide to RIAs.

**20.** When signing-off RIAs, ministers should state that there will be a Regulatory Impact Post-Implementation Assessment (RIPIA) to be completed, in normal circumstances, at a stipulated time twelve to eighteen months after a regulation comes into effect.

**21.** When an RIA focuses on enabling legislation and the costs and benefits of regulating will be materially governed by delegated legislation, ministers should, on signing-off an RIA, undertake to carry out secondary RIAs to cover all relevant delegated legislation. Ministers should identify areas where it is anticipated that secondary legislation will have an impact on business, charities or voluntary bodies and will require subjection to the RIA process.

**22.** Improvements in regulatory tools, such as RIAs, may be necessary but may not be sufficient to give small businesses the regulation that they think appropriate. There are limits to what can be done by developing these tools. New questions need to be asked about ways to act positively to increase the voice of small businesses in regulatory policymaking.

# 2 Small Businesses and Regulation

Government efforts to improve regulation are coming into their twentieth year and it is time to ask whether regulation is really better as a result. There is, moreover, a special need to examine whether it is better for small businesses.

Why? Because small businesses are a central force in the UK economy and because regulation bites hardest on smaller enterprises.

## The importance of small businesses

Small firms are economically vital and are collectively, big business<sup>1</sup>:

- There are around 3.8 million small businesses in the UK of which 1.6 million are sole traders.
- They account for 99% of the total number of UK firms.
- They generate more than half of total UK turnover.
- They employ 12.6 million people (56% of the private sector workforce).
- They are key drivers of innovation and new efficiencies.

## Why regulation hits small businesses hard

Regulatory requirements affect small enterprises disproportionately:

- Fixed cost elements of regulatory compliance produce higher relative compliance costs for small firms. OECD evidence reveals that small firms (with 1–19 employees) incur more than three times higher regulatory costs per employee than medium firms (20–49 employees) and more than five times higher costs than large firms (50–500 employees).<sup>2</sup>
- Small firms with 1–2 employees spend nearly five times as many hours per person dealing with regulation than firms with 50 or more employees.<sup>3</sup> They spend over 4% of annual turnover on compliance<sup>4</sup> and businesses with under 20 employees incur 35% higher compliance costs than firms with over 50 staff.<sup>5</sup>
- Small firms are less resilient than large firms to regulatory changes – they have fewer resources to absorb the shocks imposed by new regulatory costs. Regulatory penalties may also affect small firms disproportionately – as where a fine prejudices a self-employed person's ability to secure finance.
- Smaller firms carry out their own administration and do not have the capacity to employ regulatory specialists and so compliance-related work diverts the attention of key managers away from wealth creating activities.

### Footnotes

<sup>1</sup> See: Small Business Service, *A Government Action Plan for Small Business* (DTI: 2004). The SBS defines businesses according to number of employees: Micro = 0–9; Small = 9–49; Medium 50–249; Large – 250 and over.

<sup>2</sup> OECD, *Business Views on Red Tape* (OECD, Paris: 2001) p.8. In a US study, Hopkins has suggested that small firms' regulatory costs are 30% higher per employee than for all firms (T.D. Hopkins, *Profiles of Regulatory Costs* Report to US Business Administration, Office of Advocacy, 1995). Similar disparities in costs are reported in H. Beale and H. Kin, *Impacts of Federal Regulations* Report for the US SBA (Microeconomic Applications Inc Washington DC, 1988). In Sweden a 1997 survey for the OECD found that regulatory costs per employee were almost four times greater for small firms than for larger enterprises – see OECD, *Small Business, Job Creation and Growth, Facts, Obstacles and Best Practices* (OECD, Paris, 1997).

<sup>3</sup> Small Business Research Trust, 'Nat West SBRT Quarterly Survey of Small Businesses in Britain' Vol. 16, No 3 (2000).

<sup>4</sup> ICAEW, *Smaller Businesses and Regulation* (2000) p.8.

<sup>5</sup> ENSR, *Administrative Burdens* in the European Observatory for SMEs, Third Annual Report, 1995.

- The ability of small firms to take business risks is disproportionately affected by regulation which increases costs and demands higher levels of operational gearing. This reduces flexibility and the ability of small firms to exploit new opportunities or invest in research and development.
- Growth is vital to small businesses<sup>6</sup> but they see compliance with regulatory requirements as their number one barrier to growth<sup>7</sup> and around a half see it as a “serious barrier.”<sup>8</sup>
- Small firms face cumulations of regulation as well as the costs of administering employment tax and other bodies of legislation (PAYE, NIC, Employment Law, V.A.T., Climate Change Levy etc). The disproportionate administrative costs relating to such legislation make small firms even less able to cope with regulatory costs. Inland Revenue research shows that firms with 1–4 employees spend £288 per employee per annum on administering legislation, compared to a little over £5 for the 5,000 + employees group.<sup>9</sup>
- Small firms face disproportionate costs in influencing new regulations. Only a minority of small businesses belong to a representative organisation – the FSB is the largest small firms representative organisation, but only 4.5% of small firms are FSB members. This makes regulatory participation difficult and expensive. As the OECD has pointed out, vested interests are accordingly often able to block reforms that would be of benefit beyond concentrated interests.<sup>10</sup>
- Small firms are very dependent on regulators for assistance in interpreting their obligations to comply but, from a regulator’s perspective, small firms are elusive and hard to help. Small firms, moreover, may find even ‘alternative’ regulatory methods, such as

voluntary codes and quality assurance schemes more difficult to comply with than larger firms. Large businesses often welcome the flexibility of goal-based regulation<sup>11</sup> (frequently employing specialists to produce customised compliance solutions) but small firms have particular difficulties with goal-based regulation.

- If regulation proves excessively onerous, governments may rectify the situation but this may be too late for small firms who are less able than large concerns to sustain and survive excess regulatory costs.

The strength of small business concerns about regulation stems from their feeling regulatory costs so acutely. That is why the search for better regulation matters so much to them. What small businesses may want from regulation may, moreover, not prove identical to the demands of other groupings in society. “Better” regulation may mean different things to different persons, interests or groups and it is as well to pause, in the next section, to consider those different meanings.

After the connotation of ‘better regulation’ is discussed, sections three and four below describe the development of the ‘better regulation’ movement and the use of different tools for improving regulation. Attention then turns to measurement and an analysis of regulation in the wake of the better regulation movement. A ‘small business vision’ of better regulation will be borne in mind in asking whether regulation has improved over the last ten or twenty years.

#### Footnotes

<sup>6</sup> Two-thirds have ambitions to grow in the next 5 years – see S. Carter et.al *Lifting the Barriers to Growth in UK Small Businesses*, FSB, (2002) p.5.

<sup>7</sup> ICAEW, *Barriers to Growth* (1996) p.2.

<sup>8</sup> ICAEW, *Small Businesses and Regulation* (2000) p.5.

<sup>9</sup> D. Collard et.al, *The Tax Compliance Costs for Employers of PAYE and National Insurance in 1995–96* (Inland Revenue Economics Papers: No.3, 1998).

<sup>10</sup> OECD, *Regulatory Policies in OECD Countries* (OECD, Paris, 2002) p.21.

<sup>11</sup> In which the regulator stipulates that an end or outcome be achieved but offers freedom as to the method used to achieve it.

# 3 What is 'Better Regulation'?

In the UK the leading formulation of benchmarks for 'good regulation' is set out by the Better Regulation Task Force of the Cabinet Office (BRTF)<sup>12</sup>. Five principles for measuring and improving the quality of regulation and its enforcement were first set out by the BRTF in 1997 and can be summarised as set out in Table 1:

Table 1 **BRTF Principles of Good Regulation**<sup>13</sup>

<b>Proportionality</b>	Regulators should only intervene when necessary. Remedies should be appropriate to the risk posed and costs identified and minimised.
<b>Accountability</b>	Regulators must be able to justify decisions and be subject to public scrutiny.
<b>Consistency</b>	Government rules and standards must be joined up and implemented fairly.
<b>Transparency</b>	Regulators should be open and keep regulation simple and user-friendly.
<b>Targeting</b>	Regulation should be focused on the problem and minimise side effects.

The above principles are supplemented by the BRTF's nine tests of good regulation. These demand that regulation must:

- Be balanced and avoid knee-jerk reactions.
- Seek to reconcile contradictory policy objectives.
- Balance risks, costs and benefits.
- Avoid unintended consequences.
- Be easy to understand.
- Have broad public support.
- Be enforceable.
- Identify accountability.
- Be relevant to current conditions.

There is some overlap between the Principles and the Tests but, overall, it can be seen that there is a focus on accountability, openness, fairness and pursuit of the right objectives at the lowest cost to both society and regulated firms.

Other governments have put forward similar benchmarks. Thus, in January 2004 the Irish Government produced a White Paper, *Regulating Better*<sup>14</sup> that placed particular stress on improving regulation by adopting the following principles:

- Necessity** requiring higher standards of evidence before regulating.
- Effectiveness** targeting new regulations more effectively.
- Proportionality** regulating as lightly as possible.
- Transparency** consulting more widely before regulating.
- Accountability** strengthening accountability in the regulatory process.
- Consistency** ensuring greater consistency across regulatory bodies.

## Footnotes

<sup>12</sup> For a review of benchmarks of regulatory quality see University of Bradford, Centre for European Studies, *Interim Report on Indicators of Regulatory Quality* (CEC, DG Enterprise, 9 May 2004) (website: [www.bradford.ac.uk/irq](http://www.bradford.ac.uk/irq)).

<sup>13</sup> BRTF, *Principles of Good Regulation* (BRTF, Cabinet Office, 2003).

At the supra-governmental level, the OECD<sup>15</sup> has recommended that good regulation should:

- *Be needed to serve clearly identified policy goals and effective in achieving those goals.*
- *Have a sound legal basis.*
- *Produce benefits that justify costs, considering the distribution of effects across society.*
- *Minimise costs and market distortions.*
- *Promote innovation through market incentives and goal-based approaches.*
- *Be clear, simple, and practical for users.*
- *Be consistent with other regulations and policies.*
- *Be compatible as far as possible with competition, trade and investment-facilitating principles at domestic and international levels.*

More generally, the OECD has added that good regulatory systems should be set within effective governmental mechanisms for managing, co-ordinating, reforming and updating regulation and ensuring that regulators and regulatory processes are transparent, non-discriminatory and efficiently applied.<sup>16</sup>

Within the EU, the key statement on principles of good regulation is contained in the 1995 Mandelkern Report<sup>17</sup> which lists seven 'common principles' of regulatory quality.

### **Necessity**

whether new regulations are required.

### **Proportionality**

the need to balance advantages and constraints.

### **Subsidiarity**

the justification for action at European level.

### **Transparency**

the need to facilitate participation.

### **Accountability**

whether there is clear identification of originating authorities.

### **Simplicity**

the ease with which regulations can be used and understood.

The same Report endorses the OECD's 1995 ten point checklist for regulatory decision-making, which asks:

1. Is the problem correctly defined?
2. Is government action justified?
3. Is regulation the best form of government action?
4. Is there a legal basis for regulation?
5. What is the appropriate level of government for this action?
6. Do the benefits of regulation justify the costs?
7. Is the distribution of effects across society transparent?
8. Is the regulation clear, consistent, comprehensive and accessible to users?
9. Have all interested parties had the opportunity to present their views?
10. How will compliance be achieved?

What, though, might small businesses equate with high regulatory quality or 'better' regulation? Small businesses may accept the common thrust of the above approaches – they may see the need for proportionality, accountability, fairness, transparency and targeting – but they may do so from a particular perspective. That perspective is likely to reflect the special challenges that regulation poses for small enterprises. For small businesses, accordingly, high quality regulation may be seen in terms that read familiar benchmarks in a particular way as follows:

**Proportionality:** will be seen as involving balancing of anticipated regulatory benefits with the special costs that regulation imposes on small businesses (e.g. costs associated with disproportionate operational disturbances due to regulatory shock, compliance demands of uncertainties).

**Accountability:** will involve processes that give the small business voice due weight and influence (that avoid discriminating in favour of the largest, best-organised concerns).

**Consistency:** will demand fair treatment so that small firms' costs are not disproportionately affected by regulatory requirements; regulation does not stop small firms from competing on an equal footing with large companies; regulation does not unfairly hinder the growth of small companies (e.g. restricting their ability to take justifiable

### **Footnotes**

<sup>14</sup> Department of the Taoiseach, *Regulating Better* (2004) ([www.betterregulation.ie](http://www.betterregulation.ie)). See also the Australian Government, Department of Industry, Tourism and Resources: *Regulatory Performance Indicators* (Canberra, 1999) which measures whether regulation: confers net benefits; achieves objectives without unduly restricting business; is transparent and fair; is accessible to business; creates a predictable regulatory environment; and ensures responsive consultation. The Australian Office of Regulation Review uses the seven features: minimum necessary to achieve objectives; not unduly prescriptive; accessible; transparent and accountable; integrated and consistent with other laws; communicated effectively; mindful of compliance burdens; and enforceable.

<sup>15</sup> OECD, *Recommendation on Improving the Quality of Government Regulation* (OECD, Paris, 1995).

<sup>16</sup> OECD, *Policy Recommendations on Regulatory Reform* (OECD, Paris, 1995).

<sup>17</sup> Mandelkern Group Report on *Better Regulation, Final Report*, 13 November 2002.

business risks); the cumulative weight of regulation does not unduly impose burdens on small firms; and positive assistance is offered to small firms to allow them to comply with regulations and develop as enterprises.

**Transparency:** will require processes that are open and user-friendly within the constraints of time, resources and expertise that affect small businesses.

**Targeting:** will be seen as demanding: that regulatory process and policies take on board the regulatory side-effects that prove specially burdensome for small firms; and that regulation is practised in a manner that encourages, not deters, small-scale entrepreneurial activity and the creation of new businesses.

In asking whether “better” regulation has been better for small businesses, reference will be made to the above vision of good regulation. First, however, it is necessary to look at the development of the better regulation movement in the UK and supra-nationally.

Table 2

**A Small Business Vision of Good Regulation**

<b>Proportionality</b>	Benefits are balanced against special costs to small businesses.
<b>Accountability</b>	Small business influence is no less important than that of large business.
<b>Consistency</b>	Small business competitiveness is not prejudiced by regulation; growth is not unfairly hindered; the cumulative effects of regulation are considered; positive assistance is provided with information and compliance.
<b>Transparency</b>	Processes are open and user friendly within small business constraints.
<b>Targeting</b>	Regulatory policies take on board small businesses side effects and do not discourage entrepreneurial activity.

# 4 The Better Regulation Movement

## 4.1 The United Kingdom

The roots of the UK better regulation movement lie in a 1985 White Paper, *Lifting the Burden*<sup>18</sup> which stressed the negative effect of regulatory compliance costs on business and the need to deregulate by freeing markets and reducing administrative and legislative burdens. Two further White Papers followed in 1986 and 1988<sup>19</sup> and took deregulation policy into specifics. Compliance Cost Assessments (CCAs) were to be conducted to determine the costs to businesses of proposed regulations. A series of business task forces was established to review more than 35,000 regulations and to suggest areas of governmental activity that could be deregulated.<sup>20</sup> A central task force, the Enterprise and Deregulation Unit, was set up in the Department of Employment in 1986 to oversee the ‘anti-red tape’ efforts of individual departments. A year later the unit was renamed the Deregulation Unit and moved to the Department of Trade and Industry (DTI). In 1989 a Cabinet Committee on regulation was established. A further series of White Papers<sup>21</sup> was produced in 1994 to guide departments on improving regulatory quality and two initiatives were aimed at relieving small business burdens. British ministers and European officials were held to be accountable for minimising burdens and a “think small first” principle was introduced so that regulations would be framed “with the interests of small businesses in mind.” A ‘small business litmus test’ was introduced in 1994. Fast-tracked reductions of burdensome regulation were facilitated with the passing of the Deregulation and Contracting Out Act 1994. The deregulation initiative was placed closer to the centre of government in 1995–6 when the Deregulation Unit was moved to the Cabinet Office and, during that period,

an Advisory Panel of business people was established. Seven new Business Taskforces were created to look at specific sectors.

It was in 1997, however, that the terminological and philosophical switch from ‘deregulation’ to ‘better regulation’ was made. Dr David Clark, Chancellor of the Duchy of Lancaster, introduced the initiative ‘Better Regulation’ in July 1997 and emphasised that some regulatory activity was necessary for public and consumer protection. He said:

*‘Deregulation implies regulation is not needed. In fact good regulation can benefit us all - it is only bad regulation that is a burden.’*

He set up the Better Regulation Task Force (BRTF) to be located at the Cabinet Office. This was an independent advisory body with a majority of members from the business sector and was chaired by leading businessman Chris Haskins.<sup>22</sup> It was charged to take the better regulation initiative forward and was given the express task of considering the needs of “small businesses and ordinary people.” The BRTF acted to advise the Government on the effectiveness and credibility of regulations, to motivate reductions of burdens and to check the administrative complexity of proposals. Within a year of its establishment the BRTF published a set of principles of better regulation (which were subsequently endorsed by the Government) and the Compliance Cost Assessment procedure was replaced by a Regulatory Impact Assessment. The new process included reference to regulatory impacts on charities and the voluntary sector as well as on business.

The new governmental concern with small firms was reflected in a number of developments. The BRTF published a report in

### Footnotes

<sup>18</sup> DTI, *Lifting the Burden* (Cmnd of 9571, 1985).

<sup>19</sup> DTI, *Building Businesses Not Barriers* (Cmnd 9794, 1986); *Releasing Enterprise* (Cm 512, 1988).

<sup>20</sup> See F. Chittenden, S. Kauser and P. Poutziou, *Regulatory Burdens on Small Business* Manchester Business School. These task forces launched 605 deregulatory initiatives see OECD, *From Red Tape to Smart Tape* (OECD, Paris, 2003). UK Chapter by C. Scott and M. Lodge, p.198.

<sup>21</sup> DTI, *Deregulation: Cutting Red Tape* (DTI, London, 1994); *Thinking About Regulation; A Guide to Good Regulation* (DTI, London, 1994); *Getting a Good Deal in Europe* (DTI, London, 1994).

<sup>22</sup> The current chair is David Arculus.

1999 which acknowledged the disadvantages that small firms suffer regarding compliance costs.<sup>23</sup> This was followed by a set of BRTF recommendations to the Government that were aimed at easing burdens on small firms.<sup>24</sup> By this time the Better Regulation Unit had been renamed the Regulatory Impact Unit at the Cabinet Office, Regulatory Reform Ministers had been appointed in each department and a Ministerial Panel for Regulatory Accountability (chaired by a Cabinet Office minister) had been established to scrutinise the implications of regulatory plans and to improve the regulatory system both generally and within departments.

Small business concerns were also reflected in the creation, in April 2000, of the Small Business Service at the DTI with a remit of enhancing support for small and medium sized businesses (SMEs) and to act as an advocate for small businesses within Whitehall. Legislative support for improved regulation was provided with the passing of the Regulatory Reform Act 2001 and the associated announcement of over 50 potential Regulatory Reform Orders. The Labour Government's commitment to better regulation was underlined in the business manifesto to the 2001 election and, more recently, in early 2004, further stimulus was given to the better regulation movement by a number of steps. In March 2004, the Government announced that the Prime Minister would lead the effort to reduce the 'red tape burden' by chairing the Panel for Regulatory Accountability; Sir Peter Gershon, Head of the Office of Government Commerce reported on government efficiency and emphasised the "desperate" need to rationalise regulation and reduce red tape; the BRTF launched investigations into unnecessary regulation and "regulatory creep" (the way regulation grows in unintended ways); and Gordon Brown instigated a review of regulatory inspection burdens by former Lloyds TSB Finance Director, Philip Hampton.

## 4.2 Better Regulation in Europe

For many enterprises the 80,000 page body of European legislation represents the source of a huge set of burdens. Firms in Europe put the cost of regulation at 4% of Community GDP.<sup>25</sup> The Edinburgh European Council of 1992 made the task of simplifying and improving the regulatory

environment one of the Community's main priorities. Nine years later, however, the Commission reported that results fell short of objectives due to "the complexity of the task and the lack of real political support."<sup>26</sup> During the early nineties, for instance, the EU operated its own system of regulatory impact assessment – the *fiche d'impact* – but the DTI Efficiency Scrutiny Report of 1993 characterised these assessments as "perfunctory."<sup>27</sup>

It was only in the mid-nineties that the search for better quality regulation became systematic. A protocol attached to the Treaty of Amsterdam (1995) set out the principles of good regulation to be respected at the European level. Further co-ordinated action was stimulated when the 2000 Lisbon Council of Europe emphasised the need to develop better regulation as a part of making the EU the most competitive and dynamic knowledge-based economy in the world. During that year, Ministers of Public Administration from across the EU met and established the high-level Mandelkern Group to look at ways of improving regulatory quality. The final report of the Mandelkern Group was produced in November 2001 and set down seven core principles of better regulation.<sup>28</sup> It advocated the implementation, to a stipulated timetable, of an Action Plan for Better Regulation based on key recommendations, including the following:

- From 2003 the Commission should produce an annual report to the European Parliament and Council on developments in better regulation.
- Joint programmes on better regulation should be introduced.
- The Commission should propose, by June 2002, a set of indicators of better regulation.
- The Commission should introduce, by June 2002, a new system of impact assessment (to be made mandatory for proposals put to Council or the Parliament after 2002).
- All Member States should introduce, by June 2003, an effective system of impact assessment.
- Adoption by the Commission of a standard minimum consultation period of 16 weeks and adoption by the Commission, by March 2002, of a Code of Practice for consultations.
- Launch, by 2002, of a commission-led programme of simplification of European legislation in all areas.

### Footnotes

<sup>23</sup> BRTF, *Regulation and Small Firms Progress Report* (Cabinet Office, London, 1999).

<sup>24</sup> BRTF, *The Better Regulation Guide and Regulatory Impact Assessment* (Cabinet Office, London, 2000). See also BRTF *Helping Small Firms Cope with Regulations*.

<sup>25</sup> See Commission of the European Communities, *Communication: Simplifying and Improving the Regulatory Environment* COM (2001) 726 Final.

<sup>26</sup> *Ibid.*

<sup>27</sup> DTI, *A Review of the Implementation and Enforcement of EC Law in the UK* (DTI, London, 1993).

<sup>28</sup> Noted above, namely, necessity, proportionality, subsidiarity, transparency, accountability, accessibility and simplicity.

- Creation by the Commission, by 2002, of a single, effective, better regulation network in all regulatory Directorate Generals (DG).
- Drawing up by the Commission of guidelines on the use of alternatives to regulation, by June 2002.
- Developing a concerted Commission, Parliament and Council Plan by June 2002 to codify European regulation, to produce a 40% reduction in European Acts and legislation.
- Improving the online Commission database of regulation requiring transposition by December 2002.

The Mandelkern recommendations were reinforced by the Commission's White Paper on European Governance.<sup>29</sup> This re-asserted the need to improve the "quality, effectiveness and simplicity" of regulatory acts. The White Paper, alongside Mandelkern, accordingly provided the foundations of the Commission's Action Plan for Better Regulation, which was presented to the Seville European Council in June 2002.<sup>30</sup> Key elements of the Action Plan included:

- The introduction by the Commission of a two stage impact assessment process covering economic, social and environmental impacts – to be implemented gradually from 2003 onwards.
- A commitment by the Commission to establish minimum standards for consultation to improve openness and transparency.
- The creation of a programme of simplification of existing legislation aimed at reducing the volume of Community law.
- The establishment of an internal better regulation network within the Commission, involving all the Directorates-General and co-ordinated by the Secretariat-General.

A series of associated initiatives can be seen as part of the same better regulation movement. The Simpler Legislation for the Internal Market (SLIM) initiative was introduced fully in 1998 and was designed to reduce the burden of single market legislation. (Teams of Member State experts and representatives of users of legislation meet regularly to examine specific areas and report to the Commission on proposals for simplification).

A European Business Test Panel was also established in 1998 in order to assess business community responses to proposed

legislative measures. In December 2001 the Commission established the office of the SME Envoy of the Commission in order to feed SME concerns more systematically into EU regulatory and other programmes.<sup>31</sup> The Commission issued a communication on impact assessment in 2002 that committed itself gradually to carry out impact assessments for all major legislative and policy initiatives.<sup>32</sup> Simplification objectives were carried forward with the Commission's 2003 communication on 'Updating and Simplifying the Community Acquis'<sup>33</sup> which undertook, *inter alia* to remove obsolete legal texts; rewrite legal texts to make them more understandable; develop more user-friendly access to consultations on community law; and to replace old policy approaches with "better adapted and proportional regulatory instruments." Other Communications have dealt with 'Better Lawmaking';<sup>34</sup> 'The Operating Framework for the European Regulatory Agencies';<sup>35</sup> and 'Minimum Standards of Consultation.'<sup>36</sup>

More recently, in early 2004, the Irish, Dutch, Luxembourg and British Presidencies agreed a joint initiative to prioritise regulatory reform over the course of 2004–5.<sup>37</sup> This proposed new steps to monitor and support progress on regulatory reform; to nominate a Commission Vice President with responsibility for providing leadership on reform; for gaining annual agreements on proposals to be subjected to Extended Impact Assessment; for establishing an agreed timetable on regulatory simplification; for more active and generalised consideration of alternatives to regulation; and greater commitment to ongoing regulatory reform initiatives at Member State level.

### 4.3 The OECD and Better Regulation

In the last 20 years the OECD has moved the focus of its concerns away from deregulation, regulatory reform and 'regulatory management' towards better regulation through 'regulatory policy' – government-wide policy that aims continuously to improve the quality of the regulatory environment.<sup>38</sup>

#### Footnotes

<sup>29</sup> COM (2001) 428 Final.

<sup>30</sup> European Commission, *Action Plan on Simplifying and Improving the Regulatory Environment* COM (2002) 278 final.

<sup>31</sup> For arguments that the SME Envoy should play a stronger advocacy role for SMEs within the Commission see L. Allio et. al., *Achieving a New Regulatory Culture in the European Union: An Action Plan* (European Policy Centre, Working Paper 10, April 2004).

<sup>32</sup> Communication on Impact Assessment COM (2002) 276.

<sup>33</sup> COM (2003) 3 71 Final.

<sup>34</sup> COM (2002) 275, 05.06.2002.

<sup>35</sup> COM (2002) 718 final, 11.12.2002.

<sup>36</sup> COM (2002) 277 final.

<sup>37</sup> See Irish Presidency, Joint Initiative on Regulatory Reform Letter 26.1.04.

<sup>38</sup> See OECD, *Regulatory Policies in OECD Countries* (OECD, Paris, 2002).

The key step of the OECD in the nineties was the 1995 adoption of the *Recommendation of the Council of the OECD on Improving the Quality of Government Regulation*.<sup>39</sup> This Recommendation set out the first internationally accepted set of principles on ensuring regulatory quality. It included the 10 point OECD Reference Checklist for Regulatory Decision-Making (set out in section 4.2 above). Following that Recommendation, the OECD has sought to promote better regulation in member countries by attention to three key matters:

**Regulatory policies:** the systematic development and implementation of government-wide policies on how governments use their regulatory powers. OECD analyses<sup>40</sup> suggests that successful regulatory policies contain three basic components:

- *Adoption at the highest political levels.*
- *Explicit and measurable regulatory quality standards.*
- *A continuing regulatory management capacity.*

Regulatory policies, moreover, can be seen as needing to attend to both the appraisal of new regulations and the reform of existing regulations. In 1997 the OECD recommended that all member countries adopt such policies with clear objectives and frameworks for implementation.<sup>41</sup>

**Regulatory tools:** these are devices aimed at improving regulatory design and implementation. The essential design tools, in OECD terms, are: Regulatory Impact Analysis (RIA); public consultation; consideration of regulatory alternatives; and compliance burden reduction measures (including administrative simplification and red tape reduction). Implementation tools focus on improving the accountability and fairness with which regulation is applied and include processes of appeals and reviews.

**Regulatory institutions:** these are bodies that take forward regulatory policy. They include regulatory oversight bodies within cabinets and the executive government, and within parliaments. They also include independent regulators and other organisations contributing to better regulation.

If the OECD's 1995 Recommendation can be seen as the first milestone in OECD pursuit of better regulation, the second was the 1997 *Report on Regulatory Reform* which linked regulatory policy with the broader government policy agenda. In its wake followed a series of 'country reviews' of regulatory reform<sup>42</sup> and the OECD has continued to drive forward an emphasis on regulatory policies as a part of broader governmental improvement. At the current time, almost all OECD countries have adopted policies on regulatory quality and the OECD has produced a series of leading-edge publications on strategies for improving regulatory policies, tools and institutions. Reports have, for instance, dealt with the following:

- *Choices of Policy Instruments (1997).*
- *Regulatory Reform (1995, 1997).*
- *Regulatory Impact Analyses: Best Practices in OECD Countries (1997).*
- *Voluntary Approaches for Environmental Protection (1998, 1999).*
- *Information, Consultation and Public Participation (2000).*
- *Regulatory Compliance (2000).*
- *Business Views on Red Tape (2001).*
- *Regulatory Reform in the UK (2002).*
- *Administrative Simplification in OECD Countries (2003).*

As a result of the above, and other initiatives, the OECD can be seen as a major driver of the better regulation movement in the UK as well as other member countries. The OECD has, as much as anything, encouraged those countries to develop a complete set of tools for improving regulation. It is to the development of that 'better regulation toolkit' in the UK that we now turn.

#### Footnotes

<sup>39</sup> OECD/GD (95) 95 OECD, Paris (1995).

<sup>40</sup> See OECD (2002) p.29.

<sup>41</sup> OECD, *The OECD Report on Regulatory Reform* (OECD, Paris, 1997). By late 2000, 24 out of 30 OECD countries had adopted government-wide regulatory policies. The UK did so in 1985 (OECD, 2002, p.40).

<sup>42</sup> The UK Review was carried out in 2001–2: see OECD, *United Kingdom: Challenges at the Cutting Edge* (OECD, Paris, 2002).

# 5 The Better Regulation Tool Kit

UK governments have developed a number of tools for improving regulation and it is worthwhile considering these and their significance for small businesses. One issue is whether small business friendly tools have been developed, another is whether they have operated in a manner that enhances small business prospects.

## 5.1 Regulatory Impact Assessments (RIAs)

In August 1998 Tony Blair announced that no regulatory policy proposal that impacted on business, charities or voluntary bodies would be considered by Ministers without a RIA being carried out. This involves an assessment of the impact of policy options and covers the purposes, risks, benefits and costs of the proposal and also considers: how compliance will be obtained; expected impacts on small business; the views of affected parties; and the criteria to be used for monitoring and evaluating the regulatory activity at issue. The RIA process precedes a recommendation to ministers and, in carrying out the RIA, the alternatives to regulatory options for achieving policy objectives must be considered. Since the RIA system was introduced, almost 900 RIAs have been issued, at around 160 a year.<sup>43</sup>

RIAs are carried out by regulatory agencies and Departmental Regulatory Impact Units (DRIUs).<sup>44</sup> Guidance is offered by the Cabinet Office Regulatory Impact Unit (RIU). Each RIA will be drafted at an early stage in policymaking and should be developed following consultation. The DTI's Small Business Service (SBS) advises those conducting a RIA of the small business implications of a regulatory proposal and the SBS can

have its views recorded on the face of a RIA. The final RIA will be submitted to the relevant Government minister who is asked to sign it off with a statement that, in their opinion, the benefits justify the costs. The final version accompanies the submission of legislation.

RIAs are intended to inform decision-making, not to determine decisions or to substitute for political accountability. They are designed to encourage better regulation by the following means:

- Clarifying regulatory objectives and definitions of problems.
- Ensuring that regulatory objectives are achieved effectively and at lowest cost by the strategy that maximises benefits over costs – be that regulatory or non-regulatory.
- Identifying alternative options for achieving desired objectives.
- Identifying the informational needs of policymakers.
- Unpacking assumptions about compliance effects and real world (including business) impacts.
- Facilitating ministerial and parliamentary scrutiny of regulation.
- Increasing regulatory accountability and transparency.
- Furthering the BRTF's five principles for good regulation: transparency, proportionality, targeting, consistency and accountability.

If RIAs are carried out expertly and used astutely the hope is that they will enhance regulatory policy-making. Effective use of RIAs does, however, involve a series of technical and other difficulties,<sup>45</sup> notably concerning: the availability of good data, the assumptions to be made on values underpinning the RIA; the consistency of RIAs with statutory social objectives; the

### Footnotes

<sup>43</sup> See T. Ambler, F. Chittenden and M. Obodovski, *Are Regulators Raising Their Game: UK Regulatory Impact Assessments in 2002/3* (British Chambers of Commerce, London, 2004) (hereafter 'BCC 2004'). See also T. Ambler, F. Chittenden and M. Shamutkova, *Do Regulators Play by the Rules?* (British Chambers of Commerce, London, 2003) (hereafter 'BCC 2003').

<sup>44</sup> From January 1999 to December 2000, 283 RIAs were conducted by government departments – see NAO, *Better Regulation* HC 324, Session 2001–2, 15.11.2001, p.43.

<sup>45</sup> See e.g. OECD (2002) pp.48–51; R. Baldwin and M. Cave, *Understanding Regulation* (Oxford 1999) Ch 7, National Audit Office (NAO) *Better Regulation: Making Good Use of Regulatory Impact Assessments* (HC329 Session 2001–2, 15 November 2001) (NAO 20–1); NAO, *Evaluation of Regulatory Impact Assessments Compendium Report 2003–4* (HC358, Session 2003–4, 4 March 2004).

timing of the RIA; and administrative resistance to the RIA process.

What is clear from the Cabinet Office's guidance on RIAs<sup>46</sup> is that small business concerns should be taken into account in conducting a RIA.<sup>47</sup> An integral part of each RIA has to be a Small Firms Impact Test. This demands that proponents of a policy ask whether the proposal has an impact on small businesses – if necessary informal discussions with a number of small businesses or a representative group should be undertaken.<sup>48</sup> The Small Business Service (SBS) should be consulted. If there is an expected impact, a Stage 1 initial sounding on a range of options must be made with small businesses to reveal possible unintended consequences and contentious issues. Findings from the initial sounding are to be researched in the initial RIA.<sup>49</sup> If anticipated impacts are significant, Stage 2 focus groups or panels should be arranged to explore options in detail. (The SBS issues detailed guidance on this process). The results of Stage 1 and Stage 2 investigations are then to be used to revise questions for public consultation. The full RIA must publish the findings of both stages. All of the above analysis is designed to inform the RIA submission to ministers and to guide the decision-making on the proposed policy.

Examinations of the RIA process have, however, revealed some difficulties in taking account of the potential small business impacts of proposed regulations. When the National Audit Office examined 23 'test case' RIAs in 2001<sup>50</sup> it found that policy makers did not necessarily understand how to identify and evaluate likely impacts on small firms, nor how to consider options to limit the applicability of regulation to small business. There was, moreover, little widely available guidance on the application of the small firms litmus test. The NAO recommended that the SBS took action on these fronts. On the matter of consultation, the NAO found that it was not easy

for policymakers to obtain informed responses from small businesses for the purposes of evaluating impacts. It recommended that the SBS should develop focus groups and networks of small businesses to assist on these fronts and that the SBS could use business panels to give feedback on regulatory proposals – a model adopted in some other countries such as the USA and Denmark.<sup>51</sup>

By the time the NAO reported on ten further sample RIAs in 2004<sup>52</sup> the SBS had produced detailed guidance on how to run small business focus groups. The NAO's 2004 study revealed, however, a number of difficulties with the RIA process that may be of concern to small businesses:<sup>53</sup>

- Only half included "a reasonably clear statement of objectives."
- Seven out of ten did not consider any option for regulation other than the one preferred by the department. They did not, moreover, consider a 'do nothing' option.
- No risk assessments considered what would happen in the absence of the regulation.
- Consultations were generally well conducted but there was variation in the records that were prepared by the department on how consultations had affected policies and in some cases these risked the perception that responses had been ignored.<sup>54</sup> A good consultation did not always lead to a good RIA.
- All RIAs studied had considered costs to small businesses but had concluded that there would be none or that that they would not be disproportionate.<sup>55</sup>
- All acknowledged a level of uncertainty about data used for estimates but such uncertainties were not always reflected in the cost and benefit figures used which presented single point estimates rather than ranges. Only one out of ten gave the results of sensitivity tests.
- Only three out of the ten contained quantified estimates of benefits (often no market for benefits existed making quantification difficult). Most RIAs accordingly did not offer a quantified comparison of expected costs and benefits.

#### Footnotes

<sup>46</sup> See Cabinet Office, *Better Policy Making: A Guide to Regulatory Impact Assessment* (Cabinet Office, London, 2003) ([www.cabinet-office.gov.uk/regulation](http://www.cabinet-office.gov.uk/regulation)).

<sup>47</sup> The record should include details of companies consulted; how contacted; issues raised, whether a significant impact was revealed and whether Stage 1 changes the substance of the recommendation to Ministers (On Stage 2 see text below).

<sup>48</sup> Ibid para 2.62. A small business is defined in the guidance as one with less than 50 employees and no more than 25% owned by another enterprise that is not a small business and either: less than £4.44 million turnover or less than £3.18 million annual balance sheet total.

<sup>49</sup> The record should include details of companies consulted; how contacted; issues raised; whether a significant impact was revealed and whether Stage 1 changes the substance of the recommendation to ministers.

<sup>50</sup> NAO (2001).

<sup>51</sup> NAO (2001) p.10.

<sup>52</sup> NAO (2004).

<sup>53</sup> It should be emphasised, however, that the sample of RIAs examined by the NAO was not intended to be representative of RIAs conducted across Government. Six of the ten were RIAs that the BRTF had put forward as of poor quality and only one was explicitly an example of a good RIA – see NAO (2004) p.3. For a similarly critical view of RIAs in Sweden see NNR, *The NNR Regulation Indicator for 2002* (Board of Swedish Industry and Commerce for Better Regulation, June 2002).

<sup>54</sup> NAO (2004) p.6.

<sup>55</sup> Not all RIAs do consider small business effects – see BCC 2003.

- Only half of the sample RIAs considered enforcement and sanction effects.
- Most RIAs described how the regulation would be monitored but “often in a very brief and vague way” and only four stated that there would be a formal review to evaluate the success of the regulation.

The NAO’s findings are broadly in line with, though perhaps less critical than, the British Chambers of Commerce (BCC) studies of 2003 and 2004 which looked respectively at 499 and 167 RIAs produced by government in the two periods studied (1998–2002 and 2002–2003).<sup>56</sup> The BCC studies noted the following problems with RIAs:

- Only 3% of RIAs considered SMEs’ differentiated (pro-rata) costs (BCC 2004).<sup>57</sup>
- Ministerial statements that benefits justified costs were not in general supported by the evidence in the RIAs (BCC 2004).
- The option of not regulating was considered in only a minority of cases (11% in 1998–2002 and 23% in 2002–3).
- Less than half of RIAs (44%) quantified all the options considered (BCC 2003).
- Costs for business were only quantified in 23% of RIAs (BCC 2004).
- A quarter of RIAs did not consider SMEs (BCC 2003).
- Some departments are under resourced or badly managed for conducting RIAs (BCC 2004).
- Departmental Regulatory Impact Units do not appear to recognise the impact that a lack of economies of scale has upon the relative costs of SMEs (BCC 2004).
- A substantial minority of RIAs contain little factual data about consequential costs and benefits (BCC 2004).
- Most RIAs contain only a very high level summary of consultations (BCC 2004).
- Scant attention is given to ‘sunset’ clauses or to subsequent monitoring or evaluation (BCC 2004).
- There is little evidence that RIAs reduce the number of regulations and they seem to be used to promote rather than objectively to assess regulations (BCC 2003).
- The RIA process shows little recent evidence of improvement (BCC 2004).

Some of the problems listed affect the value of RIAs to all parties concerned with proposed regulations (e.g. problems of benefit quantification) but some are of special concern to small businesses, notably: failures to consider alternative options and ‘do nothing’ strategies; weak linkages between consultations and RIA recommendations; the lack of sensitivity analyses; apparently easy assumptions that effects on small businesses were absent or not disproportionate; failures to consider sanction effects (which may impact on small business disproportionately);<sup>58</sup> and failures to cater for evaluative mechanisms. On the last issue, an earlier point should be re-emphasised: mechanisms for evaluating regulation and reforming excessively onerous regulation are particularly important to small businesses since small firms lack the capacity to withstand and survive excessive regulation for any extended period.

UK businesses, as indicated, are not merely affected by regulations with domestic origins. Around 40% of new regulations affecting business are calculated to stem from Brussels.<sup>59</sup> The UK’s RIA processes apply to implementing provisions<sup>60</sup> and the European Commission has, for its part, carried out (in qualified form) impact assessments since the Business Impact Assessment system was introduced in 1986. European impact assessments have, as noted, however, possessed many shortcomings. These were analysed between 2000 and 2002 and a new Impact Assessment system was outlined by the *Communication on Impact Assessment* of 5 June 2002. This formed part of the Better Regulation Action Plan and aimed to analyse the effects of European regulatory proposals on business in order to conduce to competitiveness, innovation and growth.<sup>61</sup> The first year for carrying the new Impact Assessment process was 2003 and so it is early to draw conclusions. A review by the European Policy Centre has, however, suggested that only 30% of proposals have been assessed and there are a number of general failings, notably: to list alternatives; to comment on or quantify impacts; and to identify data gaps.<sup>62</sup>

For small businesses, the difficulty with the European RIA process is that it brings with it the problems of the UK system

## Footnotes

<sup>56</sup> See BCC 2003 and BCC 2004.

<sup>57</sup> This figure dropped from 4% in 1998–2002 (BCC 2003).

<sup>58</sup> The BRTF has recommended that RIAs should ‘stress test’ regulations by sector and size so as to indicate the industry sectors and size of businesses that will be most affected, see BRTF, *Employment Regulation: Striking a Balance* (2002) p.8. *The Cabinet Office Guide to RIAs* (2003) demands identification of business sectors affected.

<sup>59</sup> OECD (2002) p.56.

<sup>60</sup> The British Chamber of Commerce has suggested that in 1998–2002 58% of RIAs related to UK and 42% to EU legislation – see BCC, 2003.

<sup>61</sup> For a proposal to increase scrutiny of better regulation processes in the EU institutions – by establishing an independent Regulatory Audit Bureau in the Court of Auditors see L. Allio, B. Ballentine and D. Hudig, *Achieving a New Regulatory Culture in the European Union* (European Policy Centre, Working Paper No. 10, April 2004).

<sup>62</sup> See L. Allio et. al (2004).

– but in more acute form. A special problem that flows from combining the UK and European legislative regimes is, moreover, that implementing civil-law based regulation through the UK’s common-law based approach produces dangers of “gold-plating” and over implementation of EU directives.<sup>63</sup> A further danger is of ‘double banking’ – whereby firms have to comply with parallel UK and EU legislation. The UK Government has sought to counter such dangers with Cabinet Office guidance<sup>64</sup> but small businesses, for reasons already noted, have special reasons to worry about their capacities to withstand gold-plated regulation.

## 5.2 Consultations and Transparency

Public consultation has long been seen as a tool for improving regulation by allowing those parties who are affected by regulation to input into regulatory processes their expertise, perspectives and ideas for alternative actions. Consultations help to: inform regulators and balance opposing interests; identify unintended effects and practical problems; quality check RIAs; and identify interactions between regulations as well as cumulative effects. The consultative tool is given an important place in the OECD’s strategy for better regulation<sup>65</sup> as well as that of the European Union.<sup>66</sup>

Public consultations, moreover, contribute to regulatory transparency – the capacity of regulated entities to identify, understand and express views on relevant obligations and policies. Where regulation is open this improves accountability, helps to reduce arbitrariness and conduces to the fair consideration of affected interests.

In the UK, the RIA process, as noted, incorporates consultative arrangements, notably in evaluating small business impacts, but, more generally, any consultative requirements for regulations tend to depend on secondary legislation and non-

statutory arrangements. As the OECD review of UK regulation noted, however, the UK has a long-established tradition of well-respected consultation.<sup>67</sup> It has required consultation with business since 1985 and the UK Government has produced a number of initiatives in this area. A guide on best practice in written consultation exercises was produced in June 1998 and the Government published an evaluation of the guide’s use in 2000. This noted, however, that less than half of departments used the guide, quality of consultation was variable, consultation results were inadequately disseminated, and the weighting of comments was criticised by business.<sup>68</sup>

A response to the evaluation came with a package of measures in November 2000 including a new code of practice and a commitment to set up a register of all main consultations. The code sets down consultation criteria<sup>69</sup> and stipulates twelve weeks as the minimum consultation period. In the UK there is increasing use of ‘notice and comment’ procedures with disclosures set out on one Website. Consistently with the White Paper *Modernising Government*<sup>70</sup> the Government plans to take forward web-based schemes of consultation as part of its aim to make 100% of all dealings with government capable of being done by the public electronically by 2008. Access to legislation has now eased via the Internet.

As a package, UK regulatory consultation procedures have been characterised as “impressive” and “consistent with international good practices for flexibility, transparency and accessibility.”<sup>71</sup> The OECD has, however, noted that “consultation fatigue appears to be a growing issue.” Such fatigue is likely to afflict small businesses rather sooner than large enterprises and the role of the SBS (as well as bodies such as the FSB) is vital in assisting small business participation. It may well be the case, also, that as consultation becomes increasingly electronic there becomes a case for offering greater assistance to small enterprises in participating by the electronic route.<sup>72</sup>

### Footnotes

<sup>63</sup> For a discussion see: T. Ambler, F. Chittenden and M. Obudovski. *How Much Regulation is Gold Plate?* (BCC, London, 2004). For leading business organisation’s complaints about gold-plating see Institute of Directors, *Your Business Matters* (1996) p.9.

<sup>64</sup> Cabinet Office, *Transposition Guide* (Cabinet Office, London 2003); *Better Policy-Making* (Cabinet Office, London, 2001).

<sup>65</sup> OECD (2002) pp.69–71.

<sup>66</sup> See Mandelkern Group *Report on Better Regulation, Final Report*, 13 November 2001, pp.26–32.

<sup>67</sup> OECD (2002) p.57, Command papers play an important role in publicising major reforms. 408 such papers were produced in 2000.

<sup>68</sup> OECD (2002) p.57.

<sup>69</sup> The guideline criteria state that timing should be made available from the start of planning; it should be clear who is being consulted, the consultation document should be as simple and precise as possible; documents should be widely available; twelve weeks should be the minimum period for consultations; responses should be dealt with open-mindedly; and consultations should be monitored and evaluated.

<sup>70</sup> Cabinet Office, *Modernising Government* Cm 4310 (1999)

<sup>71</sup> OECD, (UK Report) (2002) p.58.

<sup>72</sup> The BRTF’s report on Payroll Regulation (2000) emphasised the need to enable smaller businesses to access the newest technology.

### 5.3 Reducing Burdens and Red Tape: Administrative and Regulatory Simplification

In the UK, efforts to improve regulation by reducing burdens on business have spanned both programmes designed to reduce *administrative* burdens and strategies to lessen *regulatory* burdens.<sup>73</sup> With the former, the emphasis has been on reducing the requirements involved in interactions between individual firms or other actors and government, or on minimising form-filling and tax administration costs. With the latter, the focus has rested on reducing costs. There is, however, considerable overlap between the two and both aspects of simplification will be considered here.

UK Governments have given high priority to reducing unnecessary legislative requirements ever since the modern movement to reform regulation commenced in 1985. The Deregulation and Contracting Out Act 1994 offered a legislative means to ignite the ‘bonfire of red tape’ that so many politicians had promised. By 1995, when the Cabinet Office took over from the DTI as the central government’s driver of regulatory reform, it was clear, however, that much was still to be done to reduce red tape. A regime was introduced whereby departments would report monthly on planned regulation and departments were cautioned against ‘gold-plating’ the transposition of EC directives.<sup>74</sup> The Government’s commitment to better regulation and simplification was emphasised in the 1999 White Paper, *Modernising Government*<sup>75</sup> and red tape was responded to with the creation of the BRTF (1999), the Small Business Service (2000) and the Cabinet Office’s Panel for Regulatory Accountability (now chaired by the Prime Minister).

New underpinnings for the ‘war on red tape’ were provided by the Regulatory Reform Act 2001 (RRA) which enhanced and widened the use of the Deregulation Orders that had originated in the Deregulation and Contracting Out Act 1994. Since that date ministers had been empowered to repeal and amend primary legislation by means of secondary legislation. The aim had been to reduce not only burdens of regulatory compliance but the administrative burdens of excessively complex rules or overlapping and outdated regulations. In the years 1995 to 2000, however, only 48 deregulation orders had been pursued and the RRA 2001 was designed further to ease

the removal of regulatory inconsistencies and anomalies. It allowed constraints of parliamentary time to be overcome by operating through consultation and scrutiny by parliamentary committee rather than by conventional legislative procedures.<sup>76</sup>

Following the passing of the RRA 2001, the Government committed itself to producing an Action Plan on Regulatory Reform. This emerged in February 2002<sup>77</sup> and itemised over 260 proposals for changes to reduce administrative and regulatory burdens. It noted progress made since 1997 by, for example, removing 51 sets of regulations and two Acts in the health and safety field and reforming licensing laws through use of the RRA 2001. The simplification measures proposed in the Action Plan included such terms as rationalising fire safety regulation (which was spread over 120 Acts); removing some burdensome requirements and consolidating in the area of weights and measures and streamlining the planning system.

Reviews of regulatory measures have been conducted within departments (e.g. the DTI in 1999) and RIA guidance urges that simplified procedures should be considered by all regulators.

The target to make all dealings with government capable of being delivered electronically by 2008 also serves as a stimulus to lower costs. The Office of the e-Envoy was set up in September 1999 within the Cabinet Office in order to “lead the drive to get the UK online” and the Government’s e-Government strategy from April 2000 onwards contains a range of measures designed to reduce the burdens of administrative regulations.<sup>78</sup>

The BRTF’s report on *Payroll Regulation* (2000) stressed the benefits of modern technology. It looked at social regulation and those requirements for employers to be responsible for paying out ‘working families’ tax credits. The report stressed the potential benefits of automated payroll systems and the need to enable small businesses to access the latest technology.

‘One stop shops’ constitute a further way to simplify regulatory compliance. They are offices or websites where businesses and citizens can process numbers of different regulatory issues. A development in the direction of ‘one stop shops’ is represented by the Small Business Service whose

#### Footnotes

<sup>73</sup> See C. Scott and M. Lodge, ‘Administrative Simplification in the United Kingdom’ in OECD, *From Red Tape to Smart Tape* (OECD, Paris, 2003).

<sup>74</sup> See Cabinet Office, *Transposition Guide: How to Implement European Directives Effectively* (Cabinet Office, London, 2003) p.17.

<sup>75</sup> Cabinet Office, *Regulatory Reform: The Government’s Action Plan* (Cabinet Office, London, 2002).

<sup>76</sup> For a review see House of Common, *First Special Report, The Operation of the Regulatory Reform Act 2001: A Progress Report* (HC (2002–2003) 908).

<sup>77</sup> Cabinet Office, *Regulatory Reform: The Government’s Action Plan* (Cabinet Office, London, 2002).

<sup>78</sup> A public web page ([www.businesslink.org](http://www.businesslink.org)) has the objective of helping smaller companies regarding the interpretation and compliance with different regulations.

aims are *inter alia* to strengthen the input of small business views into governmental processes and to simplify and improve the quality of business support. It has a staff of around 30 dealing with regulatory issues and, as noted, has a key role in the RIA procedures. The SBS has published a series of regulatory guides and fact sheets and by 2001 had started work on a series of sector-specific guides specifically aimed at small and medium sized businesses.

The Government has also launched initiatives on one-stop shops in respect of land use obligations and licensing for alcohol, public entertainment and other functions.<sup>79</sup> The DTI's Business Link organisation also provides one-stop guidance on, for example, regulatory and taxation requirements attending business start-ups.<sup>80</sup>

For its part, the BRTF has published a series of reports on strategies for simplifying and reducing the burdens of regulation. In its analysis of *Employment Regulation*,<sup>81</sup> for instance, it recommended that the commencement dates for employment regulations should be grouped together. The BRTF, moreover, has taken a lead on reforms of special significance to small firms. Its Payroll Review of 2000 responded to a particular concern of small business – the burdens of tax and benefit administration though the payroll – notably regarding PAYE, National Insurance Contributions, Statutory Sick Pay, Statutory Maternity Pay, Child Support Agency payments, tax credits, student loan repayments, and contributions to stakeholder pensions. The BRTF recommended, *inter alia* that the Inland Revenue should examine ways to simplify the calculation of tax for the smallest employers, offer all new employers an automated payroll service and enhance small businesses' access to new technology by offering financial support and training. The Government subsequently welcomed the report, stating that its taxation plans would encourage small business use of IT, including internet-based payroll services.

At the European level, the Commission's 2002 *Action Plan for Simplifying and Improving the Regulatory Environment*<sup>82</sup> involved the creation of a programme of simplifying existing legislation and reducing the volume of Community law. In February 2003 the Commission went further and launched a new rolling

programme for the simplification of European legislation. This was designed to complement the SLIM (Simpler Legislation for the Internal Market) Programme that had commenced in 1998 with the aim of simplifying and reducing the burdens of European requirements.

These developments built on the Mandelkern recommendations that Europe and Member States should adopt a systematic, targeted and rolling programme of regulatory simplification in all areas, a programme that should be:

- Made up of annually-reviewed steps.
- Comprised of prioritised areas.
- Marked by clear targets and methods.
- Fully resourced.
- Involving business and other 'recipients' of regulation.
- Connected with a review of existing regulation.
- Combined with the repeal of old regulation.
- Consistent with the use of ICT to re-engineer procedures.

Across OECD member countries there has been a general trend to seek to simplify and ease regulation<sup>83</sup> by such methods as: burden reducing programmes; quantitative targets; burden measuring; reallocations of responsibility; streamlined processes; and use of information and communication technologies. In such endeavours four trends have been noted:<sup>84</sup>

- A shift from *ex-post* to *ex ante* burden reduction.
- A move towards 'top down' government initiatives on simplification.
- An increasing pressure from market-based policies in the direction of simplification.
- IT driven moves to cut red tape.

The OECD has, moreover, identified three strategies for dealing with the particular difficulties that small enterprises experience with red tape. A first is to provide special assistance and guidance with compliance requirements; a second is to make requirements less stringent for small businesses; and a third is to design regulation with SMEs in mind by establishing appropriate RIA procedures or government bodies dedicated

#### Footnotes

<sup>79</sup> See Scott and Lodge, loc.cit.

<sup>80</sup> See Business Link, *The No Nonsense Guide to Government Rules and Regulations for Setting up your own Business* (DTI, London, 2003). In 1996 the Institute of Directors, CBI, BCC, FSB and other leading UK business organisations welcomed 'one stop shops' for advice and advocated extension of publicity for the Business Link regime. They did, however, advocate a "less bureaucratic" approach to Business Links – see IOD, *Your Business Matters* (1996).

<sup>81</sup> BRTF, *Employment Regulation: Striking a Balance* (2002) BRTF.

<sup>82</sup> COM (2002) 278 final.

<sup>83</sup> See OECD, *From Red Tape to Smart Tape* (OECD, Paris, 2003). For a review of practices in twenty countries see: RAMBOLL *Management and ITPS* (Sweden), *Efforts to Reduce Administrative Burdens and Improve Business Regulation* (Denmark: Ministry of Business and Economic Affairs, August 2003).

<sup>84</sup> Ibid.

to helping small firms and representing them within government.<sup>85</sup>

Exemptions from regulation are another tool for improving regulation by helping small business to cope with complex or burdensome controls. Exemptions are encountered in the UK in a number of regulated areas. Firms with under five employees, for instance, are exempt from some health and safety rules and do not have to set up a stakeholder pension scheme. Firms with under fifteen employees are exempt from the employment provision of the Disability Discrimination Act. Other exemptions apply to such areas as union recognition, company abbreviated accounts, and publication requirements in directors' reports. (For a table of examples see BRTF, *Helping Small Firms Cope With Regulation* (2000) Appendix G).

The BRTF produced a foundation report<sup>86</sup> on exemptions in 2000 that began by warning that regulators had failed to consider what it was like to run a small business<sup>87</sup> and calling on the Government to take “a strategic view of the cumulative effect of all regulations on SMEs.” The BRTF found that businesses were often in favour of exemptions but that employee and consumer groups tended to oppose removals of protections. SMEs tended to favour not merely exemptions but also better information, simplified procedures and compensation for burdens. Exemptions, said the BRTF, might be useful where regulatory burdens put SMEs at a significant competitive disadvantage or where small firms needed help with an administrative burden. The case against them was strongest where the protection of citizens or consumers was at issue. The Task Force recommendation was that where exemptions were the preferred approach, the level of the threshold involved should have a clear, published rationale.

Compensation is a further tool for improving regulation that the BRTF considered in its 2000 report on small firms. This was most appropriate, said the BRTF, when a burden was transferred from the state to the private sector without the entrepreneur feeling any benefit. Compensation could be paid on a sliding scale to reflect costs and to allow firms to pay for external expertise. An example of practice on such lines was found by the BRTF in arrangements for Statutory Maternity Pay, where small employers are permitted to claim reimbursement from the state at a higher rate than larger firms.

Has action on the above fronts produced better regulation for small businesses? It can at this stage be said that the development of new tools and institutions, together with a new policy emphasis on small business concerns, at least lays a foundation for better regulation. Whether the net effect on the ground is “better regulation” as envisaged by small businesses is a matter to be returned to in section 6 below.

## 5.4 Enforcement Guidelines

The quality of regulation depends not merely on the design of the control system or the nature of rules and requirements but on how controls are applied on the ground. Enforcement guidelines, accordingly, constitute an important tool for regulatory improvement. A small business, for instance, will be interested in such matters as whether enforcement officials give assistance in compliance, whether timeframes for obeying rules are reasonable, and whether enforcement policies take account of the difficulties that small concerns may have in taking certain compliance steps. From the regulator's point of view, enforcement strategies are important in ensuring that objectives are met effectively, economically, accountability, openly and fairly.

Section 5 of the Deregulation and Contracting Out Act 1994 offered protection against the unreasonable application of regulations but it was only applied once.<sup>88</sup> The Labour Government has opted to control enforcement not by statute but by resort to a voluntary code – the Enforcement Concordat. This was devised by the BRTF, signed by the Government in March 1998, and has been adopted by more than 95% of local authorities and central government agencies.

The Concordat signatories agree to help businesses and others to meet their regulatory obligations without unnecessary expense. The principles of good enforcement policy call, amongst other things, for:

- *Clear standards of performance, published and reported on.*
- *The provision of plain language information on rules, widely disseminated.*
- *Openness about working methods and any changes.*
- *Helpfully and actively working with businesses, especially small ones, to assist with compliance.*
- *Clear explanations from enforcers.*

### Footnotes

<sup>85</sup> OECD (2003) p.40.

<sup>86</sup> BRTF, *Helping Small Firms Cope with Regulation: Exemptions and Other Approaches* (BRTF, 2000).

<sup>87</sup> *Ibid*, p.17. For advocacy of exemptions see IoD, *Your Business Matters* (1996).

<sup>88</sup> Scott and Lodge *loc.cit* p.212. Section 5 was repeated by the Regulatory Reform Act 2001 which gave ministers a reserve power to set out a code of good practice in enforcement.

- *The opportunity to resolve difference before formal enforcement action is taken.*
- *Information on rights of appeal.*
- *Fair, practical, proportionate and consistent enforcement.*
- *Well-publicised, timely and effective complaints procedures.*

The Small Business Service promotes the Enforcement Concordat and, to this end, has produced a good practice guide.<sup>89</sup> As for action on the ground, when the BRTF investigated enforcement activity in 1999<sup>90</sup> it was addressing concerns about consistent and efficient enforcement that had been raised in the course of other Task Force reviews. It looked closely at fire safety and health and safety enforcement and noted that small firms had a problem with guidance on enforcement. The difficulty was not the absence of guidance but that there was too much of it and that it assumed a certain level of knowledge, expertise and systems. Small firms wanted guidance to be more user-specific and explicit about what they were expected to do. They also wanted correspondence to be in plain English. The BRTF made a recommendation to this effect. It also provided a 'Good Practice Checklist for Regulators' which advocated, *inter alia* a risk-based approach to inspection and the use of "secondments and training to raise awareness of business concerns and pressures to encourage the practical application of enforcement."<sup>91</sup>

## 5.5 Alternatives to Traditional Regulation

The routine consideration of alternative ways to achieve policy objectives constitutes a tool of regulatory improvement insofar as it encourages regulators to seek out strategies for achieving their given aims at least cost. Thus the OECD has argued that a crucial challenge for regulatory policy is to encourage cultural changes within regulatory bodies so that regulatory and non-regulatory policy instruments are systematically considered when objectives are to be pursued.<sup>92</sup> Policy instruments that might be used include, for instance; information campaigns, performance-based regulation, process regulation, voluntary commitments, deregulation, contractual arrangements, co-regulation, taxes and subsidies,

self-regulation, insurance schemes and tradeable permits.

As indicated above, the RIA process demands that alternative policy instruments and strategies are considered alongside any given proposal. UK governments, more generally, have an established tradition of promoting alternatives to state regulation. Self-regulatory regimes, for instance, are encountered in the advertising field and approved codes are provided for under the Fair Trading Act 1973. Since the Conservative administrations of the 1980s and 1990s, competition has been encouraged as an alternative to regulation, especially in the utilities.

Systematic overviews of alternatives to state regulation and to 'traditional command regulation' have been undertaken by the BRTF, whose 2000 report *Alternatives to State Regulation*<sup>93</sup> recognised that state regulation was not necessarily the best way to achieve policy objectives. The BRTF developed its approach with *Imaginative Thinking for Better Regulation*,<sup>94</sup> published in September 2003. This divided regulatory strategies into:

- *Classic regulation*
- *No intervention*
- *Incentive-based systems*
- *Information and Education*
- *Self-regulation and co-regulation*

The BRTF report made it clear that examples of alternative methods of control abound within UK government. Many departments already consider approaches other than classic regulation and some (e.g. the DTI and Defra) have set up units whose role includes considering regulatory alternatives and advising colleagues on these. The BRTF, however, issued a challenge to Government and regulators: "... to be more inspired and creative in the way they achieve their regulatory objectives." On current practice, the verdict was "... more needs to be done. The culture of Whitehall needs to change to make sure that businesses and others are not unnecessarily burdened with prescriptive regulation where it is not necessary. Regulatory intervention can be necessary, but generally should be used only as a last resort."<sup>95</sup>

### Footnotes

<sup>89</sup> SBS, *Enforcement Concordat: Good Practice Guide for England and Wales* (DTI, London, 1998).

<sup>90</sup> BRTF, *Review: Enforcement* (BRTF, 1999).

<sup>91</sup> *Ibid.*, p.5.

<sup>92</sup> OECD, *Regulatory Policies in OECD Countries* (OECD, Paris, 2002), p.52.

<sup>93</sup> BRTF, *Alternatives to State Regulation* (BRTF, July 2000).

<sup>94</sup> See also the BRTF leaflet *Alternatives to Regulation* (2004).

<sup>95</sup> BRTF, *Imaginative Thinking for Better Regulation* (BRTF, 2003).

As for the RIA process and its requirement that alternative methods be considered, the BRTF conclusion was:

*“the quality of RIAs still leaves much to be desired ..... For RIAs to be a tool of better policy-making there needs to be further commitment by Departments to getting them right. This includes properly considering all the alternatives to classic regulation and consulting on these alternatives.”<sup>96</sup>*

In response to the BRTF report, the Government produced an action plan to promote the use of regulatory alternatives and undertook to flag up the consideration of alternatives within all RIA training events for departmental regulatory impact units and policy officials. Departments were instructed to include a section in their Annual Reports giving figures on their performance in considering alternatives to classic regulation and the BRTF plans to publish a critique of their reports.

Action has also taken place outside the UK in an effort to stimulate the consideration of alternatives. The European Commission’s 2002 *Action Plan on Better Regulation*<sup>97</sup> included a commitment to giving greater consideration to alternatives to legislation as a way of delivering policy. The OECD has also seen consideration of alternatives as an important tool for regulatory improvement. It produced a report on alternative instruments in 1997<sup>98</sup> and returned to the issue in its ‘flagship’ report on regulatory policies in 2002.<sup>99</sup> In 1997 the OECD argued that governments tended to stick to familiar strategies and not to engage in rational analysis of the suitability of different tools. In 2002 the organisation emphasised that cultural changes were needed within regulatory bodies to encourage a comparative approach to alternatives.

Concerning practice on the ground, the OECD summarised:<sup>100</sup> “the use of [regulatory alternatives] is increasing at a substantial pace but the absolute extent of its use – in contexts in which regulation has traditionally predominated – remains low.” The OECD cited one reason why governments were sometimes slow to opt for alternatives to traditional regulation (such as codes of practice) – citizens, consumers, NGOs, pressure groups and others were often concerned that

alternatives were ‘soft’ regulatory options that were not readily enforced and favoured business at the expense of the public or the consumer and so evidenced regulatory capture. Small businesses, moreover, often feared that alternative methods of regulation placed them at a competitive disadvantage because large concerns were better placed to use them to their advantage (e.g. by using self-regulatory systems to limit competition).

## 5.6 Sunset and Review Provisions

A legislative sunset clause states that a given regulatory provision will expire after a stipulated time. A variant is a statement that there will be an automatic review of the regulation after a given period. (The regulation will, accordingly, continue unless action is taken to eliminate it). The advantage of sunset and review procedures is that they force regulators and parliaments to look afresh at the need for a given control, they ensure a rolling review of regulation and encourage the weeding out of regulations that are no longer justified. Such processes are, however, expensive in terms of governmental and parliamentary time and they can create uncertainty in regulatory systems which can both increase investment costs and prejudice consumer confidence in the durability of protections.

The Mandelkern Report<sup>101</sup> argued, nevertheless, that sunset or review clauses can have a particular value in certain circumstances:

- Where regulation is introduced at short notice in response to a crisis and without detailed analysis.
- Where regulation is introduced on a precautionary motive and where further research will provide a firmer basis for decision-making.
- Where a sector, event, technology or market is changing rapidly and the rationale for regulating may fall away.
- Where the legislation is in the nature of a ‘pilot project.’
- Where the regulation confers rights on the state (rather than on citizens).

In the UK, the Cabinet Office’s *Better Policy-Making: A Guide to*

### Footnotes

<sup>96</sup> The BCC’s research has found that less than a quarter of RIAs consider non-regulatory options and that BRTF guidelines or alternatives were “largely ignored” – see T. Ambler, F. Chittenden and M’ Obodovski, *Are Regulators Raising their Game?* (British Chambers of Commerce, London, 2004).

<sup>97</sup> Com (2002) 278 Final, <http://europe.eu.int/eur-lex/en/com/cnc/2002/com20020278en01.pdf>

<sup>98</sup> OECD, *Choices of Policy Instruments* (OECD, Paris, 1997).

<sup>99</sup> OECD, *Regulatory Policies in OECD Countries* (OECD, Paris, 2002) pp.51–7.

<sup>100</sup> *Ibid.*, p.55.

<sup>101</sup> Mandelkern Group, *Report on Better Regulation* (2001) p.18.

*Regulatory Impact Assessment* notes a similar set of considerations that might make such clauses useful – adding: where “measures are taken in the face of considerable opposition.” The Cabinet Office makes the point that review clauses serve an important role in allowing unintended consequences and implementation issues to be considered as part of consultative and reform processes. For small businesses this may offer a valuable opportunity to highlight excessive burdens. It has been the UK Government’s policy since 2000 that RIAs shall include a statement of how a proposed regulation will be monitored and reviewed; and that the appropriateness of time limiting the whole or parts of legislation (including a commitment to review legislation) shall be considered for all new regulations.<sup>102</sup> There are examples of sunset clauses being used in the UK.<sup>103</sup> The price control mechanisms used in the utilities do moreover involve time-limits.

When the Regulatory Reform Act 2001 was under discussion, the House of Lords Committee on Delegated Powers and Deregulation had rejected sunset clauses as too crude and not

appropriate but the Government did offer to report on the operation of the Act after three years.<sup>104</sup> The strategy is, nevertheless, not yet used widely in relation to primary legislation.

## 5.7 Regulatory Policies and Reviews

A widely recognised tool for improving regulation is the adoption, at the centre of government, of a regulatory improvement policy. The UK has adopted such a policy since 1985 and it has taken that policy forward by developing improvement tools (e.g. RIAs), by establishing new institutions (e.g. the BRTF, the SBS, the Panel for Regulatory Accountability) and reviews of regulation have been carried out regularly by not only the above bodies and central departments but by other scrutiny agencies such as the National Audit Office (which has analysed not merely regulatory activities in specific sectors but also the use made of regulatory improvement tools such as RIAs).

### Footnotes

<sup>102</sup> Though see the BCC’s criticism that ‘scant’ attention is given in RIAs to sunset clauses or to monitoring and evaluation – noted section 4.1 above and BCC 2004.

<sup>103</sup> See e.g. section 16 (4) of the Electronic Communications Act 2000; section 5 of the Football (Disorder) Act 2000 (which had to be renewed annually but was amended by the Football (Disorder) Amendment Act 2002 to extend the period to five years); section 15 (3) of the Criminal Justice and Police Act 2001; section 2 of the Education Act 2002.

<sup>104</sup> See Scott and Lodge loc.cit p.208.

# 6 Measuring the Effects of Better Regulation

It can be seen above that since 1985 the UK regulatory system has changed quite dramatically in many respects and, since 1997 there has been much talk of better regulation and much activity under the banner of better regulation. But has the effect on the ground been better regulation from the small business perspective – as judged by the criteria set out in *Table 2* above.

Here it is useful to consider the evidence of achievements under three headings:

- *Regulatory Outcomes*
- *The Regulatory Environment*
- *The Regulatory Processes*

## 6.1 Regulatory Outcomes

In considering outcomes, reference should be made to changes in the regulatory toolkit, and to regulatory burdens.

### The Regulatory Toolkit

It is clear from section 5 that the better regulation movement has produced a number of tools for improving regulation and that these have been designed with a clear eye to ameliorating the position of small businesses. If, however, we focus on the small business concept of good regulation, as summarised in *Table 2* above, it can be asked whether the new toolkit has yet realised its potential to improve regulation. The RIA process, we have seen, has still to shift regulatory culture so that the practice of considering alternatives to classic regulation is embedded within regulatory policymaking. Questions still stand to be asked about the extent to which RIAs prompt action following the consultation of small businesses. Not all RIAs offer a sustained analysis of costs to the different types of small business. The effects of regulatory sanctions and uncertainties on small businesses are not routinely considered in RIAs and much more could be done to obtain rapid feedback on the effects on small businesses of new regulations so that errors (notably excess costs) can be rectified before unsustainable economic damage is suffered.

More can also be done within the RIA process to consider the *cumulative* effects of regulatory and administrative burdens on small businesses. Similarly, the proponents of new regulations could do more within the RIA process to indicate how, by a variety of means, assistance could be given to small businesses through better information about compliance with proposed regulations. A series of ‘options for amelioration’ should be set out within RIAs to indicate choices for making regulations less threatening to small enterprises.

Ministers should also agree, when signing-off RIAs that Regulatory Impact Post-Implementation Assessments (RIPIAs) should be conducted at a stipulated time twelve to eighteen months after a regulation comes into effect. The Government has stated that it is committed to systematic post-implementation reviews of “major pieces of legislation” (RIA guidance 2003, para 3.30), but bespoke reviews should be carried out (either by the body regulating or by a separate authority such as BRTF) soon after each significant regulation is implemented. Such a process would serve a number of purposes:

- *It would allow small businesses, consumers or others to point to unanticipated effects or costs as well as to policy failures.*
- *It would allow affected parties to point out departures from RIA forecasts or assumptions.*
- *It would provide an opportunity for swift reform where mistakes have been made (e.g. in RIAs) and accordingly would reduce dangers to small businesses and others from misplaced regulatory judgements and decisions.*
- *It would supply feedback of value in improving the quality of RIAs.*

There are other, but more general difficulties with RIAs – notably tendencies not to state the objectives of proposals clearly and uncertainties concerning data.<sup>105</sup> These affect a wide range of parties and bodies but even these general problems may hit small businesses particularly hard because

#### Footnote

<sup>105</sup> See the discussion of RIAs and secondary legislation in section 6.3 below.

any errors in regulatory decisions are likely to produce excess costs or competitive imbalances and small businesses are exceptionally vulnerable on these fronts. There may be room, moreover, to improve the small business friendliness of other tools. Consultation procedures, as noted, involve dangers of 'fatigue' in small firms and the developing role of the SBS is important here. There may, moreover, be a case for the Government to develop taxation and other concessions to encourage small business participation in regulatory decision and policymaking.

Regulatory simplification tools have been developed in the UK and their proponents have set out to attack both administrative and regulatory burdens. Legislative steps have been headed by the Deregulation and Contracting Out Act 1994 and the Regulatory Reform Act 2001. It is early yet to see the full effects of the 2002 Action Plan on Regulatory Reform but there are indications of disburdening that offer some hope for small business. What such businesses may, however, look for is, first, greater attention to reducing cumulative burdens, second, a reversal of the trend to place administrative (and notably tax or credit) functions outside government and in the hands of business, and, third, fewer regulatory requirements. The last issue is returned to below in looking at the quantum of regulatory burdens.

There is evidence of other improvement tools having been developed since 1997, notably the Enforcement Concordat; the consideration of alternative strategies, sunset provisions and scrutiny processes and institutions. From a small business perspective, however, there is work yet to be done: to extend practical application and monitoring of the Enforcement Concordat; to change regulatory cultures so that alternatives are routinely considered; to use sunset provisions more widely where circumstances are appropriate; and to apply regulatory scrutiny processes in a manner that routinely moves beyond considering particular regulatory proposals and looks to cumulative effects.

## Regulatory Burdens

There is evidence from a number of sources that regulatory burdens on business have grown, rather than decreased in

recent years and that businesses have perceived there to have been such an increase.<sup>106</sup>

In April 2004 the BCC launched their updated Burdens Barometer on red tape, which calculated that legislation introduced since 1998 was costing companies an additional £30 billion.<sup>107</sup> A year earlier, in 2003, an HBOS survey found that two thirds of small businesses believed that the burden of red tape had increased in the preceding twelve months.<sup>108</sup> This figure had doubled from the preceding year when a Small Business Research Trust survey found that a third of respondents perceived legislation and government regulation to have increased. Four out of five small businesses, moreover, seemed to consider the absolute level of burdens to be excessive. The Small Business Research Trust Survey of 2003 found that around 80 percent of small businesses believed that there was too much regulation and paperwork related to employees. When the FSB surveyed 18,635 small businesses in 2004, three out of five of them said that they were dissatisfied with the volume and the complexity of legislation.<sup>109</sup>

It was clear in the years preceding the 1997 move to "better" regulation that small businesses were increasingly unhappy with regulatory burdens. The Institute of Chartered Accountants reported in 1997 that over the preceding two to three years its members had felt that burdens had worsened and that more than a third of members noted a deterioration in the timing and scheduling of compliance deadlines, the prescriptiveness of regulations and enforcement procedures and the balance between the needs of regulation and the encouragement of enterprise.

Matters, however, seemed not to improve after the 'better' regulation initiative had started. By 2000 the ICAEW was reporting<sup>110</sup> that generally advisers to small businesses considered that regulation was increasingly burdensome. Two fifths of respondents said that the balance between the needs of regulation and the encouragement of enterprise had worsened and only eight per cent thought that it had improved. This general negativity was repeated in 2002 when 43% of respondents pointed to no improvement and 9% thought that the balance had worsened.<sup>111</sup> A year later, the

## Footnotes

<sup>106</sup> On the problems of measuring burdens and of separating out different 'compliance costs' from 'administrative' and 'regulatory' burdens see Chittenden, Kauser and Poutziou, *op.cit.*

<sup>107</sup> See BCC 2004.

<sup>108</sup> See SBS, *A Government Action Plan for Small Business: The Evidence Base* (2003) para 18.

<sup>109</sup> FSB, *Lifting the Barriers to Growth in UK Small Businesses* (FSB, 2004) p.85.

<sup>110</sup> ICAEW, *Smaller Businesses and Regulation: Research Report* (ICAEW, London, 2000).

<sup>111</sup> ICAEW, *Developing the Enterprise Economy* (ICAEW, London, 2000) p.19 (44% did, however, point a marginal improvement.)

outlook was even more bleak, particularly in some regions where six in ten respondents felt that the balance had worsened.<sup>112</sup>

A further set of surveys, by the Small Business Research Trust (SBRT) shows the change over the decade from 1990 to 2000. In 1990 only 3.1 per cent of respondents rated governmental regulation and paperwork as the most important problem facing their business. This rose to 18.9 per cent in the second quarter of 2000. By 2003 the figure was averaging at 15 per cent. These figures indicate that, whatever actions the Government has taken, it has some way to go to convince business owners that their burdens have eased as a result of the better regulation movement. Calls for action continue. The British Chambers of Commerce (BCC) argues that there is a range of measures that the Government could introduce to reduce red tape and burdens on business – and particularly on smaller firms, notably it could:

- Use regulation as a last resort – use information, education, awards, and other incentives before regulation.
- Introduce a system of shadow regulatory budgets for government departments.
- Provide greater transparency on the cumulative burden of regulation on businesses, publishing RIAs in electronic format in one place.
- Use sunseting as a norm and make the criteria for sunseting more explicit.
- Pledge not to increase the existing cumulative burden of regulation on businesses.

## 6.2 The Regulatory Environment

When considered comparatively, there are indications that in the UK regulatory burdens are light. The UK ranked to have the lowest barriers in the OECD's 2002 survey of barriers to

entrepreneurship – a survey that took into account such factors as administrative burdens on start up and the degree to which administrative systems are difficult to understand.<sup>113</sup> A further study of the same year looked at legislation, taxation and regulation affecting established businesses in the USA and nine EU countries. This concluded for the second consecutive year that the UK provided the most entrepreneurially friendly environment.<sup>114</sup>

Business perceptions of regulation may, however, differ from the above indications and, as already stated, perceptions about regulatory quality and burdens can matter as much as factual positions on the ground. Perceptions impact on business confidence, the ambition of entrepreneurs, the propensity to start new businesses, and small business aspirations of growth.<sup>115</sup>

A number of surveys have consistently found significant proportions of small businesses citing regulation as their greatest concern or obstacle to success.<sup>116</sup> The SBS Omnibus Survey of 2002<sup>117</sup> found that around one in five small businesses cite regulation as the greatest obstacle they face – more than any other factor. A similar finding resulted from the SBRT's 2001 small business survey.<sup>118</sup> About a third of respondents, moreover, said that regulation and red tape had acted as a barrier to growth and a similar percentage said that, due to red tape, they had seriously considered not continuing with their business.<sup>119</sup> The ICAEW's small business survey of 2000<sup>120</sup> found that 46% of respondents thought that regulatory compliance was a serious barrier to growth and business success. A further 42% considered it 'something of a barrier.' In accord with these figures was a more recent survey by SAP, the software company, which found in 2004 that four in ten companies considered that red tape was stifling their growth.<sup>121</sup> There is evidence, moreover, that even the heads of large enterprises now see regulation as a more serious problem than lack of demand or interest rates.<sup>122</sup>

### Footnotes

<sup>112</sup> ICAEW, *Enterprise Survey 2003* (ICAEW, London, 2003) p.4.

<sup>113</sup> OECD, *Competition, Innovation and Productivity Growth: A Review of Theory and Evidence* (OECD Economics Department Working Paper 317, Paris, 2002).

<sup>114</sup> Anderson/Growth Plus, *Not Just Peanuts* (2002) ([www.notjustpeanuts.com/introduction.htm](http://www.notjustpeanuts.com/introduction.htm)).

<sup>115</sup> Lack of information on regulations can lead small businesses to over estimate costs of compliance – see DTI, *Cross-Cutting Review of Government Services for Small Businesses* (DTI, London, 2002).

<sup>116</sup> See the review in SBS, *A Government Action Plan for Small Business: The Evidence Base* (DTI, London, 2004).

<sup>117</sup> SBS, *Omnibus Survey of Small Business Opinions* (unpublished, 2002).

<sup>118</sup> SBRT, *Government and Regulations* (SBRT, Milton Keynes, 2001).

<sup>119</sup> In 1996 the ICAEW's survey revealed that for small businesses (11–100 employees) 58% of respondents cited legislation in a barrier to growth – more than any other barrier (next was local regulation at 53%) – ICAEW, *Barriers to Growth* (ICAEW, London, 1996).

<sup>120</sup> ICAEW, *Smaller Business and Regulation: Research Report* (ICAEW, London, 2000) p.5.

<sup>121</sup> See Financial Times, Growth, Say Companies' 'Red Tape is Damaging', 8 April 2004.

<sup>122</sup> See MORI, *Captains of Industry Survey*, London (2004). During the Thatcher governments lack of demand was the top concern, this changed to interest rates in the Major years and the focus of worry has now become government regulation – see R. Worcester, 'Whatever Happened to Blair's Better Regulation?' (2004) 43 Profile 11.

International studies showing that the UK is lightly regulated in general, do, moreover, contrast with surveys that focus on new business start-ups (measured by the number of procedures required to register a new business). The Global Entrepreneurship Monitor survey of 2004 ranked the UK as around average on such burdens<sup>123</sup> and the SBS has found that around a third of those adults that think about starting up a business view the complexity of regulation as a barrier to entrepreneurial activity.<sup>124</sup>

A degree of caution has to be used in drawing conclusions from statistics such as those cited. Small businesses differ in kind and may experience a wide variety of problems. Survey respondents, moreover, may conflate regulatory burdens with administrative and particularly taxation burdens – it is noteworthy that the SBRT survey of 2003 found that V.A.T. and employee taxation were the two areas of ‘government regulation and paperwork’ that took small businesses the most amount of time. That said, however, it has to be repeated that perceptual problems may be self-fulfilling.<sup>125</sup>

### 6.3 The Regulatory Process

Small business concerns about regulatory burdens can to a degree be assuaged if those businesses are content that regulatory processes are appropriate – if, for instance, they consider that they are given good advice and assistance with compliance. When UK small businesses were asked by the FSB about possible measures that would encourage compliance the most popular, apart from ‘evidence of cost savings’ was ‘the provision of clear information about government requirements.’<sup>126</sup> Small businesses may also be reassured if they are confident that their voice is heard in regulatory policymaking.

This has been a point taken by the SBS which, in 2004 started

to employ a new indicator of small business experience of government improvements, namely: “Increased small business perceptions that their concerns are being taken into account by government.”<sup>127</sup> SBS analyses on this front are awaited but the ICAEW has for some time deployed process satisfaction measures.

ICAEW figures are available on certain aspects of regulatory process satisfaction in the period 1996 to 2001. On a number of issue ratings respondents generally indicated strong and consistent perceptions of deterioration – notably in:

- *The care with which new regulations are considered before introduction.*
- *The timing and scheduling of compliance deadlines*
- *The regulator’s understanding of both the nature of small businesses and the resources available to them.*<sup>128</sup>

On one matter, however, the six surveys all showed perceptions of improvement. This was the “level of advice and support offered by Government and other agencies.” Such an improvement may reflect the development of consultative tools as described in section 4.2. It is, however, just one aspect of process satisfaction. As for the impact of the small business voice on legislative proposals, some indication of how this operates post ‘better regulation’ can be gained by examining some concrete examples, notably those processes leading to the Employment Act 2002 and the Local Government Act 2003.

A look at the passage of the Employment Act 2002 is instructive in showing why the merits of the small business case and the small business voice can be undervalued even in the era of “better” regulation. When the Bill preceding the Act was introduced, small business concerns centred on a number of changes in the law, notably:

#### Footnotes

<sup>123</sup> P. Reynolds et.al, *Global Entrepreneurship Monitor (GEM)* (London Business School, London 2004 and Kauffman Foundation, Kansas City USA, 2004). The UK was found by the GEM to be (like the USA) in the “intermediate” group of entrepreneurial countries (It was not in the “most” or “next most” entrepreneurial countries). On firm entrepreneurship the UK rated 16th out of 40 countries listed and on total entrepreneurial activity it was 18th out of 31 countries.

<sup>124</sup> SBS, *Omnibus Survey of Small Business Opinions (2002)* unpublished.

<sup>125</sup> In *Lifting the Barriers to Growth in UK Small Businesses* (FSB, London, 2002) employment was the legislative area most negatively assessed for its effect on small business (36% rated it ‘very negative’ or ‘negative’ in effect).

<sup>126</sup> It is noteworthy that the third least important potential driver of compliance was ‘threats of fines or legal proceedings’ and the least important was ‘voluntary code of conduct’ – see FSB, *Lifting the Barriers to Growth in UK Small Businesses* (FSB, London, 2004) p.90. The importance of information on regulation was stressed by the Institute of Directors and other leading business organisations in IoD, *Your Business Matters* (1996): “What small businesses would really like to see is half a dozen bullet points on any regulation and a good set of guidance notes to support them”; (p.9).

<sup>127</sup> See SBS, *A Government Action Plan for Small Business: The Evidence Base* (DTI, London, 2004) p.66.

<sup>128</sup> Small Business perceptions on regulatory process quality may be affected by their views on the quantity of regulations emerging. The Federation of Small Businesses Membership Survey of 2004 revealed that around 60% of small businesses are dissatisfied with the volume and complexity of legislation and that a third are “very dissatisfied” with the rate of change of legislation. See FSB, *Lifting the Barriers to Growth in UK Small Businesses* (FSB, London, 2004) p.85.

- *New flexible working rules meant that all employers would have to formally consider all requests for flexible working.*
- *New statutory grievance procedures.*
- *Increases in awards for failure to follow statutory procedures.*

The FSB campaign on the Bill expressed concern about new administrative burdens for small employers (particularly relating to flexible working), it raised worries about the Government's late decision to drop plans to charge applicants for bringing a case to an Employment Tribunal, and it argued for an exemption for undertakings with less than five employees. This campaign, however, achieved little success for a number of reasons.

1. Government supporters and Ministers tended to be committed to certain regulatory measures for ideological reasons or because of manifesto commitments – this reduced the impact of small business objections or RIA-based concerns about costs.<sup>129</sup>
2. The costs and benefits of regulation tended to be difficult to quantify<sup>130</sup> and this reduced the impact within the policy process of any RIA balancing of costs and benefits or analysis of small business effects.
3. Government supporters and ministers tended to revert to 'pre-better regulation' attitudes in which objections to small business burdens were seen as attacks on the Bill's objectives (indeed, as calls for deregulation) rather than as more balanced efforts to produce better regulation. This response was seen in Trade Secretary, Pat Hewitt's taunt to opponents on the Second Reading of the Bill: "If they are shown fair standards for working people, all they can do is complain about burdens on business."<sup>131</sup> This comment was, moreover, made alongside statements from Ms Hewitt that.... "we started with the needs of small businesses and the people working in them uppermost in our minds" and ...."our priority ... has been to adopt a light touch approach."
4. It was difficult for parliamentarians to assess the various burdens being placed on business because regulation relied heavily on secondary legislation that was not available for discussion – the Act authorised the imposition on small businesses of an unknown body of

new regulatory obligations. As one MP said:.... "the cost to business of the regulations in the Bill is extremely difficult to judge. As it is often the case with legislation introduced by this Government, the Bill contains enabling legislation that will result in many of the new regulations being introduced by statutory instruments at a later date."<sup>132</sup> Objectors were concerned that ministers could make numerous speeches on cutting red tape but, within minutes, authorise rafts of new regulations.

5. Numerous regulatory powers were introduced late in the parliamentary process and this ruled out sustained analysis of their effects on small businesses.
6. The designers of regulation tended to design controls after consulting large employers and assuming the flexibilities, resourcing, and administrative capacities of such employers. People from big companies tended to have limited small business experience and tended to underestimate the shock effects of new regulations on small businesses.
7. Critics considered that governments often offered businesses procedural assurances rather than substantive help. As one MP put it bluntly:

*"It appears that the Government want to counter some of the ill-will generated by over-complex regulation by making somewhat ham-fisted pro-business initiatives. The most recent was the announcement that senior business people would be seconded to operational jobs in the Department of Trade and Industry."<sup>133</sup>*

8. Governments have incentives to generate new initiatives in a constant flow of regulation. Small businesses, on the other hand, tend to want periods of regulatory stability and certainty in which to develop. This produces a deep-seated conflict of attitudes and interests.

Small businesses are concerned about both regulations that affect their competitiveness and how regulation affects their competitors' market behaviour. The Employment Act 2002 concerned the former, the Local Government Act 2003 affected the latter.<sup>134</sup> For small businesses debating the merits of the Local Government Bill in 2002–3 it was Part 8 that was a particular worry.

#### Footnotes

<sup>129</sup> The RIA did contain express cautions regarding small firms. It acknowledged (para 49) that the new grievance procedures were "likely to disproportionately affect small firms" and that (para 50) the costs of covering for staff absences were more acute in small firms.

<sup>130</sup> The RIA acknowledged that "a great many assumptions" had to be made to prepare the RIA; that much depended on future behaviour that was difficult to test as the basis of historical data; and "many benefits cannot be quantified" (RIA p.12).

<sup>131</sup> (27 November 2001, Col. 866). See also the comment of government supporter Rob Morris MP: "We are talking about quality of life. Simply focussing on financial costs is to be like an old – fashioned Stalinist and say 'It's all about material gain: the quality of human life does not come into the question.'" (27 November 2001, Col. 904).

<sup>132</sup> John Whittingdale MP, 27 November 2001, Col. 875.

<sup>133</sup> Dr Vincent Cable, 27 November 2001, Col. 886.

<sup>134</sup> For the position in Scotland see the Local Government in Scotland Act 2003.

The proposals at issue were formulated to allow local authorities to charge for discretionary services and to give the Secretary of State powers to allow Best Value authorities to trade in relation to any of their ordinary functions. Small business worries were that local authorities would compete unfairly with private firms because they possessed a number of unacceptable advantages – notably: they could charge on a cost recovery basis without a need to make a profit; they could trade on the basis of cross-subsidies; and they might form dominant partnerships that would drive small firms out of business. The FSB, representing over 185,000 small businesses, campaigned for local authorities to have to submit trading proposals to a Business Impact Assessment procedure or adopt the Office of Fair Trading competition assessment process. Such an assessment, said the FSB, should have to be published to ensure transparency and there would have to be complete openness in local authority accounting regarding all financial flows relevant to charging and trading. Further protections against unfair competition, and conflicts of interest, said the FSB, should be ensured in regulations and guidance.

As with the Employment Act, there were a number of reasons why the impact of the small business voice in the regulation-making process was less than it might have been.

1. Experience with the Employment Bill, was repeated in so far as much regulation (including potential small business protections) depended on the use of enabling powers by ministers and this future activity could not be considered when the Bill was debated.
2. Predicting small business impacts was rendered difficult because this depended on attempts to quantify the potential use of the new powers by local authorities. A sample survey was conducted (in October 2002). The response rate was extremely low and, the RIA admitted: “the results are therefore of limited use.”
3. The Office of the Deputy Prime Minister (ODPM) and the RIA process did not assess small business implications in detail. The ODPM looked at potential charging in domiciliary care and concluded that small firms would face competition from local authorities – but it did not quantify this with any precision. The ODPM analysed three trading areas for competition effects (industrial catering, industrial cleaning and leisure provision). In the first two, detrimental impact on small businesses was highlighted but not addressed in detail. In relation to leisure provision, the market was already dominated by the local authority. The RIA looked at possible competitive effects in just two other areas (Arboriculture and Pest Control) and made broad brush estimates. The RIA analysis of small business impacts (excluding case studies) occupied only six and a half lines of text.

4. Politically, Part 8 of the Bill was difficult to shift because of cross party support and because there were strong concerns to allow local authorities to maximise their potential to earn revenue charging and trading activities.

Experience with both of the above pieces of legislation points to the difficulty of applying RIAs to framework laws where the substance of a regulatory proposal turns on the way that delegated powers will be used at a future date by ministers or agencies. If this is the case, it will often be impossible to evaluate a proposal by using primary legislation as the focus of the RIA. It is the case that when secondary legislation follows a ‘framework’ Act, the secondary legislation itself should be liable to RIA if it impacts on businesses, charities or voluntary bodies. There are dangers here, however, since some secondary legislation may escape the RIA net and some proponents of regulation may consider that if a framework Act has passed an RIA this satisfies the need to impact assess each item of secondary legislation used. In such cases the RIA process may fail to catch some regulations. In order to clarify this position and to ensure complete coverage of the RIA process it should be made plain that when a RIA is used to evaluate enabling legislation and the costs or benefits of regulating will be materially governed by secondary legislation, ministers, on signing-off the RIA, should always undertake to carry out secondary RIAs to cover all relevant delegated legislation. Ministers should, moreover, identify areas where it is anticipated that secondary legislation will have an impact on business, charities or voluntary bodies and will require subjection to the RIA process. Cabinet Office guidance should demand this. If such a practice is not adopted, many RIAs may miss the full substance of regulatory proposals. They will accordingly fail to give a voice to small businesses and others who are concerned about the effects of such proposals.

To summarise on small businesses and regulatory processes, the message from the above review is that even in the post ‘better regulation’ era there are grounds for concern about small business perceptions of regulatory processes and government’s propensity and capacity to listen to the small business voice. Small businesses, worryingly, think that in a number of key respects, the regulatory process is deteriorating and small business fears about legislative and rulemaking processes are not lessened by analyses (as above) that reveal structural reasons why the small business voice tends to be lost.

# 7 Conclusion

Small enterprises are disproportionately affected by regulatory requirements, red tape and burdens. Regulation can make them vulnerable, it can affect their competitiveness and reduce their ability to grow. Small businesses, accordingly, are highly sensitive to regulation and to changes in regulation. They, moreover, have a particular perspective on what constitutes good or better regulation. They look for regulation that is *inter alia*: proportionate, given the special costs regulation imposes on small businesses; accountable to small business influence as much as to big business; fair to small businesses as competitors; consistent with growth; not cumulatively excessive; and applied with appropriate assistance and advice. They also want openness within small business constraints and well-targeted regulation so that side effects do not discourage small scale entrepreneurship or small business growth.

It cannot be denied that, alongside European and OECD initiatives, the UK government has, since 1997, developed a series of strategies for moving towards 'better' regulation and that it has done so with energy. It has, we have seen, developed systematic policies on regulatory improvement as well as an extensive toolkit for pursuing better regulation – as exemplified by its efforts to improve the RIA process. It has, moreover, developed a series of institutions, such as the BRTF and SBS that are centrally concerned to look to small business interests.

There is still some way to go before the 'better regulation' movement can be said to have delivered the goods for small business. The RIA process is of central importance to the movement but more needs to be done to change cultures so that alternatives to familiar regulatory methods are fully embraced and considered; too many RIAs fail to deal with small business costs and benefits in a convincing manner, or in a way that deals with cumulative effects as well as options for ameliorating small business impacts. The extent to which RIAs make assumptions bordering on the heroic means both that small business concerns are pursued in a muted form within policy processes and that such businesses are highly exposed to the effects of regulatory miscalculations. Other tools, such as consultations, need to be developed further (e.g. by small business assistance schemes) if the small business voice is to be heard properly. For such reasons, current

regulation will not readily be seen as proportionate, accountable, consistent, transparent and targeted in the small business sense.

On regulatory burdens, the Government, again, has developed strategies energetically in the last seven years. Small business perceptions, however, are that burdens and red tape have increased during this period – and, even if they were misguided, such perceptions would negatively affect business confidence and entrepreneurial activity. As for the regulatory environment, the good news is that the UK has been ranked as a leader in avoiding barriers to entrepreneurship. The less good news is that such rankings have taken on board factors beyond regulatory burdens and that such burdens are perceived by too many small businesses to be a (or the) major impediment to growth and success. Nor can it be said that perceptions regarding burdens and barriers to growth are generally compensated for with high levels of small business satisfaction on regulatory processes. When, moreover, a closer look is taken at legislative and regulation-making processes, further worries emerge. There are some significant reasons why the small business voice can be poorly heard and heeded in those processes in spite of governmental protestations. Weakness in RIAs can allow small business concerns to give way too early to regulatory commitments. Complaints about burdens can be dismissed in a 'pre-better-regulation' manner as more calls for deregulation. The use of enabling provisions and secondary legislation can undermine real debating on regulatory costs and benefits as can the difficulties of predicting the future behaviour of ministers, employers and employees. The voice of big businesses remains powerful, often drowning out small business concerns.

To draw matters to a close, it can be said that if the better regulation movement is judged by small business benchmarks there is much more work to be done.

One step that can be taken is to harden the requirement that RIAs should consider ways to reduce adverse impacts on small businesses. The Cabinet Office's current guide to RIAs talks of using small business focus groups to consider less burdensome ways to deliver the chosen policy. The guidance should expressly demand that all RIAs set out and discuss an array of options for reducing small business impacts. Such

guidance moreover, should be applied more robustly than at present and, to this end, ministers, when signing a RIA, should certify that it meets those guidelines (as advocated in BCC 2004).

A further measure that should be taken is, as indicated above, the institution of a system of Regulatory Impact Post-Implementation Assessments (RIPIAs) so that regulatory effects, and particularly unanticipated effects, can be picked up and remedied as soon after as implementation as possible. It should similarly be provided, in the Cabinet Office Guide to RIAs, that secondary RIAs should be undertaken whenever the substance of a regulatory initiative will be provided by the exercise of secondary powers by ministers or agencies. The Guide should demand that when ministers sign-off framework primary legislation, they should identify anticipated areas where secondary legislation will require application of the RIA process.

There are dangers, however, in assuming that all that is necessary is for the Government to try harder – to make greater effort with its established strategies for better regulation. New questions may have to be asked with a new urgency about the best way to make regulation ‘better’ for small businesses. This may involve asking, for instance, whether RIA processes, as currently operated, really are the best way to feed small business concerns into regulatory processes. There are limits to the intensity within which RIAs can be conducted and used. There are also limits to the confidence with which we can build RIAs on extensive sets of assumptions. This should prompt us to resist placing ever more faith on RIAs as protections for small businesses and to ask whether more emphasis should be placed on other strategies such as focussing more directly on mixes and cumulations of regulations and on more actively helping small business to play a greater role in regulatory policy-making.

# 8 Key References

- Allio, L., Ballentine, B., and Hudig, D.**, *Achieving a New Regulatory Culture in the European Union* (European Policy Centre, Working Paper No. 10, April 2004).
- Ambler, T., Chittenden, F., and Shamutkova, M.**, *Do Regulators Play by the Rules?* (British Chambers of Commerce, London, 2003).
- Ambler, T., Chittenden, F., and Obodovski, M.**, *Are Regulators Raising their Game?* (British Chambers of Commerce, London, 2004).
- Anderson/Growth Plus**, *Not Just Peanuts* (2002) ([www.notjustpeanuts.com/introduction.htm](http://www.notjustpeanuts.com/introduction.htm)).
- Australian Government**, *Department of Industry, Tourism and Resources: Regulatory Performance Indicators* (Canberra, 1999).
- Baldwin, R., and Cave, M.**, *Understanding Regulation* (Oxford 1999).
- Beale, H., and Kin, H.**, *Impacts of Federal Regulations* (Report for the US SBA, Microeconomic Applications Inc Washington DC, 1988).
- BRTF**, *Regulation and Small Firms Progress Report* (Cabinet Office, 1999).
- BRTF**, *Review: Enforcement* (Cabinet Office, 1999).
- BRTF**, *Alternatives to State Regulation* (Cabinet Office, 2000).
- BRTF**, *Helping Small Firms Cope with Regulation: Exemptions and Other Approaches* (Cabinet Office, 2000).
- BRTF**, *Payroll Regulation* (Cabinet Office, 2000).
- BRTF**, *The Better Regulation Guide and Regulatory Impact Assessment* (Cabinet Office, 2000).
- BRTF**, *Employment Regulation: Striking a Balance* (Cabinet Office, 2002).
- BRTF**, *Imaginative Thinking for Better Regulation* (Cabinet Office, 2003).
- BRTF**, *Principles of Good Regulation* (Cabinet Office, 2003).
- BRTF**, *Alternatives to Regulation* (Cabinet Office, 2004).
- Business Link**, *The No Nonsense Guide to Government Rules and Regulations for Setting up your own Business* (DTI, London, 2003).
- Cabinet Office**, *Modernising Government Cm 4310* (1999).
- Cabinet Office**, *Regulatory Reform: The Government's Action Plan* (Cabinet Office, London, 2002).
- Cabinet Office**, *Better Policy Making: A Guide to Regulatory Impact Assessment* (Cabinet Office, London, 2003) ([www.cabinet-office.gov.uk/regulation](http://www.cabinet-office.gov.uk/regulation)).
- Cabinet Office**, *Transposition Guide: How to Implement European Directives Effectively* (Cabinet Office, London, 2003).
- Carter, S., et.al** *Lifting the Barriers to Growth in UK Small Businesses*, FSB, (2002).
- Chittenden, F., Kauser, S., and Poutziou, P.**, *Regulatory Burdens on Small Business* (Manchester Business School, 2001).
- Collard, D., et.al**, *The Tax Compliance Costs for Employers of PAYE and National Insurance in 1995–96* (Inland Revenue Economics Papers: No.3, 1998).
- Department of the Taoiseach**, *Regulating Better* (Dublin, 2004).
- DTI**, *Lifting the Burden* (Cmnd of 9571, 1985).
- DTI**, *Building Businesses Not Barriers* (Cmnd 9794, 1986).
- DTI**, *Releasing Enterprise* (Cm 512, 1988).
- DTI**, *A Review of the Implementation and Enforcement of EC Law in the UK* (DTI, London, 1993).
- DTI**, *Deregulation: Cutting Red Tape* (DTI, London, 1994).

- DTI**, *Thinking About Regulation: A Guide to Good Regulation* (DTI, London, 1994).
- DTI**, *Getting a Good Deal in Europe* (DTI, London, 1994).
- DTI**, *Cross-Cutting Review of Government Services for Small Businesses* (DTI, London 2002).
- ENSR**, 'Administrative Burdens' in the European Observatory for SMEs, Third Annual Report, 1995.
- European Commission**, *Communication on Impact Assessment* 5 June 2002.
- European Commission**, *Action Plan for Simplifying and Improving the Regulatory Environment COM (2002) 278 Final*.
- European Commission**, *Better Law Making COM (2002) 275*.
- European Commission**, *Communication: Simplifying and Improving the Regulatory Environment COM (2001) 726 Final*.
- European Commission**, *Minimum Standards of Consultation COM (2002) 277 Final*.
- European Commission**, *The Operating Framework for the European Regulatory Agencies COM (2002) 718 Final*.
- European Commission**, *Updating and Simplifying the Community Acquis COM (2003) 371 Final*.
- European Commission**, *White Paper, European Governance COM (2001) 428 Final*.
- FSB**, *Lifting the Barriers to Growth in UK Small Businesses* (FSB, London, 2004).
- House of Commons**, First Special Report, *The Operation of the Regulatory Reform Act 2001: A Progress Report* (HC 908, Session 2002–2003).
- ICAEW**, *Barriers to Growth* (ICAEW, London, 1996).
- ICAEW**, *Developing the Enterprise Economy* (ICAEW, London, 2000).
- ICAEW**, *Small Businesses and Regulation* (ICAEW, London, 2000).
- ICAEW**, *Smaller Businesses and Regulation: Research Report* (ICAEW, London, 2000).
- ICAEW**, *Enterprise Survey* (ICAEW, London, 2003).
- Institute of Directors**, *Your Business Matters* (IoD, London, 1996).
- Irish Presidency**, *Joint Initiative on Regulatory Reform* (Dublin, 2004).
- Mandelkern Group** Report on Better Regulation, Final Report, 13 November 2002.
- MORI**, *Captains of Industry Survey*, (London, 2004).
- National Audit Office**, *Better Regulation* (HC 324, Session 2001–2).
- National Audit Office**, *Evaluation of Regulatory Impact Assessments Compendium Report 2003–4* (HC358, Session 2003–4).
- NNR**, *The NNR Regulation Indicator for 2002* (Board of Swedish Industry and Commerce for Better Regulation, June 2002).
- OECD**, *Recommendation on Improving the Quality of Government Regulation* (OECD, Paris, 1995).
- OECD**, *Policy Recommendations on Regulatory Reform* (OECD, Paris, 1995).
- OECD**, *Choices of Policy Instruments* (OECD, Paris, 1997).
- OECD**, *Report on Regulatory Reform* (OECD, Paris, 1997).
- OECD**, *Small Business, Job Creation and Growth, Facts, Obstacles and Best Practices* (OECD, Paris, 1997).
- OECD**, *Business Views on Red Tape* (OECD, Paris: 2001).
- OECD**, *Competition, Innovation and Productivity Growth: A Review of Theory and Evidence* (OECD Economics Department Working Paper 317, Paris 2002).
- OECD**, *Recommendation of the Council of the OECD in Improving the Quality of Government Regulation* OECD/GD (95) OECD, Paris 2002.
- OECD**, *Regulatory Policies in OECD Countries* (OECD, Paris, 2002).
- OECD**, *United Kingdom: Challenges at the Cutting Edge* (OECD, Paris, 2002).
- OECD**, *From Red Tape to Smart Tape* (OECD, Paris, 2003).

**RAMBOLL Management and ITPS (Sweden),** *Efforts to Reduce Administrative Burdens and Improve Business Regulation* (Denmark: Ministry of Business and Economic Affairs, August 2003).

**Reynolds, P., Bygrave, W., Autio, E., et al,** *Global Entrepreneurship Monitor* (London Business School, London, 2004 and Kaufman Foundation, Kansas City, USA, 2004).

**Small Business Research Trust,** *Government and Regulations* (SBRT, Milton Keynes, 2001).

**SBS,** *A Government Action Plan for Small Business: The Evidence Base* (DTI, London, 2004).

**SBS,** *Enforcement Concordat: Good Practice Guide for England and Wales* (DTI, London, 1998).

**Scott, C., and Lodge, M.,** 'Administrative Simplification in the United Kingdom' in *OECD, From Red Tape to Smart Tape* (OECD, Paris, 2003).

**University of Bradford,** Centre for European Studies, *Interim Report on Indicators of Regulatory Quality* (CEC, DG Enterprise, 9 May 04) (website: [www.bradford.ac.uk/irq](http://www.bradford.ac.uk/irq)).



## **Better Regulation**

### **Is it Better for Business?**

Written for the Federation of Small Businesses

by

**Professor Robert Baldwin**

*Professor of Law, The London School of Economics*

©Federation of Small Businesses

Copies of this publication may be obtained by writing to:

Federation of Small Businesses  
2 Catherine Place, London SW1E 6HF  
Telephone: 020 7592 8100  
Facsimile: 020 7233 7899  
email: [london.policy@fsb.org.uk](mailto:london.policy@fsb.org.uk)  
website: [www.fsb.org.uk](http://www.fsb.org.uk)

Designed on behalf of the Federation of Small Businesses by  
Hutton Design, Long Road, Paignton, TQ4 7BB  
Telephone: 01803 668718  
Fax: 01803 557148  
email: [luke.hutton@virgin.net](mailto:luke.hutton@virgin.net)

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without prior permission of the Federation of Small Businesses (FSB). While every effort has been made to ensure the accuracy of the facts and data contained in this publication, no responsibility can be accepted by FSB for errors or omissions or their consequences. Articles that appear in the book are written in general terms only. They are not intended to be a comprehensive statement of the issues raised and should not be relied upon for any specific purposes. Readers should seek appropriate professional advice regarding the application to their specific circumstances of the issues raised in any article.

Published by the Federation of Small Businesses (FSB)  
Copyright © 2004 FSB Further copies of this report and  
information on the regional results can be downloaded from FSB  
website at <http://www.fsb.org.uk/policy/archivePubs/>

September 2004



©Federation of Small Businesses  
2 Catherine Place  
London  
SW1E 6HF  
Telephone: 020 7592 8100  
Facsimile: 020 7233 7899  
email: [london.policy@fsb.org.uk](mailto:london.policy@fsb.org.uk)  
website: [www.fsb.org.uk](http://www.fsb.org.uk)

ISBN: 0-906779-39-1