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"SMART REGULATION": HOW TO FIND THE RIGHT BALANCE

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Abstract

In the article issues of regulating economic activity are analysed. Concrete examples are provided to show ways and methods of achieving high-quality regulation, of an effective application of legal and regulatory acts. The author invites to a discussion about problems in the field of regulatory administration in the different countries and about possible ways of their solving.

Keywords: state regulation of economic activity, good regulatory practices, quality and efficiency of regulatory acts, regulatory impact assessment.

Introduction

Globalization and integration of countries into the global economy attracts attention to the issue of governmental regulating of economic activities in a broad sense (legal, administrative, technical, etc.) as it becomes important not only for the government and for the society, but, at the end, also for the country's competitiveness on the international market and essentially becomes a factor that promotes or hinders the development of a country.

Regulation exists everywhere and in various, often disguised forms - be it a tax or a customs declaration, product standards, legal requirements for mandatory liability insurance of car owners, etc.

It is indisputable that the purpose of governmental regulating is legitimate and it focuses on the interests of the society in order to protect the consumer, to collect taxes, have statistical data for informed decision-making, etc.

However, we tend to forget that every element of regulation also has its price, it costs money, and it is ultimately paid by the consumer. Regulations also directly influence companies. A closer look reveals a direct link between business and regulation: the more complex, non-transparent and expensive are the rules set by the state, the less the interest of entrepreneurs - both domestic and foreign - to start a new business, and thus it hinders the economic activity, which is finally reflected in the level of employment in a country.

A recent study (2013), prepared by the World Bank for the Economic Forum in Davos, provides an example of calculating the efficiency of a production facility in Mexico

compared with the United States in Mexico: wages are one third of the U.S. level, capital costs are 10% less, but given the lower productivity of labour in Mexico and various administrative and transportation costs, half of the price savings disappears , which shows the importance of considering and comparing the full range of factors, including invisible barriers[1].

The above-mentioned study claims that improvements in the area of border administration, transport and telecommunications infrastructure, could increase global GDP by 5%, and world trade – by 15%. For comparison, the complete elimination of tariffs in the world would allow for GDP growth by 0.7% and trade by 10%. Here it is - the price of administrative barriers.

In recent years, a growing number of Western countries call for the need of revising the regulatory role of the state as a whole: on the one hand, to reduce the level of state intervention in the sectors which can do without it, and to improve the quality of regulation, where warranted, on the other. We are not talking about the complete elimination of regulation: even the most ardent supporters of "free market" understands the danger of a possible chaos .

Governments debate ways of how to identify and eliminate unnecessary, superfluous, "excessive" regulation and, at the same time, to improve the quality of remaining controls. Such debate on so-called "good regulatory practices" takes place at different fora, including at WTO[2].

The essence of the regulatory reform in different countries is reflected in the slogans under which it is being implemented:

In the European Union - "less red tape = more growth";

In Canada - "smart regulation";

In Australia – "the minimum effective regulation";

Japan - "freedom in principle, regulation as an exception";

In the Netherlands - "competition, deregulation, and regulatory quality";

UK succinctly calls to regulate "fewer, better, simpler,"

and the U.S. claims that "the American people deserve a regulatory system that works for them, not against them."

The list of examples could be continued but it is clear that this is not a fashion, but a long-term trend, based on emerging urgent needs.

The degree of "over-regulation" varies both between countries and within them (for example, Russian and foreign entrepreneurs note that requirements for business seriously differ by regions and cities in Russia). According to a study of the World Bank "Doing Business" (2013, covered 185 countries) Russia occupies 112 place in this ranking (Belarus - 58th, Kazakhstan – 49 th, Ukraine - 137 place)[3]. In its previous similar study the World Bank noted that out of the 10 surveyed regions in Russia the best environment for business was in Kazan, Tver, Petrozavodsk and Moscow (the capital) was the last on this list (!).

[1] Enabling Trade. Valuing growth opportunities, World Economic Forum, 2013
[2] See, for example, WTO Committee on Technical Barrier to Trade, G/TBT/1/Rev.10, 9 June 2011
[3] Business 2013.Smarter Regulations for Small and Medium-Size Enterprises, World Bank, 2012

Another major factor is the "price" (depending on the size of a company) of complying with regulations. Thus, the price of "paper work" in terms of the cost per employee per year can be 5 times more expensive for smaller companies.

Easing the regulatory burden of the "paper work" can be a direct material benefit (one can say - a subsidy to business), especially to small enterprises, in particular taking into consideration that it costs nothing (neither to the government nor to the society).

It is hard to imagine the amount of a paperwork required by legislative and state regulatory acts, which set rules and requirements for production, business and trade. Government themselves admit that to some extent they lost control over such regulatory acts and about how they are interlinked. This is not surprising, as in the U.S., for example, since the early 80's more than 114,000 regulations were adopted only at the federal level. In the European Union, legislation on the "single market" contains more than 100,000 pages. Governments understand this problem and the European Union set the target to reduce the number of mandatory laws and regulations by 1/4[4].

Businesses, especially small businesses, find difficult to understand and to link various acts. In addition, to comply with the rules business is obliged to submit a big amount of information (often, similar) to different government agencies.

Eliminate this duplication (for example, through the so-called "single window " mechanism where the public authority to which the company has filed the required information, shares it with other authorities) - is the first step that could help in the reduction of "red tape", as discussed above, and to increase the financial benefits.

If it were only about the willingness or unwillingness of States "to face the problem," "to take actions on the pressing issues" and "to make an effort" to elaborate regulatory mechanism so it works securely, easily and without delay, then the purpose of improving regulations could have been easily solved in the diplomatic sphere.

In practice, government regulation meets with a whole set of problems that require serious analysis, namely:

1. Lack of coordination

The first group of problems may be classified as "lack of coordination". Ministries often make decisions without consulting each other, and, as the result, regulatory acts that reflect these decisions are not related to each other. Not to mention the extent to which the state can monitor their implementation, these "discrepancies" confuse everyone. What the government really wants? A question that often leads to the confusion of business.

The situation is aggravated by a different understanding of the role of a regulation in a society in various Western countries, which often leads to certain distortions (for example, when the political power switches to another party which relies heavily on regulation). In these cases there is a difference in the "relative importance" of each act, so the problem has also a "theoretical" aspect.

2. "Sectoralism"

The second group of problems concerns the concept of a narrow "departmental" approach and a short-term nature of a problem and, ultimately it confronting the interests

[4] EC press release IP/07/77 of 24/01/2007

of the society. It's about elaborating instruments for short-term solutions of sectoral objectives, without considering long-term effects and without a complete vision of potential consequences. Constraints of the suggested solution “do not fit” to the problem, and, even if it is incorporated, on the contrary, it leads to appearance of even greater number of issues which need to be regulated.

3. “Life cycle” of a regulation

Another set of issues relates to the quality characteristics of a regulation and can be called its “life cycle” Even the best regulations which are “good” today, due to a changing environment might become obsolete tomorrow. Thus, a mechanism is required to review the existing acts and to do it quickly as need requires. At this moment the majority of the enacted regulations are “immortal” and very often - outdated. They block the way to the new approaches, not allow even considering the possibility of more modern solutions or of other technologies based on the development of science and technology, do not account for new social demands and requirements (which finally may be the most important issue).

Often, state agencies are not responsible for the control of their undertaken measures. The “immortals” acts continue to exist, and new regulations “sectoral” and “not linked” are added to them. Moreover, the lack of transparency enables public authorities to continue to operate in the abstract environment without reporting back, and as the result nobody knows the real cost of a regulation itself and of its costs for business and society at large. As it were assumed (behind the scenes) that the cost of implementing all the acts (far-fetched and indeed necessary) will be taken on by a private business, not by a specific user, which happens in reality. It must also be admitted with regret that government decisions are often made in the specific interests of a certain group of persons, but the “closeness” of government agencies in this field has become so typical, that it rarely becomes known to public and to law enforcement authorities.

4. Quality of preparing regulations

Now a few words shall be said about the quality of regulations. Public authorities in their decisions usually rely on detailed prescribed procedures and not on market forms of control. What does this mean in practice? Poor quality of regulations which often have more symbolic than an effective value.

Preparing them and “reporting” on the action taken, the authorities consider their job done as they have no understanding of what has happened with the implemented regulations.

As an example, one might recall the anti-alcohol campaign of the Soviet President Gorbachev which resulted in the increase of “moon shine” liquor production, fall in official alcohol sales and in governmental receipts and finally in liberalizing sales again. As a continuation of the theme - increase (several years ago) in Russia, of the price of ethanol in order to prevent its use in the production of counterfeit vodka. Sales of sub-standard vodka continued, but as a result of such not properly considered management decision ethanol in many chemical products was replaced with cheap and toxic carcinogenic additives. Secondary effects of such regulation are still difficult to assess adequately.

We should not think that everything in Russia and other countries in transition is going wrong and in the West - well. The problems are the same, but Western experts have a long experience in the approach to quality regulation and have developed a series of requirements for it. ***First***, the emphasis is not on an automatic response to a problem (there is a problem – now there is a new law), not to “fight back” but a serious analysis of your every situation to decide if it is necessary for the government to step in, or the problem will be solved by the market forces.

Second, the benchmark for a quality control is that established measures and control procedures can not be considered satisfactory unless they bring the desired solution.

The principle of using already existing measures shall not work, if it can not ensure enough flexible and dynamic approach. The goal should justify the suggested means; this is the basis for the decision and the purpose is to obtain actual, verifiable results.

Ideally, the legal and regulatory acts should not be based on the opinions and solutions invented by the state authorities and / or to reflect the interests of certain groups in business or public administration (in reality, such influence can not be ignored).

The third component in addressing the quality issue, from the point of experts, is the need for the participation of the market in regulatory acts. Not the imposition of the decisions made by the state from top to down, but cooperation with the business should be its foundation.

In addition, legal and regulatory acts must be balanced and integrated into the overall scheme of the legal framework of a state. Moreover, this balance should be evaluated not only by weight and volume, but also by its performance in relation to possible expenditure.

OECD (Organization for Economic Cooperation and Development) has developed a check list of issues for government agencies to allow them to detect problems in the area of regulatory administration in the country, and to identify and apply best international practices in this area[5].

This checklist allows to see if the government action is justified and proportionate to risks, if benefits of regulation justify the cost, how views of interested parties will be taken into account, how compliance will be achieved, etc.

Strictly speaking, this approach can be used to improve any regulations and to assess their quality on the basis of a phased analysis of a problem.

The first phase/step is to define the problem and to identify the largest number of possible solutions. Important also is to take into account risk levels of the required solutions, which are certainly different for various sectors, groups, businesses (depending on size), and to select the period of time during which the regulatory influence will be assessed.

The assessment of these risks is to be taken into account, ideally in advance, to understand the implications of the decisions / acts of the public authorities. It is evident that the concept of risk may differ from the real danger to the lives of people to, say, the potential for an abuse in a particular area.

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[5] See OECD Guiding Principles for Regulatory Quality and Performance, OECD, 2005 decision.

But more important is to identify what are the consequences of "no decision" (i.e. government does nothing). It is possible that in such case the costs will be disproportionate to the expected benefits.

The next question is what level of risk should form the basis for a regulatory

A typical dilemma: how deep to lay water pipes, when forty-degree frosts occur once in 30-40 years. If there is no frost, you can save a lot of money, but if the frost hits tomorrow, all the pipes burst and the bill to the country will be enormous.

Consequently, if a problem is identified, the main issue is to agree on the threshold that is the one that we would like and we can really achieve. And, finally, the problem of formulating the regulatory act itself.

The second stage - an analysis of the complex of the consequences of the identified possible solutions. What impact they will have on the economy can be found only through careful consultations with the affected sectors. On the basis of these consultations, the right approach shall be singled out and it serves as an additional check: if it the approach is correct, whether the problem is rightly outlined, how deep it should be studied in depth.

The final decision comes in the form of a legislative act, is, therefore, made at the last stage through selection and comparison of different approaches to solving the problem, their cost, options of their acceptance by the interested stakeholders.

This work is difficult and cumbersome, but, apparently, and from the experience, for example, of the EU, the more carefully it is done, the better, simpler and more efficient its results.

Another way to test and to check how clearly a future regulatory act solves the problem is through the assessment of its impact, not only on an individual problem, but also on other related sectors. For example, what is the place of a new regulation in the economy; how the act affects competition on the domestic and international markets, trade, investment flows, the cost of doing business, its administrative costs, innovation and research, what would be the impact on the consumer, on the specific regions, sectors, third countries and international relations with them, and, finally, on the macroeconomic environment as a whole.

Here is an example of everyday dilemmas faced by regulators. Suppose a municipality discusses the question of disposing of garbage through dumping or incineration. Burning pollutes the air and landfilling - soil and water. Of the two evils, the public authority must choose the lesser, and a balanced decision is required. In practice, as a rule, it is impossible to find a solution without any negative impact. For example, looking into the EU experiences, it can be recommended, on the one side, to take into account all existing factors, and on the other, to base a regulatory decision on the principle of "lesser evil." In other words, do not try to create a perfect act of the legislative power, but to ensure the least damage to the economy when the regulation is necessary and to reduce its potential negative side effects. Because the final aim is to find a solution acceptable to everyone and with the least painful effects.

With this approach, it is now time to decide on how one can evaluate the effectiveness of a regulation. In the field of technical regulations such instrument exists and it is calculated on the basis of the possibility to save "statistical" human lives (how many can be saved, what are the costs per "statistical" life saved, based on the cost of

implementing this regulation), that is, how many lives could be saved by implementing it. It is a paradox but , in some sectors, the use of regulatory methods will save more "statistical" lives, thus allowing for more "efficient" regulations than in others.

To compare seriously such claims is a difficult and complicated process which is not always easy, as there are visible and invisible benefits.

Thus, the officials usually claim that the adoption of legal and administrative provisions costs nothing to the society, and that they are imposed in the interests of the society. In fact, any regulation has an implementation cost and it is included into the price of the goods (or imposed indirectly - through taxes, services, etc.), that is to say, the consumer pays for everything.

Not to mention the fact that state agencies often ignore (forget), for example, about the costs of bringing the existing legislation into conformity with the new act, and about the cost of controls over its execution (and if no control, why adopt it?). Therefore, as stated above, it is necessary to tailor the costs (all direct and indirect, tangible and otherwise) to the expected benefits, which may be material in nature or not (for example, increased confidence in the authorities).

Business participation in the discussion of future legislation allows, according to Western experts, to improve the quality of the proposed measures and enhance their future performance and regulatory discipline. This is due to the fact that it is possible to identify in advance the possible pitfalls and to find the best solution (and not solve them in haste, after the new act comes into force). And, thus, companies have a better understanding of why the government had to resort to new regulatory measures.

Such cooperation foresees not simply informing the business after the introduction of a regulatory measure, but allowing for a real participation in the discussion of draft laws with the aim, if possible, to take into account views of the companies (subject to the respect of public interests). In any case, at the end the final decision is made by an authorized government agency, which is fully responsible for all the consequences of a new regulation.

In the West, the consolidated position of the business is often generated in different associations and federations of companies. In many cases, such associations have essential regulatory functions in some sectors, for example, in many countries standards setting bodies are funded by business which actively participates in such activities together with governmental experts.

Business pays for the implementation of legal acts, and what is the role of the public authorities? A very important role, as the lives of people are often in their hands. Such decisions are not easy, especially when the expected consequences affect a number of sectors. Restrictions on the use of asbestos, for example, according to calculations of the U.S. authorities, allow to save thousands of lives a year. At the same time, the use of asbestos in brake pads for automobiles increases their efficiency by 2%, which means shorter stopping distances in an emergency, especially for heavy trucks. Thus, the restriction of the use of asbestos or the use of non-asbestos brake pads will lead to a greater number of accidents (to a greater number of deaths on the roads). It means that the authority must decide what is more important: to save the lives of the workers working in the asbestos industry, or to save the lives of people who will be sitting in a truck or in a car

during the accident because its brake shoes are less effective (as asbestos was not used). Public authority which is making a decision is responsibility for the consequences of its decision. It is important to determine what level of risk may be considered "acceptable", and what is the price society is willing to pay for it.

Does the technological progress help us in this respect? Yes and no. At present, for example, seat belts in the car (and for many models, and air cushions) became a mandatory standard set. But 20 years ago it was a luxury. It means that today society is concerned about the safety and death or injury of its "unfastened" citizens, which was not the case before. That is to say that the level of "acceptable" risk has increased and it is directly related to economic and social development level.

There are, unfortunately, the opposite examples. For example, a game dependency on computers. So, shall we ban computers? Find the optimal regulatory decision in this case is almost impossible. As a result, the Western countries find it necessary to use the so-called method of "regulatory impact assessment"[6].

The approach is the following: it is desirable to have an "X-ray" of a legislation (using as a yardstick the above-mentioned principles of "good regulation"), but the governments understand that it is expensive and make sure this procedure is used only for the most important pieces of legislation.

As an example, we look into how a "legislation X-ray" is applied in Ireland and in the United States. Criteria of importance in Ireland has two aspects: cost and scope. Cost: the high price of the initial implementation of 10 million euros or more or the total cost of € 50 million over 10 years (including all costs and expenses of government, business, consumers). Scope: regulatory act can be particularly important if its cost is unproportionately high for one sector (groups), or in case of an important impact on the economy, environment and social programmes.

In the U.S., the principles are similar, but the primary cost ceiling raised to $ 100 million a year. Based on these approaches, of the 4,500 federal regulatory acts adopted in the United States on average each year, about 500 are considered "important" and 70 "economically important", i.e. they are required to undertake "X-ray" and lawmakers will not even consider such acts, if they are not accompanied by an assessment of the regulatory impact.

Summary and concluding remarks

So, caution, prudence, transparency, alignment with good regulatory practices, and most important, the principle of "do no harm" ("lesser evil") ─ these are the principles which, after serious consultation and verification at a national level shall serve as the basis for the development of legal and administrative acts and procedures. There is already extensive experience available on these issues (be it customs administration, trade facilitation or technical regulations). Implementation of such good regulatory approaches will allow to find a reasonable balance between legitimate governmental regulatory requirements and the need for improving trade and business environment with a view to enhance the economic development of countries.

[6] See Regulatory Impact Analysis: a tool for policy coherence, OECD, 2009

Endnotes

1. Enabling Trade. Valuing growth opportunities, World Economic Forum, 2013
2. WTO Committee on Technical Barrier to Trade, G/TBT/1/Rev.10, 9 June 2011
3. Doing Business 2013.Smarter Regulations for Small and Medium-Size Enterprises, World Bank, 2012
4. EC press release IP/07/77 of 24/01/2007
5. OECD Guiding Principles for Regulatory Quality and Performance, OECD, 2005
6. Regulatory Impact Analysis: a tool for policy coherence, OECD, 2009

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FACILITATION AND SECURITY OF INTERNATIONAL TRADE: INNOVATIVE MECHANISMS AND INSTRUMENTS

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Abstract

This paper is a result of the collaborative study of experts from 11 countries. It is based on the materials of the training workshop, which was held by the UNECE in Turin, Italy on the theme "Trade Facilitation Implementation Guide ─ Capacity Building Phase" in the period of 12 ─ 14.02.2013. A group of authors provides an analytical review of the reforms carried out in 11 countries in order to facilitate international trade. The following data are presented by categories: regulatory reforms aimed at achieving clarity, concision and transparency of the legal framework, institutional development, business – sector consultation, inter-agency cooperation, modernization of infrastructure of electronic data processing and changes in trade processes and procedures.