



Evaluation of Regulatory Impact Assessments Compendium Report 2004-05

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EXECUTIVE SUMMARY



1 Regulation is an important instrument available to governments for fulfilling their objectives. Regulation can however impose costs on businesses, the voluntary sector and individuals, and may not always be the most effective way of achieving a Government's objectives.

2 Since 1998, the Government has used a process known as Regulatory Impact Assessment (RIA) to identify the objectives, and review the likely costs, benefits and uncertainties, of regulations. RIAs should inform decisions on alternative options to achieve those objectives, and should also communicate clearly why the preferred option has been selected.

3 In April 2002, the Committee of Public Accounts recommended that the NAO evaluate a sample of the RIAs produced each year and in December 2002 the Cabinet Secretary invited the Comptroller and Auditor General to undertake an annual evaluation of a sample of RIAs. In March 2004, the results of the first such annual evaluation were published.¹

4 This report summarises the second year of RIA evaluations. Out of some 175 RIAs produced in 2003-2004 we selected a sample of ten. This was based on RIAs identified by the Better Regulation Task Force as those from which lessons could be drawn.² We are, once again, grateful to the Task Force for providing an excellent sample of RIAs containing many useful examples of good practice and also learning points.

Findings

5 The NAO's evaluation considered seven technical aspects of RIAs: defining the problem; the identification of alternative solutions; the analysis of costs and benefits; competition assessment; compliance analysis; taking account of small business; and monitoring and evaluation. In addition to the technical aspects, we broadened our scope to consider the RIA process as a whole and undertook structured interviews with key staff to consider aspects such as how well departments felt the process worked, and the role of the Cabinet Office. Appendix 1 gives a full description of our methodology. Our findings are based on a similar framework of evaluation to that used in our 2003-04 report, and in some areas in this report we draw attention to the relevant findings from last year's evaluations.

Defining the problem

6 Clear objectives at the outset derive from what departments aim to achieve with their policy proposals. Departments need to define the problem the proposed regulation aims to address. This is referred to in Cabinet Office guidance as risk assessment. A robust analysis of the problem, quantified where possible, will allow departments to consider how their objectives relate to the problem, and to analyse the relevant costs and benefits of the proposed regulation. Eight out of ten RIAs in this year's sample contained good or acceptable problem definitions, with quantified estimates in four of them.

The identification of alternative solutions

7 Departments should consider a range of options to achieve their policy objectives. These options should include alternatives to regulation, and an analysis of the Do Nothing option. This should provide a clear analysis of the likely situation in the absence of the proposals. Without this there can be no proper assessment of the costs and benefits of the proposal. A good RIA should demonstrate and justify the reason for the choice of the preferred option.

8 The extent to which some RIAs could consider a full range of options was limited, because they were started at a late stage in the decision making process. Nine of the ten RIAs in our sample did however include a Do Nothing option. Six of the RIAs in our 2003-04 sample did not.

The analysis of costs and benefits

9 RIAs go through a number of stages of development, the last of which is the Final RIA. This includes a statement signed by the relevant Minister indicating that the benefits of the regulation justify the costs. Eight of the ten RIAs in our sample included some quantified assessments of costs. Benefits are often more difficult to quantify than costs and only four RIAs in the sample did so.

10 Cabinet Office guidance states that a central component of the RIA is the analysis of costs and benefits. It is therefore important that departments involve specialists, such as economists, at an early stage to advise those preparing the RIA of available methodologies. But estimating costs and benefits involves judgement and many cannot be calculated to a fine degree of precision.

¹ C&AG's report: Evaluation of Regulatory Impact Assessments Compendium Report 2003-04, HC 358, 4 March 2004.

² The Better Regulation Task Force is an independent body, set up in 1997 to advise Government on action to ensure regulation and its enforcement accord with good practice (paragraph 1.22).

11 Departments should reflect uncertainties when they present quantified estimates. Where a single point estimate is presented, departments should be clear about the assumptions or strength of evidence supporting the estimate. They can reflect uncertainties by undertaking sensitivity analysis. Where evidence is sufficiently robust, departments can present a range of costs and benefits, which can be used to inform consideration of different scenarios. Here again, departments should be clear about the degree of uncertainty underlying the ranges. Some of the quantified estimates in the RIAs in our sample were presented as single point estimates, but without clearly reflecting the underlying uncertainties.

The assessment of competition

12 For all RIAs produced from 2002 departments must consider the implications for competition of the regulatory proposals and include a competition assessment in the RIA. Where an initial test indicates there may be an impact departments should discuss the competition assessment with the Office of Fair Trading,³ which also provides expert advice and training. All departments in our sample included an initial competition assessment, and all sought the advice of the Office of Fair Trading.

The analysis of compliance

13 Compliance with regulations by the targeted bodies or individuals is crucial to the achievement of the regulating Department's objectives. Analysis of likely compliance should inform a Department's choice of policy options, and the regime by which the regulation will be enforced. Departments should consider the level and pattern of compliance to ensure the proposals are properly targeted. In our sample departments did not present their consideration of different levels or patterns of compliance. As in last year's sample, all RIAs presented a discussion of 100 per cent compliance with the proposals.

Taking account of small businesses

14 Small businesses are important to the UK economy and regulations can have a disproportionately large impact on them. Departments must therefore pay particular attention to the potential impact of their proposed regulations on small businesses, and all the departments in our sample did so. Where appropriate, departments should consult with the Department of Trade

and Industry's Small Business Service (SBS) in preparing RIAs. Departments did so in all eight appropriate cases in our sample, and the SBS was generally content that the RIAs reflected its views.⁴ However, it felt that in four of the eight cases it had not been given sufficient time to provide a considered response.

Monitoring and evaluation

15 Monitoring and evaluation are important parts of any effective policy making framework, and they can inform future policy development in the relevant areas. RIAs should include an outline of how the regulation and its impacts are to be measured and monitored. Four out of the ten provided a reasonable description of the monitoring and evaluation procedures, such as when and how reviews would be undertaken. The remaining six did not.

The consultation process

16 Departments are expected to undertake formal consultations with affected stakeholders on the proposal. The consultation document should include and draw attention to the Partial RIA and ask for consultees' comments on the estimates in it. Consultation was generally done well in our sample. Nine of the ten RIAs in the sample undertook formal consultations.⁵ The Partial RIAs and consultation documents in our sample were clear and explained well the relevant department's expectations of impacts. We found that consultation was most effective where departments held ongoing discussions with stakeholders throughout the process, in addition to the formal consultations.

17 Cabinet Office guidance states that RIAs should act as stand alone documents, which should contain sufficient information to explain a department's justification for choosing the preferred policy option to achieve its policy objectives. The RIAs in our sample set out the proposed regulations fairly clearly, though there were gaps in some areas noted above, such as monitoring, evaluation and compliance.

Characteristics of RIAs

18 Our overall finding is that the RIAs in our sample demonstrated an improvement in technical terms compared to last year's sample. The sample illustrates, however, important areas where there is still scope for significant improvement.

³ Office of Fair Trading, Guidelines for Competition Assessment, OFT355.

⁴ The nature of the High Hedges and The Financial System and Major Operational Disruption proposals meant that consultation with the SBS was not appropriate, as there were no likely impacts on small businesses. The SBS agreed with this view.

⁵ The RIA for the National Care Standards Commission Fees and Frequencies of Inspection 2003-04 did not consult, as it merely updated elements of existing legislation. Legal advice had confirmed that consultation was not necessary.

19 We also considered the influence on policy of the RIAs in our sample, because one of their main roles is to inform the policy process. Four of the ten RIAs in our sample led to some changes in policy, ranging from minor refinements to the department deciding not to regulate at all. One in particular showed how the RIA process can have a major impact on the policy making process. The Treasury considered measures to protect the financial system in the event of major disruption using the RIA process. This resulted in the Department deciding not to proceed with regulation.

20 The RIAs in our sample which influenced policy were generally started early in the process, involved good consultation processes, and produced good assessments of the impacts of the policy proposals. These characteristics were similar to those identified in our 2001 Report: *Better Regulation: Making Good Use of Regulatory Impact Assessments*.⁶

21 Three factors limited the influence of RIAs on policy:

- Some RIAs are produced after important decisions have been made. In such cases the RIA may not have much influence on policy, but can still be useful to communicate the decision and its expected impacts;
- Some RIAs deal with the implementation of European Union Directives. In such cases, the measures have already been decided and the UK and other Member States are obliged to implement them.⁷ While the RIAs cannot influence policy directly, it is important that departments continue to produce them. They allow departments to identify the flexibility allowed under the Directive to implement regulation in the least burdensome way; and
- Some RIAs are produced to update aspects of an existing policy, whilst leaving the rest of the policy unchanged.

22 Nevertheless, even in these cases departments can derive some benefit from producing RIAs. Regardless of their influence on policy, RIAs fulfil a vital communication role in line with the Transparency principle of Better Regulation (Figure 1, page 10). For example, departments told us that their RIAs had been used as reference documents and sources of information for Members of Parliament, businesses and others. This illustrates the usefulness of the role of RIAs in gathering evidence and information.

Three approaches to RIAs

23 On the basis of our experience of evaluating RIAs,⁸ we have identified three approaches to preparing RIAs, differentiated in terms of their technical quality and their influence on policy-making:

- **Pro-Forma RIAs:** These have no impact on policy and are produced merely because there is an obligation on departments to do so and may be started after the decision has been made. This can lead to poor RIAs as they may be inadequately resourced and produced too quickly;
- **Informative RIAs:** These have limited impact on policy. These RIAs are not integrated into the policy-making process; for example, they may have been started fairly late. Although the RIA will have only limited relevance, a department can still produce a high quality RIA that clearly outlines the expected impacts, and is therefore a useful communication tool; and
- **Integrated RIAs:** These inform and challenge policy-making. These RIAs are started early and are properly resourced, which allows better gathering and analysis of evidence. In these cases the RIA can help shape the policy making process and communicate the reasons for the department's decision to regulate in the chosen way. In some cases the role of the RIA in challenging policy makers will lead them to a non-regulatory response.

⁶ HC 329 Session, 2001-02.

⁷ In the case of European Directives, the UK will have been involved in the negotiations and consideration of policy options that took place before the Directive was passed. These discussions may also have been the subject of Impact Assessments. In our work for this report, we have not looked at the negotiations that informed the passing of the Directives, or at any Impact Assessments that may have been carried out at that time. We may consider such assessments in future evaluations.

⁸ The C&AG has published two reports which examined RIAs: *Better Regulation: Making Good Use of Regulatory Impact Assessments* (HC 329 Session 2001-02); and *Evaluation of Regulatory Impact Assessments Compendium Report 2003-04* (HC 358 Session 2003-04).



RECOMMENDATIONS

To Departments

A Regulation may not always be the best response to achieve objectives. Departments should use the RIA process to assess options to achieve their objectives, including alternatives to regulation, and whether a regulatory response is the best option.

B Final RIAs should summarise briefly options that have been considered and discarded. This increases transparency and demonstrates that departments have considered a range of options.

C Departments should analyse and present the Do Nothing option in all cases to provide a measure of the impact of the proposals. They should ensure this takes account of the contribution which known existing measures can make to the proposals in the RIA.

D Departments should involve specialists, such as economists, in completing competition assessments at an early stage, and should seek advice from the Office of Fair Trading.

E Departments should include in the RIA process the impacts of different levels and patterns of compliance, and the effectiveness of different enforcement strategies. This should help inform the choice of options and the most appropriate enforcement regime.

F Departments should allow the Small Business Service sufficient time to consider the implications of proposals on small businesses.

G RIAs have the greatest value if they are integrated into the policy process. Departments should aim to produce good quality RIAs that inform and challenge policy-making.



H Departments should ensure that the RIAs produced are fit for the required purpose. There is no point in producing complex or elaborate RIAs for small-scale regulations, while other regulations demand in-depth analysis integrating the efforts of economists, statisticians, lawyers and subject-matter experts.

I Producing RIAs and monitoring and evaluation lead to collection and analysis of a great deal of information. Where this information relates to departments' performance measurement indicators, departments should ensure that the information is incorporated into their performance reporting.

To the Cabinet Office

J Around 175 RIAs were produced across the Government in 2003. If RIAs are to maximise their influence, and to serve as a communication tool, it is important that businesses and others can obtain up to date lists of RIAs. Cabinet Office should update its website regularly to ensure all RIAs are included.