Chapter 1. Overview: Why does the quality of domestic rule-making matter?

Laws and regulations are essential tools in the hand of governments to promote well-being and economic growth. Over the past 30 years, governments have progressively developed the disciplines and tools of regulatory policy to ensure their quality. However, as governments have continuously improved their understanding of regulatory quality, regulating itself has become increasingly difficult. The growing pace of technological changes and the deepening of globalisation are raising substantial challenges for domestic regulators. This chapter highlights the high-level trends in regulatory policy and governance and points to some of the challenges and opportunities faced. In doing so, it lays the grounds for the following chapters of the Regulatory Policy Outlook that investigates in more depth country practices in the systematic application of selected regulatory policy approaches.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Laws and regulations are a critical tool for policy making that supports well-being and economic performance

Regulation affects all areas of business and, indeed, of life. We see proof of this every day: when we eat our breakfast without questioning the quality of the food, when we take our kids to school using public transport or driving, when we feel safe at work, when we consult doctors and undertake medical exams. The rules that determine our safety and lifestyle are usually taken for granted and yet are so important.

Laws and regulations are issued by governments and legislators to protect consumers, workers, the environment and the like. However, it is an area where too little or too much can be similarly harmful. When too limited, poorly conceived, redundant or incoherent, these rules can make it difficult to start up a new business, trade abroad or comply with basic administrative procedures, such as getting married, renewing a passport or registering a new birth. Overcomplicated regulatory frameworks, lack of transparency in rule-making, and inefficient or improper enforcement can become irritating or worse. Unbalanced or disproportionate regulations can lead to losses in organisational performance, too much administrative discretionary power to make decisions or enforce rules and even to corrupt behaviour.

Worse, inadequate rules may not achieve their objectives and thus fail to protect us, leading us to lose trust in our institutions and even in government itself. We notice the importance of rules typically when they do not work, either because they are patchy, badly designed or poorly enforced. That is also when they tend to make headlines (Box 1.1).

Box 1.1. Regulatory failures in the news

2008 Financial crisis: Regulators asleep at the wheel (The Economist, 7 September 2013) – "Failures in finance were at the heart of the crash. But bankers were not the only people to blame. Central bankers and other regulators bear responsibility too, for mishandling the crisis, for failing to keep economic imbalances in check and for failing to exercise proper oversight of financial institutions (…)".

Source: www.economist.com/news/schoolsbrief/21584534-effects-financial-crisis-are-still-being-felt-five-years-article

A Timeline of the Water Crisis in Flint, Michigan: "It's been more than three years since Flint, Michigan, switched its water source in an effort to save money, which led to a man-made public health crisis embroiling Michigan Gov. Rick Snyder's administration in scrutiny and criminal charges against a number of public officials. The most serious counts have been levied against Michigan's top health official and four others, who were charged Wednesday with involuntary manslaughter".

Source : www.usnews.com/news/best-states/michigan/articles/2017-06-14/a-timeline-of-the-water-crisis-in-flint-michigan

Dieselgate in Europe: How Officials Ignored Years of Emissions Evidence: "When American authorities revealed that Volkswagen used software to trick pollution tests, it spurred widespread outrage. Documents obtained by SPIEGEL show that European officials knew about the deception for years – but didn't act on it."

Source: www.spiegel.de/international/business/volkswagen-how-officials-ignored-years-of-emissions-evidence-a-1108325.html

Facebook Scandal: a "Game Changer" in Data Privacy Regulation (Bloomberg, 8 April 2018) – "Revelations that data belonging to as many as 87 million Facebook Inc. users and their friends may have been misused became a game changer in the world of data protection as regulators seek to raise awareness about how to secure information".

Source: www.bloomberg.com/news/articles/2018-04-07/facebook-scandal-a-game-changer-in-data-privacy-regulation

Laws and regulations may be perceived as burdensome and inadequate

Despite their importance, laws and regulations come at a price. Along with the benefits they are expected to generate and the objectives they are supposed to achieve, laws and regulations impose constraints on behaviour and therefore imply a range of costs. These regulatory costs include those attributable to the adoption of a regulatory requirement, including the costs of designing and enforcing borne by the authorities, as well as the costs of complying, which can be borne by business, consumers, government authorities or other groups (OECD, 2014[1]). Many (in particular businesses) increasingly lament the burdens of laws and regulations. A variety of institutions have started scrutinising and calculating the administrative costs involved in complying with laws and regulation.[1]

Against the growing perception that regulatory and legislative inflation stifles economic activity, attempts to control the overall amount of regulatory costs have developed in most OECD countries. In the 1990s, the Netherlands pioneered the Standard Cost Model, a method to quantify administrative burdens in monetary terms, and initiated a government commitment to reduce administrative burdens by 25% within five years. Most European governments, starting with Denmark, the United Kingdom and the Czech Republic, adopted the approach. Other countries took slightly different approaches and introduced a cap on administrative burdens, zero-growth policy regarding administrative/regulatory costs, or moratoria on regulatory costs. In the last five years, the offsetting of new regulations by reducing the existing ones (or variation of the "One-In, One-Out" policy initially adopted in the United Kingdom in 2011) started gaining ground across countries, including Canada, Germany, Korea, the United States, Mexico and France (OECD, Forthcoming[2]). Governments have identified some achievements and positive impacts of these strategies (Box 1.2).

Box 1.2. Examples of results of burden reduction strategies

In Belgium, reforms have led to a EUR 1.25 billion reduction in administrative costs for citizens and businesses over the period 2008-2014 (with roughly 65% of these savings benefitting business and 35% benefitting citizens).

Source: www.simplification.be.

In Germany, regulatory reform achieved various reductions in compliance costs for business, citizens and the administration. A 2014 amendment of the Social Code decreased annual compliance costs by EUR 126.8 million. By simplifying electronic invoicing, the administrative burden for business was reduced by circa EUR 3.3 billion per year in 2011 compared to 2006 (measured as of 1 January 2012). Additional key elements of the regulatory reform initiatives included benefits for the economy of some EUR 1.45 billion a year, through a shortening of retention periods under commercial, tax and social legislation (EUR 600 million); e-government activities (EUR 350 million); harmonisation of requirements for financial and payroll accounting (EUR 300 million); and advanced electronic signature for businesses (EUR 100 million).

Source: (The Federal Government, 2015[3]), "Better Regulation 2014: Official – simple – tangible", https://m.bundesregierung.de/content/en/artikel/buerokratieabbau_en/anlagen_en/2015-07-20-jahresbericht-2014_en.pdf?__blob=publicationfile&v=5; (The Federal Government, 2012[4]), "A foundation for better law: five years of bureaucracy reduction and better regulation", https://m.bundesregierung.de/content/infomaterial/bpa/beauftrbuerokratieabbau/jahresbericht_2011_grundstein_fuer_besseres_recht_englisch.pdf;jsessionid=1fb39c329465b664792b56a4e7177913.s1t1?__blob=publicationfile&v=2.

In February 2014, the **Greek government**, working with the OECD, identified administrative costs totalling EUR 4.08 billion in 13 policy areas. Over three-quarters of the burdens identified were in three priority areas: VAT administration, company law and annual accounts, and public procurement. Reductions were achieved by i) cleaning the VAT register and removing VAT filing requirements on businesses with zero turnover (EUR 226 million); ii) introducing a clear minimum turnover threshold for micro businesses of EUR 10 000, so that the smallest businesses can choose whether the administrative burdens of VAT administration outweigh the business advantage for them (EUR 136 million); and iii) removing duplicate and expensive publicity arrangements for company annual accounts and event-driven notifications, and putting the arrangements online (EUR 60 million).

Source: (OECD, 2014[1]), *OECD Regulatory Compliance Cost Assessment Guidance*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264209657-en.

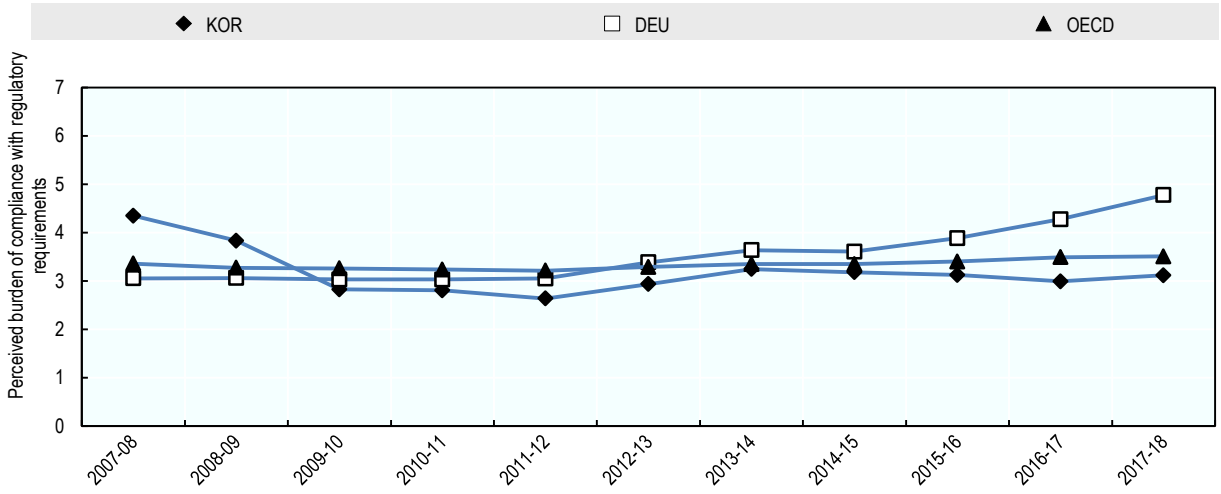
In the United Kingdom, the "war on red tape" has saved business an estimated GBP 10 billion over 2010-15 by abolishing unnecessary regulations, for example:

- Pubs and village halls can now host live music events between 8 am and 11 pm without applying for a licence
- It is no longer a legal offence to fail to report a grey squirrel on your land
- Child minders who feed children in their care no longer have to register separately as a food business
- The age at which people can legally buy Christmas crackers was lowered from 16 to 12 years old
- Bus companies no longer have to hold on to property, including decaying food left behind by passengers, for at least 48 hours and can instead decide themselves which items will be re-claimed
- Cattle movements no longer have to be recorded on a lengthy paper based system and now are tracked online, freeing up farmers

Source: (GOV.UK, 2014[5]), "Hancock: red tape drive saves business a record £10 billion", www.gov.uk/government/news/hancock-red-tape-drive-saves-business-a-record-10-billion.

However, despite government efforts, perceptions of regulatory burdens have not changed drastically. For example, results from the World Economic Forum's Executive Opinion Survey show that business perception of the burden of government regulation has stagnated over the last ten years, with some differences across countries (Figure 1.1). Business perceptions have improved most in Germany (by 1.7 points), and deteriorated most in Korea (by 1.2 points). In the United Kingdom, despite the Red Tape Challenge, the proportion of business that feel compliance with regulation is their greatest challenge and that expect regulatory burden to increase within the next year has increased since 2014 (GOV.UK, 2016[6]).

Figure 1.1. Trends in the perceived burden of compliance with regulatory requirements



Notes: Results are based on the question: "In your country, how burdensome is it for businesses to comply with governmental administrative requirements (e.g., permits, regulations, reporting)? [1 = extremely burdensome; 7 = not burdensome at all]".
Source: (Browne et al., 2016[7]), "The Executive Opinion Survey: The Voice of the Business Community", The Global Competitiveness Report 2016–2017, World Economic Forum, Geneva, http://reports.weforum.org/global-competitiveness-index-2017-2018/appendix-c-the-executive-opinion-survey-the-voice-of-the-business-community/.

StatLink https://doi.org/10.1787/888933813932

Systematic surveys of citizens' opinions on regulatory quality and burdens are less developed. Generally speaking, in line with business, citizens prefer more simplified procedures and formalities. At the same time, the regulated community often lacks awareness of the benefits of regulation, as these are often diffuse while costs are borne by specific groups more directly (OECD, 2012[8]). Citizens have benefited in most countries from simplification measures. Digitalisation, in particular, has simplified citizens' lives in diverse areas, including taxation, marriage, visas, passports and voting. Initiatives such as the critical life event surveys carried out in France and Germany (OECD, 2016[9]) have helped identify bottlenecks that were generating costs for citizens and focus public action to alleviate them.

Overall it seems that citizens' satisfaction with government services, partly a result of regulatory quality, is on the rise in a number of countries. In France, perception of public service quality increased from 5.4 to 7.2 points on a scale from 0-10 between 2010 and 2016 (Le Portail de la modernisation de l'action public, 2016[10]). In Germany, citizens

rated their satisfaction with government services at 1.06 on a scale from +2 (very satisfied) to –2 (very unsatisfied) in 2015.[2]

However, perception of regulation depends on many different aspects, such as age and level of education. A 2017 Pew Centre study on attitudes towards (financial) regulation conducted in the United States shows that younger and more educated people do not think regulation goes far enough, whereas older people and the less educated (the ones to benefit the most from many protections) think there is too much regulation (Smith, 2017[11]). More generally, the Edelman Barometer 2016 finds a widening disparity between levels of trust in public institutions according to income, with high-income persons reporting a higher degree of trust in government (on average 10% higher).[3]

In effect, the demands for regulation are multiple and contradictory, combining better protection with lower costs and less intrusion, a fact well illustrated by Professor Malcolm Sparrow in 2000:

> *"Regulators, under unprecedented pressure, face a range of demands, often contradictory in nature: be less intrusive – but be more effective; be kinder and gentler – but don't let the bastards get away with anything; focus your efforts – but be consistent; process things quicker – and be more careful next time; deal with important issues – but do not stray outside your statutory authority; be more responsive to the regulated community – but do not get captured by industry" (Sparrow, 2000, p. 17[12]).*

Despite the expectations, regulation remains a largely under-scrutinised policy tool

Despite a strong rationale – the benefits of good regulation and the dire consequences of bad regulation – regulatory quality (Box 1.3) is still not receiving the attention it deserves from governments. Regulatory policy and governance is still seen as a largely technical and less politically rewarding domain of policy making and continues to attract less attention from politicians and the media than the budget process or tax policy.

The quality of rules receives much less scrutiny than budget processes, government spending patterns or tax policy. For example, professional parliamentary oversight of the budget is strongly institutionalised in most OECD countries. By contrast, only a handful of countries have established specific technical units within parliaments to oversee legislative quality. This gap is prompting the academic community to call for more "scientific rigour" in the design of government laws and regulation. See, for example (Coglianese and Rubin, 2018[13]).

Box 1.3. What is regulatory quality?

Pursuing "regulatory quality" is about enhancing the performance, cost-effectiveness, and legal quality of regulations and administrative formalities. First, the notion of regulatory quality covers processes, i.e. the way regulations are developed and enforced. These processes should be in line with the principles of consultation, transparency, accountability and evidence. Second, the notion of regulatory quality also covers outcomes, i.e. whether regulations are effective, efficient, coherent and simple. In practice, this means that laws and regulations should:

1. serve clearly identified policy goals, and are effective in achieving those goals;
2. be clear, simple, and practical for users;
3. have a sound legal and empirical basis,
4. be consistent with other regulations and policies;
5. produce benefits that justify costs, considering the distribution of effects across society and taking economic, environmental and social effects into account;
6. be implemented in a fair, transparent and proportionate way;
7. minimise costs and market distortions;
8. promote innovation through market incentives and goal-based approaches; and
9. be compatible as far as possible with competition, trade and investment-facilitating principles at domestic and international levels.

Source: (OECD, 2015[14]), *OECD Regulatory Policy Outlook 2015*, OECD Publishing, Paris, based on (OECD, 1995[15]), *OECD Recommendation on Improving the Quality of Government Regulation*, OECD, Paris, https://legalinstruments.oecd.org/en/instruments/128.

Given the stakes, promoting the quality of laws and regulations is essential

Regulatory policy and governance are not only crucial for improving the quality of laws and regulations; they are also instrumental to build confidence in their value and importance in the everyday life of businesses and citizens. For example, (Lind and Arndt, 2016[16]) show that careful design of procedures in the development and administration of laws and regulations can enhance the perceived fairness of regulations and procedures. In turn, attitudes toward laws and regulations as well as behavioural compliance with regulatory decisions are often as strongly affected by citizens' experiences with, and perceptions of, the process as they are by its outcome (Mazerolle et al., 2012[17]); (Van den Bos, Van der Velden and Lind, 2014[18]). The links among results, perceived process fairness, and the acceptance of rules and decisions is even more important in times of deepening mistrust in institutions.

There are many instances where countries have reported significant burden reductions for businesses and citizens thanks to regulatory policy tools. If businesses and citizens see tangible results, investing in better regulation is a worthwhile investment. For example:

- Between 2012 and 2017, the Dutch government reported a EUR 2.48 billion reduction in regulatory burdens for businesses, citizens and professionals (Government of the Netherlands, 2017[19]). Measures included simplified accounting and reporting rules for small and medium-sized enterprises, a new online tool that generates a tailor-made privacy statement for businesses, and the development of an app that trains employees how to follow companies' emergency response plans.

- In March 2016, U.S. Federal agencies released their first reports estimating the impact of streamlining, revising and eliminating many existing rules undertaken in the framework of Executive Order 13563. In total, U.S. agencies estimated their savings for businesses and subnational governments at USD 28 billion over five years (Shelanski, 2016[20]).
- The European Commission's REFIT programme has resulted in a number of cost-saving initiatives, including more ambitious targets for waste prevention and recycling expected to bring savings of 1.3 billion per year; a one-stop shop allowing a business to declare VAT in the Member State in which it is established, thus reducing business compliance costs by EUR 2.3 billion a year; a Single Digital Gateway that could help companies save more than EUR 11 billion per year; and revised legislation on veterinary medicines that cuts costs by an estimated EUR 145 million (European Commission, 2017[21]).

Regulatory policy is a critical dimension of an enabling environment for investment and thus of economic growth and innovation. For example, rating agencies include the quality of regulatory frameworks as one of the key variables when making assessments and providing credit profiles for regulated utilities. See for example, (Moody's Investors Service, 2013[22]). In some countries, regulatory quality and stability can account for over one-third of the rating methodology: a good and stable framework directly translates into higher credit worthiness, a lower cost of finance and potentially higher investment.

The links made in the literature between regulatory governance and economic performance should nevertheless be updated and researched further (Box 1.4). New work is needed to link a detailed understanding of regulatory quality disciplines, their uptake in various sectors and countries and their impacts on sector outcomes, on economic performance and on well-being.

Box 1.4. Some early links between regulatory quality and economic performance

- (OECD, 2014[23]) presents a Framework for Regulatory Policy Evaluation including concrete concepts and performance indicators for the inputs, outputs and outcomes of regulatory policy. While it notes that demonstrating a causal link between regulatory policy and policy outcomes still remains the "holy grail" of performance evaluation, the application of the Framework could be a step towards measuring the application of regulatory policy in practice, and thus ultimately towards achieving regulatory objectives.
- (Parker and Kirkpatrick, 2012[24]) review the quantitative evidence on the impact of regulatory policy on economic outcomes. The result of the review seems to confirm that poorly designed regulation can stifle economic activities and ultimately reduce economic growth, and that regulatory governance and the institutional framework in a country may mitigate the damaging effects. The authors also point to considerable methodological problems and a lack of data for robust quantitative evidence on the economic impacts of regulatory policy, as well as a focus on costs of regulation in existing studies compared to few attempts to quantify the benefits of regulation.
- (Bouis and Murtin, 2011[25]) find that regulatory barriers to entrepreneurship, explicit barriers to trade and – especially – patent rights protection appear to be fairly robust determinants of long-run cross-country differences in technology. Some other policies and institutions such as trade liberalisation are found to

speed up technology convergence.

- (Jacobzone et al., 2010[26]) find that improvements in the quality of regulatory management systems yield significant economic benefits in terms of increased GDP and labour productivity in the business sector.
- Using measures of business regulations in 135 countries, (Djankov, McLiesh and Ramalho, 2006[27]) show that an improvement from the worst quartile of business regulation to the best results in a 2.3% increase in an annual growth.
- (Kaufmann et al., 2005[28]) focus more broadly on governance and compute an index of approximately 200 countries over six biannual time periods (1996 through 2004). They point to a strong observed correlation between income and governance, and argue against efforts to apply a discount to governance performance in low-income countries.
- (Hall and Jones, 1999[29]) find that across 127 countries, the difference in capital accumulation, productivity and output per worker are driven by differences in institutional and government policies.

Sources: (OECD, 2014[23]), *OECD Framework for Regulatory Policy Evaluation*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264214453-en; www.oecd.org/gov/regulatory-policy/publications-mrp.htm; (Bouis and Murtin, 2011[25]) "The Policy and Institutional Drivers of Economic Growth Across OECD and Non-OECD Economies: New Evidence from Growth Regressions", *OECD Economics Department Working Papers*, No. 843, OECD Publishing, http://dx.doi.org/10.1787/5kghwnhxwkhj-en; (Jacobzone et al., 2010[26]), "Assessing the Impact of Regulatory Management Systems: Preliminary Statistical and Econometric Estimates", *OECD Working Papers on Public Governance*, No. 17, http://dx.doi.org/10.1787/5kmfq1pch36h-en; (Djankov, McLiesh and Ramalho, 2006[27]), "Regulation and Growth", *SSRN Electronic Journal*, http://dx.doi.org/10.2139/ssrn.893321; (Kaufmann et al., 2005[28]), "Governance Matters IV: Governance Indicators for 1996-2004", www.worldbank.org/wbi/governance/govdata/; (Hall and Jones, 1999[29]), "Why Do Some Countries Produce So Much More Output per Worker than Others?", *The Quarterly Journal of Economics*, Vol. 114/1, pp. 83-116; (OECD, 2011[30]), *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264116573-en.

Regulatory policy is even more important given the transformative and disruptive changes in our societies and economies

Regulating in "normal times" can be a daunting task. With the ever-increasing pace of transformative technological change, governments face growing complexity and uncertainty in many regulated areas. Transformative technologies are innovations that use advances in computing power, connectivity, mobility, and data storage capacity to fundamentally change – "disrupt" – an established market. By doing so, these technologies simultaneously offer potential economic rewards, higher productivity growth, and improvements to living standards by often fulfilling a gap in consumer preferences. These technologies and business platforms can also posing a risk, potentially significant, and a range of regulatory challenges. These include managing the social, employment and other impacts of the digital economy, balancing the progress and impacts of artificial intelligence and robotics in a range of sectors, and addressing the ethics of stem cell technology and other genetic technologies.

Given the distinct potential of significant gains and losses, governments have to balance how to promote the adoption of innovative technologies while managing or mitigating the risks they pose. On the one hand, governments must be vigilant in adopting regulations that mitigate and protect from any potentially adverse economic and societal impacts of

technological disruptions. On the other hand, the regulatory environment should not unduly limit innovation. This trade-off is complicated by the fact that disruptive technologies are increasingly blurring the lines between consumers and producers and between regulatory domains thus making targeted interventions all the more difficult to manage. A further difficulty faced by many regulators in developing their responses is whether or not they have the mandate to address the issue, or whether they are reliant on government to institute a more fundamental policy change.

Governments have taken a variety of approaches to developing adaptive regulations that both promote innovation and mitigate risks in an impartial and proportional fashion. These have ranged from heavy handed approaches that explicitly prevent the development or adoption of new technologies to lighter touch ones, for example by adopting fixed-term regulatory exemptions (e.g. regulatory sandbox) for innovative entrants that maintains overarching regulatory objectives, such as consumer protection. In many sectors and markets, given the pace of technological advancement, regulators have opted for "wait and see" approaches to allow for time to discover which perceived risks materialise. In a few rare cases, governments also have seized the opportunity of the disruption to reform markets where legacy regulations were burdensome or irrelevant and regulatory reforms were unsuccessful.

New technologies have also shown their potential to provide consumers with more information than through more traditional sources. This can ultimately result in less information asymmetry and less need for regulation to protect consumers. However, this also requires frameworks to ensure information integrity, uphold quality and safety standards, ensure privacy, and address potentially negative impacts on society. Similarly, changes to the nature of employment brings up considerations about how workplaces are regulated, what types of support mechanisms are in place, and how to ensure workers are adequately trained to benefit from new opportunities. When considering restrictions to new technologies, governments need to consider if the restrictions are essential to public safety or interest, if they reflect real or perceived risks, and consider the best options to achieve the intended outcome.

If anything, this disruptive environment is a further justification for a more systematic use of regulatory policy and governance principles and tools. Indeed, regulatory management tools such as regulatory impact assessment, stakeholder engagement and *ex post* evaluation, offer opportunities to reflect and gather a variety of views on the impacts of regulation on innovation, while safeguarding public interest. A majority of countries assess the impacts of new regulatory measures on innovation as part of the regulatory impact assessment process, a new development since the 2015 *OECD Regulatory Policy Outlook* (OECD, 2015[14]). Using approaches such as behavioural insights throughout the policy cycle has also helped in obtaining and using evidence to drive decision making and ensure that implementation is taken into account in the early phase of policy development.

One of the great benefits of new digital technologies is that government administrations themselves can use these advances to increase their capacity to regulate effectively. Technological innovation, in particular in the field of information technology, creates opportunities to promote evidence-based, inclusive and effective laws and regulations. Artificial intelligence, the use of algorithms and the growing uptake up of open data, as well as social media are some examples of how new technologies can help regulators collect timely information, conduct data analysis, engage with various communities and

ensure greater coherence in policy. Also, the possibilities offered by "big data" might enable the development and enforcement of regulations based on risk analysis.

Data has already been utilised by governments to improve monitoring capacities and create better responses to problems in the market, especially regarding public policy objectives that were previously imperfectly observable or only observable at a significant cost. Digital technologies can also replace or complement traditional enforcement methods and support policy evaluation. However, governments often lack the capacity to use these technologies to monitor economic, environmental and social outcomes leaving them "flying – at least partly – blind". Sharing of data and cooperation between agencies would improve capacities to solve complex problems, but how to break down silos remains an issue. All these approaches require further exploration. Alongside their obvious benefits, they bring up unprecedented issues of privacy, legitimacy and impartiality.

The increased interconnectedness of economies puts strain on regulatory capacities

Partly due to the many technical revolutions of the past 30 years, the interconnectedness of countries and the integration of the world economy have increased drastically by any number of measures (trade, migration, transport, communication) (Box 1.5). The rapid flow of goods, services, people and finance across borders is testing the effectiveness and the capacity of domestic regulatory frameworks. Both the quality of new regulatory measures and their effective enforcement are under strain.

National jurisdictions are increasingly losing oversight and control of activities happening in, or having an influence on, their territory. For example, digitalisation, and in particular its consequences in terms of erasing borders, is challenging tax frameworks. Tax avoidance strategies exploit gaps and differences in tax rules across jurisdictions as well as the possibility to artificially shift profits to low- or no-tax locations.[4] The sophisticated markets of the global economy are also opening up opportunities for criminal networks to expand illicit trade activities, including trafficking in persons, wildlife, narcotics, counterfeit medicines, tobacco and alcohol, with serious negative consequences for the economy and society. The profits of international organised crime could be as high as USD 870 billion, or around 1.5% of global GDP (OECD, 2016[31]).

In addition to financial losses, these trends may undermine the benefits of international flows and citizens' trust in globalisation. For example, trade in counterfeit goods undermines the competitive advantage of rights holders, hampers innovation and employment, reduces tax revenue and can jeopardise public health and security. Globalisation also allows larger and more organised actors to take advantage of loopholes in the international framework. For instance, some multinational companies shift their revenues to other jurisdictions to reduce or evade taxation, and de facto avoid paying part of their contribution to domestic welfare.

In this context, close co-operation among regulators has become a key element of regulatory effectiveness. In particular, the exchange of information and evidence among regulators helps better identify the issues that laws and regulations are meant to address. Co-operation is also necessary in many new areas of regulation to facilitate law enforcement and prevent regulatory gaps and arbitrages. For example, countries increasingly need to discuss issues such as how to allocate taxation rights and determine the share of multinational companies' profits that will be subject to taxation in a given jurisdiction (OECD, 2018[32]).

Box 1.5. The increasing economic connectedness of countries

- Between 1990 and 2015, global trade intensity, measured as the share of the total volume of exports and imports of goods and services in world GDP, doubled (OECD, 2017[33]). Today, products cross many borders before they are finally purchased by consumers in a given country (OECD, 2013[34]).
- In 2015, 124 million people living in OECD countries were foreign-born (13% of the total population), compared to 9.5% in 2000 (OECD, 2017[35]). One in four among 15-year-old students was foreign-born or had at least one foreign-born parent (OECD, 2018[36]).
- In 2016, about 83% of the adult population in OECD countries had Internet access. In the same year, 95% of OECD firms had high-speed Internet connection and over half of individuals in OECD countries bought products online (OECD, 2017[37]). Information on Google searches and YouTube viewing revealed an almost universal trend of users increasingly accessing content outside their own country.
- Data on financial flows over Paypal's payment system showed that the Internet is enabling significant cross-border financial transfers on a daily basis, not just between developed countries but also with emerging economies (OECD, 2016[38]).
- A third of US exports in 2011 had become digitally deliverable services, and EU and US exports in general incorporate significant amounts of digitally deliverable services as intermediate inputs (OECD, 2016[38]).
- The number of airports in the world having at least one direct connection to one of the top 100 international airports grew by almost 20%, from 1 795 airports in 2005 to 2 085 in 2015. Over the next 15 years, passenger air traffic is expected to grow by between 3% and 6% annually (ITF, 2017[39]).

Source: (OECD, 2017[33]), *OECD Economic Outlook, Volume 2017 Issue 1*, OECD Publishing, Paris, http://dx.doi.org/10.1787/eco_outlook-v2017-1-en; (OECD, 2013[34]), *Interconnected Economies: Benefiting from Global Value Chains*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264189560-en; (OECD, 2017[35]); *International Migration Outlook 2017*, OECD Publishing, Paris, http://dx.doi.org/10.1787/migr_outlook-2017-en; (OECD, 2018[36]), *The Resilience of Students with an Immigrant Background: Factors that Shape Well-being*, OECD Reviews of Migrant Education, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264292093-en; (OECD, 2016[38]), "Economic and Social Benefits of Internet Openness", *OECD Digital Economy Papers*, No. 257, OECD Publishing, Paris, http://dx.doi.org/10.1787/5jlwqf2r97g5-en; (ITF, 2017[39]), *ITF Transport Outlook 2017*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789282108000-en.

Mistrust in traditional institutions is growing

This is all happening in a context where trust in public institutions, evidence, and expert advice is deteriorating in many OECD countries, a trend summarised in articles such as (Huang, 2016[40]). International surveys show that the level of trust in government has declined since the 2008 financial crisis (Box 1.6). Lack of trust compromises the success of many government policies, programmes and regulations that depend on co-operation and compliance of citizens.

Box 1.6. Results of international surveys on trust

According to the Gallup World Poll, between 2007 and 2015:

- trust in government decreased by an average of 2 percentage points in OECD member countries (from 45% to 43%). In certain countries, such as Slovenia, Portugal, Spain, Finland and Mexico, the decrease has been sharper.
- satisfaction with the education system increased by 6 percentage points in OECD member countries (from 62% to 68%).
- trust in the judicial system increased by 4 percentage points in OECD member countries (53% in 2015 compared to 49% in 2007).
- trust in financial institutions decreased by an average of 9 percentage points in OECD member countries (down to 46% in 2015.

According to Eurobarometer, between 2007 and 2015:

- trust in political parties decreased by an average of 2 percentage points in OECD/EU member countries (from 21% to 19%).
- trust in the press decreased by an average of 1 percentage point in OECD/EU countries (from 47% to 46%).
- trust in television decreased by an average of 4 percentage points in OECD/EU countries (from 60% to 56%).

According to the European Social Survey, between 2008 and 2014:

- trust in parliaments decreased by 5 percentage points (from 58% to 53%) in OECD/EU countries.

Source: (OECD, 2017[41]), *Trust and Public Policy: How Better Governance Can Help Rebuild Public Trust*, OECD Public Governance Reviews, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264268920-en.

Regulatory governance needs to be at the core of government action… but is it?

This increasingly complex environment should convince policy makers, oversight bodies and regulators of the need to entrench sound and robust regulatory policy. This would lay a solid foundation for more advanced regulatory governance initiatives such as increasing international regulatory co-operation or integrating behavioural insights in regulation. In particular, there is an urgent need to stabilise the evidence base that supports policy decisions and establish its credibility. The focus of regulatory policy needs to be on outcomes rather than process, on the effectiveness of laws and regulations and their expected achievements rather than on burden reduction and cost-savings.

The traditional tools of regulatory impact assessment and *ex post* evaluation of regulation, can generate a virtuous circle if used more systematically to improve regulatory quality rather than as a purely bureaucratic exercise. Stakeholder engagement, critical for regulatory transparency and evidence collection, should be reinforced as a safeguard against policy capture, to collect valuable insights from those affected by regulation, and to drive policy innovation.

However, the shortcomings of countries' current approaches that were highlighted in the *OECD Regulatory Policy Outlook 2015* (OECD, 2015[14]) remain largely the same in 2018. In particular, there is still a tendency to adopt a procedural rather than a strategic approach to the use of regulatory policy tools within public administrations. The "lifecycle" of regulations also remains incomplete: countries are more adept at the "early years" – making laws and regulations – than they are at what comes afterwards, enforcing and reviewing them. As a consequence, although certain laws and regulations might be obsolete, imposing unnecessary costs on business and potentially putting citizens at risk, countries still fail to systematically collect evidence, monitor implementation and evaluate results. Without this second half of the lifecycle, it is challenging for countries to reform or remove those regulations that are not working.

Nevertheless, some (albeit slow and patchy) progress has been made in the uptake of regulatory management tools. Countries increasingly seek feedback from citizens and businesses on forthcoming laws and regulations. They use more evidence-based and inclusive processes for developing laws and regulations, for example by consulting with stakeholders early in the process and allowing sufficient time for such consultations. Yet the outcomes of consultation could be better taken into account in designing regulations. More meaningful engagement, greater transparency and better communication is needed to ensure that citizens and business feel included in the policy making process, accept regulatory decisions and, ultimately, trust the government.

Regulatory impact assessment has clearly become an important step in the regulatory process. But it has also become an over-burdened and procedural step, and it is not always targeted to the most significant laws and regulations. Moreover, while attention tends to be focussed on major economic impacts of regulations, assessments largely ignore other significant effects, such as social impacts. Strikingly, despite some progress, there is still no systematic approach to evaluate *ex post* whether laws and regulations achieve their objectives in practice. This lack of evaluation seriously undermines a well-functioning regulatory policy cycle. These gaps may stem from limited quality control and oversight of regulatory policy disciplines – described in OECD work as the "missing piece of the puzzle" (Arndt et al., 2016[42]).

In 2015, the *OECD Regulatory Policy Outlook* noted implementation and enforcement as the weakest links in the application of regulatory policy, and urged countries to pay more attention to regulatory delivery. In 2018, most OECD countries still do not perceive regulatory delivery as part and parcel of regulatory policy. Government-wide policies to promote better governance structures and processes for delivering regulations, as well as to close the feedback loop between those implementing regulations and those responsible for developing them, are still missing.

The 2018 edition of the *Regulatory Policy Outlook* focuses on regulatory oversight as the critical link in the regulatory governance framework, one that can help bridge the gap between formal requirements and implementation. There are clear signs that OECD countries (and others) are establishing regulatory oversight capacities and functions in line with the 2012 Recommendation. For now, responsibilities for regulatory oversight tend to be fragmented. Quality control of regulatory management tools occurs late in the rule-making cycle, and mainly focuses on the procedural quality of RIA. Nonetheless, there are ample opportunities for countries to learn from their institutional differences and collect further evidence on how well their oversight functions are working.

The institutional set-up of regulatory policy also matters. Regulatory authorities and inspection agencies are at the front lines of regulatory delivery and have great potential to foster trust in public administrations. Their actions remain, however, largely disconnected from national agendas for regulation. The number of countries with an explicit policy and framework for improving the governance and performance of regulatory agencies remains limited. It is even worse for inspection and enforcement agencies. Effective cross-cutting policies in these areas require transparent and predictable accountability mechanisms as well as the capacity to use data to report on results. Operating in increasingly complex and uncertain markets, authorities responsible for enforcing regulations must also remain flexible and focused on encouraging and promoting compliance, rather than on exposing and punishing non-compliance.

There is currently much enthusiasm for behavioural insights (BI) as a tool for designing and delivering better policies. OECD research shows that governments around the world are increasingly using BI to improve the design and delivery of regulation, with over 190 public bodies institutionalising the use of BI. The key feature of BI is an experimental approach, seeking to understand the actual behaviour of the beneficiaries of policies and testing possible solutions before implementation. Evidence shows that this new approach is having a real impact by providing countries with the resources necessary to learn, adapt, and implement innovative policy.

There is also scope for embedding BI throughout the regulatory policy cycle to obtain and use evidence in the *ex ante* (RIA) and *ex post* phases of the policy-making process. A new frontier could entail the application of insights from individual behaviour to public and private organisations. For example, BI could be used to help create a compliance culture, helping to implement policies more effectively and to reduce the need for costly and sometimes ineffective enforcement mechanisms. These approaches can be particularly valuable when the success of a policy and regulation depends on a sustainable change in entrenched behaviours and attitudes (e.g. healthy and sustainable food consumption, energy use patterns, etc.).

While the "internationalisation" of regulation has not kept pace with globalisation, the importance of international regulatory co-operation (IRC) does seem to be increasingly recognised across countries. The *OECD Regulatory Policy Outlook 2018* sees some evidence of IRC policy, but few countries have a cross-governmental vision of IRC and IRC governance is highly fragmented. Exceptions include Canada, which has embedded a strong IRC dimension in its new Cabinet Directive on Regulation; New Zealand, which has created a toolkit for applying its IRC vision; and the European Union (EU), which relies on deep regulatory co-operation among members. An overview of OECD countries' IRC practices shows that the mainstreaming of IRC in rule-making is only partial and, so far, relatively superficial. Mexico has made great strides in embedding trade impacts in its RIA process and in systematically linking stakeholder engagement and trade notification. It is, however, quite the exception. The consideration of international instruments in domestic rule-making, a vector of regulatory coherence in line with international commitments under the 1994 WTO agreements on Technical Barriers to Trade (TBT) and on the Application of Sanitary and Phytosanitary Measures (SPS), could be made more systematic.

The *OECD Regulatory Policy Outlook 2018* acknowledges today's major challenges for regulators and their oversight bodies. It identifies areas where countries can invest to improve the quality of laws and regulations. It also provides an essential platform for stressing the importance of laws and regulations as tools of public policy, and of getting

them right, as well as for disseminating countries' efforts to improve regulatory quality. Nevertheless, the Outlook remains partial in its approach – it relies heavily on data collected for 2014 and 2017 through the Regulatory Indicators Survey and its extension to regulatory oversight and international regulatory co-operation. The 2012 Recommendation identifies 12 areas where efforts are needed to make a difference in regulatory quality. A comprehensive better regulation agenda goes beyond the systematic use of regulatory management tools – very much at the heart of this report. More analysis, data collection and identification of best practices need to be undertaken to provide an exhaustive overview of efforts, achievements and gaps in regulatory reform. Future editions of the Outlook will seek to progressively fill the knowledge gaps based on ambitious evidence-based analysis.

Notes

[1] The Nationaler Normenkontrollrat (NKR) evaluates that the annual costs of complying with regulation and rules in Germany increased by EUR 6.7 billion in the period 2013-17, of which EUR 6.3 billion result from the introduction of the German Minimum Wage (2017 Annual Report, http://www.normenkontrollrat.bund.de/webs/nkr/en/publications/_node.html). The Canadian Federation of Independent Business estimates that broad regulatory compliance costs for US businesses are around CAN 205 billion per year, while Canadian businesses, far fewer in number, pay CAN 37 billion. (Marvin Cruz et al., Canada's Red Tape Report 2015 and Toronto: Canadian Federation of Independent Business, 2015).

[2] Statistisches Bundesamt (2017), www.amtlich-einfach.de. We also have a pilot database example: (OECD, 2016[9]).

[3] www.edelman.com/trust-barometer.

[4] See the OECD "BEPS" website and work on Tax Challenges Arising from Digitalisation: www.oecd.org/ctp/beps.

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