Regulation and Cost-Benefit Analysis

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Short Presentation to Economic Society Conference

Sydney July 2017

Overview

- Why regulate: Objectives of regulation
- Examples of regulation and their objectives
- Using CBA
- Arguments against CBA
- Conclusions

Why regulate: Objectives of regulation

- Market failure and social equity – standard reasons
- Generic laws / property / prudential regulation
- Monopoly – ACCC not discussed in this presentation
- Key micro driver is protection in one form or another
  - Poor information leading to poor individual or corporate decisions / outcomes
  - Negative externalities – third party effects
  - Unequal powers

Example	Main reasons
Prudential regulation	Systemic protection
Penalty rates	Unequal powers
Occupational and workplace safety standards	Unequal powers; poor information / outcomes
Female representation on company boards	Unequal powers; poor information / outcomes
Product standards, e.g. food safety standards	Poor information / outcomes (*)
Tobacco product messaging	Poor information / outcomes (*)
Trade and professional standards	Poor information / outcomes (*)
Swimming pool safety barriers	Poor information / outcomes; third party effects (*)
Driving regulations	Third party effects; poor information / outcomes
Environmental protections	Third party effects
Lock-out regulations	Third party effects
Planning regulations	Third party effects
Minimum housing standards	Protection of residents (*)
Short-term letting	Third party effects
Regulation of dogs	Third party effects

Cost-benefit analysis

- CBA is standard method of evaluation policies (viewing costs and benefits) with objective of maximising social welfare.
- Note: the objectives of any regulatory intervention should be stated – e.g. addressing specific market failures / objectives.
- Options analysis is important; should include non-regulatory options should be explored in the CBA.

References

- Office of Best Practice Regulation, 2016, *Cost-Benefit Analysis,*
  - Fully committed to use of CBA to evaluate regulations
- NSW Treasury, 2017, *NSW Government Guide to Cost-Benefit Analysis*, TPP 17-03
  - *A CBA is required for: All significant new and amending regulatory proposals for which the NSW Guide to Better Regulation requires consideration of the costs and benefits of a range of options, and that may not affect Government funds but could affect costs or benefits for households or business.*
- Regulatory Policy Framework Review Panel, *Independent Review of the NSW Regulatory Policy Framework.*
  - Generally supportive of CBA

Selective examples of CBA for regulations

- Applied Economics, 2003, *Cost-benefit Analysis of Proposed New Health Care Warnings on Tobacco Products*, prepared for Commonwealth Department of Health and Ageing.
- Acil Allen, 2015, Independent Review of the Building Professionals Act 2005, *Cost-Benefit Analysis of Proposed Regulations*.
- CIE, 2016, *Regulation of Private Swimming Poll Barriers*, prepared for Office of Local Government.
- NSW Treasury, Centre for Program Evaluation, 2016, *Evaluation of the Sydney CBD Entertainment Precinct Plan of Management*

Four Issues with CBA

1 CBA too onerous. A general question of significance of regulation. Some regulations very minor.

CBA should be proportionate and scalable. The major costs and benefits can usually be stated quite simply. CBA does not have to be onerous.

2 CBA not possible – forecasting behavior / outcomes. Some major impacts cannot be quantified / valued. E.g. impacts of tobacco warnings on behaviour; swimming pool drownings averted ; behaviour of surveyors.

Note difference between quantification and valuation. If outcomes cannot be quantified approximately, no evaluation method will work.

3 CBA inappropriate when dealing with social equity issues, e.g. OHS; producers selling dangerous products and deceiving consumers. Or causing pollution of one or other kind. Health insurance in USA. Raises moral and weighting issues.

4 There are better methods, such as multi-criteria analysis ???

Conclusions

- CBA is core evaluation process for substantive social issues.
- Many regulations are very minor – but still consider costs and benfits
- Especially focus on reason for regulation and options
- Major problems are in forecasting behavior / outcomes not in valuation process. But they are general problems not CBA problem
- When there are significant equity objectives, CBA is a useful framework for evaluating outcomes but decision makers may weight outcomes in a different way.