G DEVELOPMENTS IN REGULATION AND ITS REVIEW

While many existing inefficient, outdated and anti-competitive regulations are being dismantled, new regulation of the business sector has continued apace. The Government has recently introduced several far-reaching reforms to corporations and competition laws, and there has been a continuation of the sustained growth in new regulations to pursue emerging social objectives.

In developing new regulations, past mistakes need to be avoided. Regulations which rely as far as possible on market-based instruments should be preferred as they can augment market forces to achieve community goals most efficiently. The Commonwealth Government also needs to adopt comprehensive procedures for vetting new subordinate legislation, such as those proposed by the Administrative Review Council.

Microeconomic reform involves more than reforming the existing stock of government interventions in markets: it also involves measures to ensure that the flow of new regulation is justified and that new regulatory regimes are well designed.

In assessing the flow of new regulatory proposals, the Office of Regulation Review (ORR) - which was incorporated into the Commission in 1989 - applies principles adopted by the Government in 1985. These require proponents of new regulations to demonstrate, using adequate documentation, that their proposals address real social or economic problems, that non-regulatory alternatives have been first considered and found inappropriate, and that the expected benefits of the regulation exceed the costs. Where regulation is deemed warranted, the ORR seeks to have efficient features incorporated into the design of the

regulatory regime. These features include specification of the objectives of the regulation, market-based incentives to meet the objectives, and targeted programs to enforce the regulation. The ORR can require agencies proposing regulation to comply with the regulation review guidelines, and it advises the Structural Adjustment Committee of Cabinet on all submissions involving business regulation. In addition to these specific functions, the ORR monitors developments in regulation and contributes to the Commission's general work program.

In this appendix, the Commission discusses:

- **long-term trends and major changes which have occurred in 1991-92 in the general regulatory environment of business; and some specific reforms in sectors which have been the subject of review;**
- **the performance of new national regulatory agencies established by the Commonwealth Government; and**
- **some proposed changes to regulation review procedures.**

Changes in Commonwealth regulation

The overall flow of regulation is difficult to judge. Inappropriate regulation has been steadily wound back in some sectors and the Commonwealth Government has recently introduced some important reforms to the general laws controlling business formation and operation, but governments at all levels continue to routinely regulate business activity.

Some aspects of aggregate regulation-making activities can be measured and a sustained growth in new regulation is apparent. In a recent study of subordinate legislation, the Administrative Review Council (ARC 1992, p.7) observed:

> **There has been vast growth in the volume of delegated legislative instruments. This is illustrated by [the table reproduced overleaf] which shows the number of statutory rules and disallowable instruments made since 1982-83. The trend is evident. The number of instruments has more than doubled, the main contribution coming from the growth of disallowable instruments, with the number of statutory rules remaining relatively constant. By 1990-91, the Senate Standing Committee on Regulations and Ordinances reported 484 statutory rules and 1161 other instruments made in that year.**

Statutory rules and disallowable instruments from 1982-83 to 1990-91

Year	*Statutory rules*	*Disallowable instruments*	*Total*
1982-83	553	150	703
1984-85	445	276	721
1985-86	429	426	855
1986-87	322	335	657
1987-88	345	493	838
1988-89	398	779	1177
1989-90	411	820	1231
1990-91	484	1161	1645

Source: **Senate Standing Committee on Regulations and Ordinances**

The effects of the growth in this new regulation, or the reduction in other forms of regulation, on the performance of the economy is difficult to assess at the aggregate level. A number of factors apart from regulation affect overall economic performance and, at present, the recession is masking the effects of structural reform in the economy.

However, judgments about impact can be made by examining changes to each class of regulation separately. There are three major classes:

- **pro-competitive regulation - laws which establish private property rights, secure private contractual obligations and keep markets open and competitive;**
- **anti-competitive regulation - laws which control the entry of firms and individuals into markets, or prices or production, generally to achieve income distribution objectives; and**
- **social regulation - interventions which direct firms' production and marketing activities to achieve social objectives.**

Pro-competitive regulation

Together, general laws and industry-specific regulation define the legislative framework of business. The most important Commonwealth general laws are the Companies and Securities Act and the Trade Practices Act. They supplement and codify the regulation of trade under common law, by establishing the foundations of corporate formation and operation, by maintaining competition in markets and by reducing the risks of contractual collusion or exploitation.

After a long period of little change, several far-reaching reforms to general business laws have been introduced or proposed this year, to rectify weaknesses perceived in the operations of certain markets in the 1980s. The more important changes are discussed below.

Companies and securities regulation

Companies and securities regulation aims to ensure the free flow of information on the financial position and prospects of corporations. It stipulates penalties for misrepresentation or financial misconduct by company directors and agents.

A new national companies and securities regime came into effect in January 1991. It replaced the previous separate State and Commonwealth laws and agencies with a national Corporations Law and a new and more independent Australian Securities Commission (ASC). As well as unifying and simplifying companies and securities law Australia-wide, the new regime was designed to significantly deregulate business activity. The ASC focuses on ensuring that companies provide adequate information to investors through general disclosure rules, rather than prescribing how businesses should operate and what they should include in their prospectuses. (These reforms were complemented by January 1992 changes to the Australian Stock Exchange listing rules which also emphasise disclosure by companies). The Government also established a Companies and Securities Advisory Committee (CSAC) to monitor the implementation of the Corporations Law and to make recommendations to the Attorney General on desirable legislative change.

The Government has since launched or foreshadowed a raft of amendments and further reforms to the Corporations Law, in four

waves. Some of the amendments are procedural; others more far-reaching.

The first wave of amendments took effect in August 1991. They were intended to clamp down on the misuse of 'off balance-sheet vehicles', to require consolidation of group accounts and to strengthen insider-trading provisions.

The second wave took effect in December 1991. One of the amendments simply sought to clarify fund-raising provisions. Another introduced a standard 12 month buy-back/redemption notice period for 'public' unlisted property trusts, and provisions to facilitate investor participation in the affairs of unit-trust and collective-investments schemes.

A third wave of amendments was initially released for public comment in February 1992. The proposals, contained in the Corporate Law Reform Bill, were based on the recommendations of three reports.[1] The Bill deals with all aspects of loans to directors, transactions between related companies, the duties and responsibilities of directors, and insolvency provisions. The business community criticised the size and complexity of the draft legislation, particularly the provision to restrict loans to directors and related parties. The Attorney General set up an Advisory Committee to re-draft the Bill, especially the provisions relating to loans to directors and directors duties. The aim of the redraft is to reduce the length and complexity of the existing draft Bill and use more 'general principle' law.

In March, the CSAC (1992) released a report in response to criticism that the prospectus provisions placed onerous conditions on directors and their advisers and made it difficult to raise funds cheaply. While the CSAC recommended various modifications to the law, it endorsed the non-prescriptive nature of the prospectus provisions which had replaced the check-list style of disclosure.

The fourth wave of changes to the Corporations Law, based on an earlier report on statutory disclosure arrangements (CSAC 1991a), introduces obligations for continuous disclosure of all beneficial or adverse material matters. It will introduce

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[1] The reports are the SSCCLA (1989) report on Company Directors' Duties, the ALRC (1988) report on Insolvency, and the CSAC (1991b) report on Corporate Financial Transactions law.

mandatory half-yearly and annual reporting, and more comprehensive annual disclosure requirements. More frequent reporting will enable companies to issue abbreviated prospectuses by incorporating other documents into them. This move away from all-inclusive prospectus documents will reduce the cost of prospectuses, at the expense of higher costs for periodic reporting. The Attorney General recently indicated that the changes would be narrower in coverage than those proposed by the CSAC or by the ASC. The proposals would impose continuous disclosure obligations on companies that presently have only limited disclosure obligations. In the Commission's view, the simplest and most cost-effective reform would be to limit coverage to those entities that access the market for funds generally.

Many of these changes attempt to replace prescriptive statutory rules with performance standards, by using general legal principles. These principles are applied by the courts to individual cases and, over time, a body of law based on actual commercial behaviour of firms will be built up. This approach is preferable to the alternative of allowing the political process to anticipate and predict the likely behaviour of firms and individuals in diverse commercial circumstances.

Critics argue that this approach reduces the certainty in the law, but any problems with uncertainty can be dealt with by according 'deemed to comply' status on the prescriptive rules - thus allowing firms who prefer to adhere to the old-type rules to continue to do so with impunity. In any case, prescriptive rules create uncertainty because of the ongoing identification of 'loopholes' and subsequent amendments.

While 'general principle' law allows firms to pursue least-cost compliance, this approach to amendments to the law may not alone be sufficient to ensure that the body of corporations law in Australia is sound. Across-the-board review of the law similar to that conducted earlier this year in the third wave of amendments is required. This would need to ensure that all remaining provisions are necessary to the overall aims of corporations law discussed at the outset.

Competition policy: changes to mergers regulation

In June 1992, the Government (Duffy 1992) announced that it would accept the major recommendations of the Cooney

Committee inquiry into Mergers, Monopolies and Acquisitions regarding the mergers provisions of the Trade Practices Act. While full details are not yet available, the changes will involve amending Part IV the Trade Practices Act to:

- **prohibit mergers and acquisitions which have the effect of "substantially lessening competition" in a substantial market, rather than mergers which "create or enhance a position of dominance of a market";**
- **increase penalties for breaches of all provisions — except the 'industrial relations' provisions: sections 45D (secondary boycotts) and 45E (primary boycotts) — to $10 million for corporations and $500 000 for individuals;**
- **introduce a simple form of compulsory pre-merger notification; and**
- **make undertakings given to the Trade Practices Commission by parties under investigation enforceable.**

The Trade Practices Commission (TPC) will prepare administrative guidelines which will explain in detail how it will administer the new mergers test.

Also in accordance with Cooney recommendations, the new merger test will be accompanied by a list of statutory factors to be taken into account in determining whether a merger substantially lessens competition:

(a) the actual and potential level of import competition in the relevant market;

(b) the ease with which new participants may enter and exit the market, now or in the future (barriers to entry);

(c) the level of concentration in the relevant market;

(d) the degree of countervailing power;

(e) the ability of the merged firm to increase prices or profit margins significantly and sustainably without being inhibited by other market participants;

(f) the extent to which acceptable substitutes for the products of the merged firm are available or likely to be available;

(h) the likelihood that the merger would result in the removal of a vigorous and effective competitor;

(i) the nature and extent of vertical integration; and

(j) any other relevant factor.

These factors will assist the courts, the Trade Practices Tribunal and the TPC in assessing competition in markets and whether proposed mergers are likely to reduce community welfare. They will help ensure consistent approaches to these issues that take into account all the important aspects of competition, not only in static terms but also in the dynamic nature of competition over time.

Potential import competition and the significance of barriers to entry to the relevant market are particularly important factors in this respect, but several of the remaining factors may need to be approached carefully. Concentration ratios and profit levels in the short-to-medium term, for example, can provide ambiguous signals on the extent of competition in a market.

At present, these factors will not apply to interpretations of 'substantial lessening of competition' in relation to other provisions of the Act, and to the similar threshold competition test in the misuse of market power provision — section 46. One of the justifications for the change in the mergers test was to make the provision more consistent with other provisions of the Act. However, applying statutory factors to this provision and not to others could undermine this goal. This suggests that relevant statutory factors should be applied to all provisions of Part IV of the Act.

Competition policy: the Commonwealth-State review

Sixteen years ago the Swanson Committee (1976) expressed the view that restrictive trade practices regulation should be applied as universally as possible:

> **We believe it to be extremely important that the Trade Practices Act should start from a position of universal application to all business activity, whether public sector or private sector, corporate or otherwise.**

More recently, there have been calls to extend the range of individuals and organisations that are subject to restrictive trade practices regulation.

In response to an initiative by the then Prime Minister in March 1991, a Commonwealth-State review will examine the possible development of a national competition policy.

At present, application of the restrictive trade practices provision of the Trade Practices Act is not comprehensive because of:

- **current exemptions applying to government;**
- **government industry-specific interventions;**
- **current exemptions applying to the labour market, particularly the professions and unions; and**
- **protections provided for intellectual property.**

Various government business enterprises are exempt from restrictive trade practices legislation, particularly in markets where the government enterprise is the sole supplier. Commonly, governments in Australia have exclusively supplied markets considered, at least in part, to exhibit natural monopoly characteristics — that is, where the markets were thought to be supplied most efficiently by only one producer. Examples include electricity generation, transmission and supply; telecommunications; water; and transport infrastructure. Governments have also undertaken exclusive supply of some products primarily to further social goals. These government business enterprises are often regulated using industry-specific regulation.

However, with current moves toward the corporatisation, privatisation and/or structural separation of existing government business enterprises, there should be a stronger role for general pro-competitive regulation — such as restrictive trade practices law — compared with industry-specific regulation in these markets. Indeed, public monopolies should be the prime targets of restrictive trade practices regulation, rather than enjoy substantial immunity. The role in these markets of another arm of pro-competitive regulation in Australia — prices surveillance — should also be examined. It is therefore timely to consider the overlap and inconsistencies between these various forms of regulation for government business enterprises.

The current special treatment of the professions is also difficult to justify: there is no economic justification for a blanket exemption from the operation of trade practices law.

The application of restrictive trade practices law to intellectual property and the unions involve more difficult issues. In both cases, however, a review is warranted to assess if the balance of regulation is appropriate.

In the Commission's view, the Commonwealth-State review could usefully address all these issues. Before it considers how the operation of the restrictive trade practices provisions of the Trade Practices Act should be extended, it could first examine how pro-competitive regulation should be applied generally. This would involve considering the goals of pro-competitive regulation, and the relationship between pro-competitive regulation and other pressures in the community to increase competition and ensure competitiveness. The most important of these pressures is the gradual removal of anti-competitive regulation, such as tariffs, other industry assistance measures, and statutory barriers to entry to, for example, the aviation and banking industries. The review might also benefit from a general examination of the nature and dynamics of competition, and whether all the current provisions of Part IV of the Act are necessary to protect the competition process.

Product liability

Product liability laws specify the circumstances in which people who suffer product-related loss or injury are entitled to receive financial payment from the producers (or sellers) of the goods. They are essentially the legal means of compensating consumers for faulty products, and they affect the incentives for firms to increase the safety of their goods, and for consumers to use goods safely.

Australian laws governing product-related loss are complex and overlap. Each state has its own peculiar regime operating in parallel with Federal law. These in turn complement common law rules of tort and contract to give claimants a range of potential actions, all of which might be included in the one case.

However, gaps remain in the provision of compensation. For example, in some instances, children have experienced great difficulty attaining compensation in deserving cases.

In 1989, the Australian Law Reform Commission proposed a new scheme, which would do away with the legal concept of 'defect' or 'fault' (ALRC 1989).

Largely as a result of business opposition to the Australian Law Reform Commission (ALRC) proposals, in October 1989 the Government asked the Industries Assistance Commission (now the Industry Commission) to report on:

- **the economic effects of the ALRC's proposals, and**
- **the effects on product innovation and insurance charges.**

In its report, the Commission (IC 1990) found a number of problems with current Australian laws, but considered that the ALRC's proposals would probably worsen things overall. It recommended that the ALRC's proposals not be adopted and, instead, that less fundamental reform measures should be implemented.

In its March 1991 Economic Statement (PM&C 1991), the Government announced that it had accepted the Industry Commission's main recommendation not to implement the regime proposed by the ALRC, and would introduce a new product liability scheme based around the European Community (EC) Directive on product liability.

Unlike the EC Directive, though, the Government's regime would include a unique double reversal of legal onuses compared to the norm. Claimants would have to show that their losses did not arise solely through misuse of the product. In turn, the onus of proving whether or not a product defect caused loss would be on producers.

In November last year, the Minister for Justice and Consumer Affairs, Senator Tate announced that the Government would modify its proposals. The double reversal of onuses of proof would be replaced by evidentiary rules that more closely reflect existing common law arrangements, while still aiming to facilitate just claims in the courts. Draft legislation was tabled in Parliament in December 1991.

However, after receiving further comment on the legislation, in June 1992 the Government introduced a new bill which removed the remaining three contentious provisions.[2] First, the new legislation does not include any special 'onus of proof' provision — legal and evidentiary onuses of proof will remain in

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[2] These three provisions are, however, currently the subject of an inquiry by the Senate Standing Committee on Legal and Constitutional Affairs.

accordance with general principles of Australian law. Second, the extra-territorial impact of the draft bill has been removed. This means that overseas customers of Australian products will not be able to take action under the Australian law. Third, the draft bill's 20-year statute of repose for personal injury — the period after the sale of products within which an action must be commenced — has been reduced to 10 years. The new legislation took effect on 9 July 1992.

Anti-competitive regulation

Anti-competitive regulation controls entry to markets or governs prices or production. This form of regulation redistributes income by limiting competition but, in doing so, it can reduce national wealth. Its reform is the main priority of the Commonwealth Government's microeconomic reform program and those co-operative reforms being undertaken with the states.

As discussed extensively in this report, there has been considerable progress in recent years in the reform of anti-competitive regulation. This has included reducing tariffs, liberalising primary industry markets, and opening up transport and communication markets.

Social regulation

Social regulation, whilst not directly limiting competition, seeks to regulate the production, marketing and employment policies of firms to achieve a variety of social objectives. These may include improved health and safety, environmental or cultural goals.

In common with other developed countries, social regulation is the predominant form of new regulation in Australia. Recent empirical research in the United States has concluded that environmental, road safety, occupational health and consumer product safety controls are the classes of social regulation having greatest economic impact (Hahn and Hird 1990).

From an economic perspective, there are cogent reasons for social regulation. Unfettered market forces can in some circumstances fail to provide optimal levels of particular social goods, services or activities. For example, firms which do not pay the full costs of pollution will emit excessive amounts of waste into the

environment or undertake insufficient recycling. Social regulation can help to overcome such market failures. Hence, provided the costs of regulation do not exceed the costs associated with the original market failure, social regulation can potentially deliver benefits to the community.

However, traditional approaches to social regulation have often failed to achieve the potential benefits or, where they have, have not done so at minimum cost. Often, governments have insufficient information to develop economically efficient regulations; and the political imperative to regulate in response to short-term social crises results in overly prescriptive, stringent and costly regulation, much of which is not efficiently enforced. Where regulation is wasteful and inefficient, community welfare is reduced because society has fewer resources available to spend on other social goals.

The reform of social regulation requires a different approach to that of economic regulation. Unlike the case of anti-competitive regulations, a general deregulatory approach is not desirable. Rather, to reform the development and review of social regulations, institutions, decision-making processes and administrative practices must be created which are able both to identify real public problems and deliver efficient solutions. As far as possible, these should use methods which harness, not over-ride, market incentives.

In determining the effects of changes in social regulation, it is therefore necessary to examine the nature of such regulations and the procedures followed by institutions entrusted to develop and administer them.

Environmental regulation

The high profile of environmental issues over recent years has been reflected in an increase in the number of Environmental Protection Agencies (EPAs). Most states already have an EPA or similar body. In 1991, the Commonwealth Minister for the Environment announced the establishment of a Commonwealth EPA within the Minister's Department. In addition, a National EPA is to be established as part of the Intergovernmental Agreement on the Environment signed by the Local Government Association and Territory, State and Commonwealth governments. The Intergovernmental Agreement (HOG 1992) sets out the roles

of the parties and establishes 'ground rules' under which they will interact on the environment. The National EPA will fulfill a similar function to the one played by the Australian and New Zealand Environment Council (ANZEC). The Commonwealth EPA will provide administrative support for the National EPA.

In June 1992, the Commonwealth Government released a National Waste Minimisation and Recycling Strategy (CEPA 1992). The strategy includes an information campaign designed to encourage people and firms to reduce waste and increase recycling; a commitment to collect further and better data on waste-disposal activities in Australia; and targets for waste reduction. The strategy will be administered by the Commonwealth EPA.

Government environmental agencies released a number of draft strategies during the year for public comment. These include, in addition to the draft of the waste and recycling strategy, a draft proposal on waste lubricating oil and used tyres (ANZEC 1991), a draft biodiversity strategy (BDAC 1992), a draft strategy on greenhouse emissions (NGSC 1992) and a draft Ecologically Sustainable Development Strategy (ESDSC 1992). The Department of Administrative Services also released a strategy on environmentally friendly product buying for government departments (DAS 1992).

The two draft strategies examined by the Commission — the draft waste and recycling strategy and ANZEC's draft proposal on oil and tyres — contained a number of undesirable features, many of which breach the Government's regulation review guidelines. First, they did not specify particular objectives. Second, they contained inadequate analysis: they failed to identify market failure or to consider the costs and benefits of the regulation. Third, they recommended various forms of regulation without comparing different instruments for achieving environmental goals. Fourth, they contained a range of 'command and control' regulations such as waste bans; and arbitrary voluntary targets which, since they are accompanied by a threat of regulation if not met, qualify as *de facto* mandatory targets (IC 1991b; ORR 1991).

The Government has also introduced an 'Environmental Choice' product labeling program. It aims to encourage businesses to register their products and receive government endorsement for their environmental claims. The program's rationale is largely to

reduce misleading environmental claims made about goods. However, the cost of registration and testing and the lack of demand for government endorsement appears to have rendered the initiative ineffective. The Advertising Standards Council also recently ruled that a commercial promoting the scheme was itself likely to be misleading (Garran 1992).

Overall, the approach to environmental regulation requires modification if the community's environmental objectives are to be met at least cost.

Motor vehicle safety regulation

US research suggests that several road-safety interventions have yielded a substantial net gain to the community (Hahn and Hird 1990, p.256). For these interventions, the sum of the benefits of avoiding collisions and/or minimising their impact exceeded the total costs of collision avoidance and protection by margins larger than for other forms of social regulation (including safety regulations in other areas).

Optimising the regulation of safety enhances social welfare as it seeks the greatest benefit, a large part of which is a reduction in human loss and suffering, at least cost. Inefficient regulation detracts from this objective as it reduces the resources available to achieve other social goals. For example, if regulation requires excessive expenditure on, say, air-safety, the community will have fewer resources available to spend on more pressing safety needs, such as road safety.

The Commonwealth Government shares responsibility for road safety regulation with the states. Since 1989, it has had a monopoly over specifying vehicle safety standards through Australian Design Rules (ADRs) made under the Motor Vehicles Standards Act.

In the past, the development of such rules, while based on sound engineering practice, has relied little on formal economic analysis to determine their net worth. The rules have often been prescriptive and have differed from the standards of other markets, thus requiring importers to make special fitments or alterations to Australian vehicles and adding costs to Australian vehicle exports.

However, some recent experience demonstrates a move towards sounder regulation development processes. For example, following a detailed study, the Federal Office of Road Safety (FORS 1992) has proposed a new vehicle occupant protection ADR — covering devices such as air-bags and seat-belt pre-tensioners — based on US Federal Motor Vehicle Safety Standard 208. The study involved risk assessment, benefit-cost analysis, a move towards contingent valuation to determine consumer willingness to pay for higher levels of safety in cars, and consultation processes. It also marks a move to performance safety standards. Manufacturers are required only to show that their cars reach a certain level of safety, rather than being forced to include particular safety features in their cars. This allows producers more flexibility to meet the regulations at lower cost.

Notwithstanding this positive development, it is apparent that the Commonwealth Government also sees the motor vehicle standards as an instrument of industry policy. In the recent inquiry conducted by the Senate Standing Committee on Industry Science and Technology into the Government's decision to impose a $12 000 per unit duty on second-hand imported vehicles, the Minister for Industry, Technology and Commerce stated:

> **Anybody who comes to this inquiry and says that the issue in 1989 was purely an issue of the safety of cars can only be described as extremely naive. It was not just an issue of the safety of cars, it was the whole question of second-hand car volumes eroding the new car market (Button 1992d).**

Clearly then, the intention of the Motor Vehicle Standards Act was not only to establish regulation for safety reasons but also to protect local producers from import competition.

As the Commission has noted in other contexts, it is inefficient to use social regulation to pursue industry development objectives. In the case of motor vehicle standards, such a dual-purpose policy approach not only reduces the transparency of the cost of assistance provided to domestic automotive manufacturers, it also impairs the FORS from regulating vehicle safety on a risk-related and cost-effective basis.

New national regulatory agencies

Intergovernmental co-operation on various social and economic issues is increasing. Governments at all levels have long acknowledged the cost of market fragmentation caused by excessive duplication and overlap of regulation in a federal system. However, effective political means to deal with the problem have been established only in the last few years — the Special Premiers' Conference arrangements being the most prominent. This increased co-operation between Australian governments has resulted in the Commonwealth Government being given a greatly increased role in the regulation of firms for a wide range of social and economic purposes — a role which the Constitution and practice has largely left with the states.

This trend has seen the creation of a number of institutions charged with developing national regulatory standards and, to a lesser extent, strategies for enforcing these standards. The more important national institutions established under Commonwealth/State agreements to rationalise regulation include the National Occupational Health and Safety Commission (Worksafe Australia), the Australian Securities Commission, the National Food Authority, the Therapeutic Goods Administration in the Commonwealth Department of Health, Housing and Community Services and, as mentioned, a National Environment Protection Agency. Negotiations are proceeding with the states to establish a national Agricultural and Veterinary Chemicals Authority and an agency to regulate the release of genetically modified organisms.

These agencies have been established by either: first, a referral of power to the Commonwealth under the Constitution; second, the implementation of parallel legislation by the States and Commonwealth; or, commonly, third, the establishment of national councils who recommend implementation of parallel legislation one by one. Each involves participation by the Commonwealth and the States, with a declining level of surrender of State influence and an increasing degree of uncertainty associated with implementation. Nonetheless, in all three, the Commonwealth enjoys a prime role.

However, these developments have occurred ahead of the Commonwealth Government's adoption of comprehensive

procedures for vetting new regulatory proposals, of the type used by some states.

Centralisation of regulatory authority has a number of potential advantages. Whilst allowing individual states to opt out of particular national arrangements in unusual circumstances, it can:

- **establish clear responsibility for the regulation of a particular activity and thereby improve political accountability for results;**
- **facilitate the development of uniform regulatory standards and their national application;**
- **provide a framework for efficient enforcement — for example, by encouraging the sharing of compliance information between authorities;**
- **ease the introduction to Australia of the desirable regulations and regulatory practices of other countries; and**
- **bring a greater concentration of expertise to the technical and economic evaluation of regulatory proposals.**

However, centralisation of regulatory authority and the creation of supporting institutions does not guarantee these benefits. The Commonwealth Government has had little experience in some areas of economic activity it is now responsible for controlling, and assembling technical expertise is proving to be a difficult task for the agencies.

More importantly, where a national agency acquires an effective monopoly on regulatory power, there are increased risks that:

- **organised interest groups will be in a better position to exercise undue influence;**
- **the absence of competing regulatory agencies will reduce incentives to regulate efficiently;**
- **more directive, rather than consultative, approaches to regulation will be adopted; and**
- **comprehensive parliamentary and executive procedures for the vetting of new regulatory proposals used by some states will be avoided.**

Given these risks, it needs to be remembered that the goal of intergovernmental co-operation is not to pursue uniformity of

regulation for its own sake, but rather to widely apply regulations which deliver real community benefits at least cost.

Early experience with the performance of the national authorities is mixed. No agency undertakes and publishes adequate analysis of its proposals — indeed most agencies lack a capability to do this. The public consultation practices of the authorities are also sometimes unsatisfactory. Some agencies, notably the Australian Securities Commission, have been under pressure to produce a large amount of new regulation in a very short time, and at an early point in their life. Other agencies, such as the National Food Authority, have inherited backlogs of outstanding applications which have inhibited them from formulating their own approach, while others, such as the Therapeutic Goods Administration, have been undergoing extensive internal reorganisation.

While the new national regulatory arrangements are potentially more efficient than those they replaced, it is unclear that they have yet delivered substantial benefits to the community. There remains considerable scope for the national agencies to adopt efficient regulatory practices — such as consideration of market-based solutions, comprehensive economic analysis of proposals, adequate public consultation and adoption of transparent decision-making criteria.

There are a number of approaches to improve the regulatory practices of agencies. One is the development and adoption by all Australian governments of standardised 'sunrise' procedures for the assessment of new regulation. These would require all proponents of regulation to follow a common set of administrative procedures prior to the approval of new regulation. In this regard under the parallel legislation approach discussed above, there is a risk that 'sunrise' procedures will either be duplicated or totally avoided in the establishment of an agency or in the implementation of its recommendations. A mechanism needs to be established whereby the recommendations of national agencies are subject to a single sunrise procedure. If comprehensive Commonwealth procedures are developed (see below), these should probably be applied. Further, these agencies should to the maximum possible extent accept the regulations of comparable countries: for example, new drug approval decisions made in the USA and the European Community. The Commission will pursue

these issues with the national agencies and the states during the year.

Regulation-making processes

The processes used by governments to make and review regulations were subject to some significant reforms during the year, and the Administrative Review Council completed the first major review of Commonwealth regulation-making practices.

Mutual recognition of regulation

Most important of these reforms was the final agreement reached by the Commonwealth and the states to recognise each others' product and occupational regulations. Heads of government of the Commonwealth, States and Territories signed a final agreement at their meeting on 11 May 1992 to introduce complementary legislation to achieve a common market within Australia. On present planning, subject to the successful passage of legislation through the Commonwealth and all State parliaments, the arrangements will commence on 1 March 1993.

Mutual recognition will allow free trade between the states in locally produced and imported goods which meet agreed base-line standards, notwithstanding continuing differences between detailed state requirements. It also facilitates labour mobility by allowing free entry by practitioners of regulated occupations to the markets of all states provided tests of the equivalence of occupations are met. It puts a strong discipline on governments not to introduce impediments to inter-state trade and, consequently, is an important adjunct to the tariff reduction program.

The mutual recognition agreement provides for a review in due course of New Zealand's participation. This option is being pursued in the present round of extensions to the Closer Economic Relations agreement.

The Commission first proposed a mutual recognition policy in its 1989–90 Annual Report. Its achievement has been acknowledged as a particularly successful outcome of the 'new federalism' processes established by the Hawke Government. These processes, which centred on a series of Special Premiers'

Conferences, proved to be an effective means of progressing micro-economic reform. The future pace of reform depends on continuing intergovernmental co-operation. The new Council of Australian Governments has been established to pursue this objective.

Administrative Review Councilreport

The Administrative Review Council (ARC) completed its review of Commonwealth regulation making and presented its report to the Attorney General on 26 March 1992. It summarised its major findings as follows (ARC 1992, p.ix):

> **... the traditional form of delegated instrument has been the statutory rule, most commonly the regulations made by the Governor-General in Council for which a framework for making, publication and scrutiny has developed over time. However, in recent years there has been a vast growth in the volume and diversity of delegated legal instruments. Different and often inconsistent practices for drafting, consultation, scrutiny and publication apply. The extension of some procedures associated with statutory rules has overcome some anomalies but significant problems still remain. In particular, the framework of principles and procedures for the making of delegated legislative instruments is patchy, dated and obscure.**

The Council recommended the enactment of a new statute, to be known as the Legislative Instruments Act, to control the assessment, making and retiring of all subordinate legislation. It proposed that the new regime contain the following elements:

- **better guidance on matters appropriate for inclusion in Acts of Parliament and matters which can be included in delegated legislation;**
- **improved practices to ensure high-quality drafting for all Commonwealth rules;**
- **mandatory consultation with the community before important rules are made;**
- **'sunsetting' of all rules on a ten-year rotating basis;**
- **establishment of a Legislative Instruments Registrar in which all rules should be published (rules would not be enforceable if they were not published in this way); and**

- **special adaptation of these general procedures for rules of court and rules made under intergovernmental schemes for nationally uniform regulations.**

The ARC's proposals extend the Commonwealth guidelines for internal governmental scrutiny of new major regulatory proposals to all subordinate legislation, and they introduce standardised and enhanced public consultation processes. Importantly, the ARC recommended that, should agencies avoid the use of these processes, the regulation should be liable to disallowance by the Senate.

In the Commission's view, public justification of proposals to regulate will improve the efficiency of regulations, by requiring that the costs and benefits be identified and by reducing the opportunities for authorities to push through regulations which simply confer benefits on some sectors of the community at the expense of others.

But while the Commission supports early adoption of the ARC's recommendations, its experience suggests that the Commonwealth regulatory agencies will need to improve their expertise in economic analysis if those recommendations concerning the justification of proposals are to be met.

Integration of business licensing databases

Most States and Territories in Australia have established 'one-stop shop' Business Licensing Centres. These centres assist people getting started in business with information on the licences, permits, approvals or registration required, and by providing the necessary paperwork.

In December 1990, Commonwealth, State and Territory Ministers responsible for small business agreed to several initiatives to enhance the performance of the small business sector, including the integration of State/Territory and Commonwealth registers of business licensing and regulatory information. Commonwealth licensing information has now been integrated in the data-bases operated by the New South Wales, Victorian and Queensland governments. The enhanced systems will enable business to obtain both Commonwealth and State licensing information through a central one-stop licence shop.

In addition to improving individuals' access to licensing information, the centralised collation of licensing and regulatory information will enable governments to review and rationalise licensing requirements across jurisdictions, to avoid duplication, overlap and inconsistencies, and to enable the reform and elimination of needless requirements and regulation.

Risk assessment in regulation development and review

Many types of risk are encountered in daily life and there are pressures on governments to use regulation to moderate the consequences of adverse events on individuals and firms. For example, governments are called on to intervene in markets to cover losses from investments or to subsidise the costs of insurance against common occurrences such as the risk of illness.

Safety risk is a generic class of risk which is extensively regulated, but policy analysts are increasingly questioning the efficacy of this form of regulation. This is partly because high economic costs are involved but mostly because the record shows that it is difficult for regulatory authorities to remain remote from political concerns about particular types of dangers.

While high risk levels are undesirable, society cannot be risk-free. For example, short of banning motor vehicles, there will always be some risk and incidence of road accidents. Similarly, short of taking all therapeutic drugs off the market, there will always be some risk of people suffering injury or dying from drugs with adverse side-effects.

Further, measures to reduce risk are often costly. For example, airbags can reduce the risk of injury to those motor vehicle occupants involved in road accidents, but can cost around $500 each to purchase. Overly stringent drug testing procedures are costly not only in financial terms but also because they can stall the introduction of safe (even life-saving) drugs to the market.

Traditional approaches to regulation development often fail to strike an appropriate balance between risk-reduction and costs, for five main reasons. First, regulatory agencies often lack proper procedures for evaluating different policy proposals, and often fail to apply procedures consistently. Second, regulatory agencies sometimes lack transparency in their decision making. Because agencies often produce their own data on costs and benefits, there

is the risk of bias in the selection process such that data will be chosen to exaggerate the importance of the agency's jurisdiction or to overstate the effectiveness of its actions (Morrall 1986). Third, regulatory agencies face incentives to 'err on the side of caution'. For example, an agency that approves a drug which turns out to have adverse side-effects may face political retribution or loss of prestige, whereas one that keeps a life-saving drug from the market is less likely to be criticised. Given this 'fear of regret', agencies tend to be overly cautious in estimating risk levels. Where cautious assumptions are compounded, the level of risk being addressed can be seriously overstated (Nichols and Zekhauser 1986). Fourth, this cautiousness may be exacerbated by pressure from incumbent firms to keep new competing products from the market. Fifth, technical specialists are often required to make not only technical judgments about the actual level of risk but also value judgments about what constitutes an acceptable level of risk, when the latter should be determined by policy makers (Refshauge 1982; Kjellstrom 1983).

These problems can all lead to overly stringent regulations which impose greater costs on the community than the benefits they confer by reducing risk levels. For example, estimates from the US show that the cost per life saved (in 1984 $US) ranges from $100 000 for steering column protection regulations to $72 billion for formaldehyde emissions regulation (Morrall 1986). This implies that, if the latter regulation were removed, the United States could afford to save more lives in other areas. Similarly, a study of mandatory swimming pool fence legislation in Western Australia found that the legislation would cost between $1.8 million and $3.2 million per young life saved: this is approximately equal to the cost of buying 200 to 300 humidicribs for public hospitals. Looked at another way, the regulation costs between $40 000 to $70 000 per year of life saved, which is far higher than the cost per year of life saved of any screening or health promotion measure (Harris, Warchivker and de Klerk 1992). Because of the trade-offs involved in pursuing health and safety goals, regulations and programs should be carefully analysed and, where necessary, rationalised.

In May 1992, the NSW Economic and Regulatory Efficiency Unit — the ORR's NSW counterpart — released guidelines for dealing

with risk management in regulation development and review (EREU 1992). The guidelines set out:

- **the nature of the risk-management problem in regulation;**
- **actual and perceived levels of risk;**
- **socially acceptable and unacceptable levels of risk; and**
- **procedures for incorporating risk assessment into cost-benefit and cost-effectiveness analysis.**

If adopted by government, the guidelines will provide a rational, data-based, analytical process to evaluate whether regulatory proposals involving risk will confer the greatest overall benefit to the community.

The Commission sees the adoption and implementation of such proposals as a desirable adjunct to regulation development and review activities. Again, however, it is cautious about the capacity of current regulatory agencies to undertake such procedures and notes that, at the Commonwealth level, successful implementation would require that personnel in the agencies receive appropriate training in evaluation techniques.