

International Studies in Entrepreneurship

André Nijsen
John Hudson
Christoph Müller
Kees van Paridon
Roy Thurik
Editors

Business Regulation and Public Policy

The Costs and Benefits
of Compliance



Springer

Business Regulation and Public Policy

INTERNATIONAL STUDIES IN ENTREPRENEURSHIP

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Business Regulation and Public Policy: The Costs and Benefits of Compliance

André Nijsen • John Hudson • Christoph
Müller • Kees van Paridon • Roy Thurik
Editors

Business Regulation and Public Policy

The Costs and Benefits of Compliance

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Introduction: The World of Regulation and Compliance

André Nijsen, John Hudson, Kees van Paridon, Christoph Müller,
and Roy Thurik

Abstract This book tries to answer the most relevant questions about how to tailor regulations in such a way that businesses are able and willing to comply with government regulations. It brings together a number of diverse contributions from leading experts in their related fields. The book is written to mark the retirement of André Nijsen in February 2008.

It explains how the authors were getting fascinated by the issue of business effects of regulations. For years, businesses are complaining about regulations and compliance costs. On the other hand, society is becoming aware of more and more risks for the well being of people, nature and planet. Regulating seems to be one of the answers to safeguard against these risks. How can we deregulate and regulate at the same time, without bargaining our public goals and acting as a brake on economic growth? That is the key question to be answered in this book.

One of the basic conditions for such a policy is the availability of clear concepts and unquestionable information about compliance effects. The question is which perspective do we need to create transparency about business effects of regulation? Do we need the classic business perspective or could a public policy perspective be more useful to take away or avoid unnecessary compliance costs? The business perspective appears to be important as a starting point but to improve the quality of regulation we need to change this perspective into a public policy one. One of the strongest arguments to favor a policy to reduce compliance costs is that compliance costs are regressive in nature. They are especially burdensome for the small businesses.

1 Introduction

The concept of compliance costs, part of which is the administrative burden, can be traced back at least as far as Adam Smith (Smith 1966). In recent years, it has become increasingly important and increasingly ‘in fashion’. This recent rise in interest, both academic and political, is due in no small part to the enduring contributions of André Nijsen to this policy domain. In fact, with

his SCM-model he has been the principal architect of this development. Together with the work done in the Netherlands, not of course unlinked to André Nijsen and the SCM model, this has provided information on the extent of ‘the problem’ and also a demonstration of what is practicable to achieve in terms of tackling that problem. In doing so, it has set an example which other EU member states and countries across the globe are following. This is André Nijsen’s true legacy.

This book tries to answer the most relevant questions about how to tailor regulations in such a way that businesses are able and willing to comply with government regulations. It brings together a number of diverse contributions from leading experts in their related fields. It is written to mark the retirement of Andre Nijsen in February 2008 whose pioneering work in developing the Standard Cost Model in the Netherlands has played such a crucial part in the revolution in attitudes and approach which is currently underway in Europe and also the rest of the World. André Nijsen’s first pioneer steps on the road to the development of SCM – at that time named *Mistral*® – were taken in 1991. The crowning glory was his PhD in January 2003, of which *Mistral*® was a substantial part (Nijsen, 2003).

Getting fascinated by a subject like business effect of regulations seems to be a contradiction in terms. Nevertheless it is what happened to all the authors of this book. The fascinating thing is not business effects as such, but the whole field of influence of which business effects are parts of. Business effects are one of the exponents of the way government is dealing with society. The simple fact that government interferes with daily business routines is a nuisance to many entrepreneurs, but the manner in which the governments are doing this makes it even worse. Until recent times, governments were hardly aware of these types of nuisances. As a consequence, the quality of many regulations and the level of compliance are suboptimal. In the end, this has a negative effect on the realization of the public goals.

Getting involved with the subject business effects of regulations implies getting in touch with many ministries, many enforcing governmental institutions, and different types of enterprises. Then, it appears, there are a lot of conflicting interests in dealing with business effects of regulations. How to deal with these conflicts of interests by optimizing benefits for society and costs for businesses is the major subject of this book.

This chapter is structured as follows: In the next section, we will present the problem description while in the following section it will be shown that business effects are two sides of a coin. We will continue in the next section with discussing what the problem with compliance costs is. The chapter will be continued with a presentation of some anticipating thoughts about what is at stake in the World of Regulation and Compliance. The central issues are ‘Better regulation as a learning curve’ and the highlighting of possible developments which may facilitate the reduction of unnecessary compliance costs. Finally, in the concluding section, the structure of the book will be presented.

2 Problem Description

For years, businesses have been complaining about regulations and compliance costs (Grilo and Irigoyen, 2006 and Grilo and Thurik, 2008). Deregulation seems to be the most appropriate reaction to that. But at the same time, society is becoming more and more aware of increasing risks for the well being of people, nature and the planet. Regulating seems to be one of the answers to safeguard against these risks. How can we deregulate and regulate at the same time, without bargaining away our public goals and acting as a brake on economic growth? (Capelleras, Mole, Greene and Storey, 2007).

The simple fact that businesses are complaining about regulations is not a sufficient argument to skip regulation, because of the necessity to safeguard the related public goals. That is why many regulations, and this holds true especially for regulations stemming from public administration law, definitely are after forcing businesses to behave in a less rational way from the business economic perspective, at least in the short term. Dumping garbage in the canal is generally much cheaper for the firm than the processing of waste in a correct manner. Nevertheless, there is enough evidence that most entrepreneurs are willing to produce in an environmentally friendly way and under safe working conditions. That is why much attention is needed from the side of the policy makers and law makers to avoid or to take away unnecessary compliance costs to businesses. Unnecessary or avoidable compliance costs mostly originate from a lack of tailoring in the policy making or the law making process. Such a lack of tailoring leads to low quality laws from the perspective of those who have to comply with these laws, the norm addressees or the business sector.

Nowadays, many instruments are available to assess the effects of laws. The so-called regulatory impact assessment (RIAs) is a well known example and applied mostly in case of new or planned regulation. The RIA system is flexible and contains a set of different instruments like cost/benefit analysis, cost-effectiveness analysis, risk analysis and cost assessments. Each of those instruments have their own strengths and weaknesses. However, most of these instruments have in common their focus on the public goals to be achieved, and not on those who are being addressed by the laws, the addressees. In this context, the businesses are the addressees. The position that we want to put forward is, that public goals will be achieved better if compliance costs of the addressees, the businesses, are as low as possible. Our argument is that businesses will comply more and in a better way in case of low(er) compliance costs. After all, complying with legal obligations in a satisfactory way is the first and most necessary step to reach the related public goals. The avoidance of unnecessary compliance costs implies a win-win situation for all involved parties, the business sector, and government and, as a consequence, the society as a whole.

Most regulations are focusing on businesses and to a lesser degree on civilians. Regulating is regulating businesses (Cranston, 1979: pp. 1–4).

Therefore, there is the need for a stronger position of a special kind of RIA, the so-called business impact assessment (BIA). The argument is not that the classic type of RIA, being cost/benefit analysis, should be replaced by the BIA. But the argument is that regulating businesses should start with a BIA to assure that businesses that are willing to comply also are in the position to comply. In the end, compliance is a function of the preparedness and the ability to comply. If government is striving in a systematic way to improve the ability of businesses to comply by avoiding unnecessary compliance costs, the preparedness of businesses to comply will increase. That is what we have called a win-win situation for all involved parties, including society as a whole.

3 Business Effects: Two Sides of a Coin

Effective debates about compliance effects require high awareness about the two sides of the coin that exist. On the one hand, there is the business side and, on the other hand, the government side.

From the perspective of the business side, the process of complying is different for nascent versus established businesses (van Stel, Storey and Thurik, 2007); also the priorities of young versus established businesses are different (Grilo and Thurik, 2008), while new businesses are concerned about raising capital and establishing a position in the marketplace, established businesses are focused on maximizing profits and maintaining or increasing market share and their relationships with government will be different. For this reason, this book will provide some commentary on the particular opportunities and challenges that entrepreneurial businesses face and how they can most effectively navigate these.

From the perspective of government – policymakers, lawmakers and inspectors – it is important to illustrate how governments can be responsive in order to promote business creation and stimulate economic growth by making high quality business regulation (Audretsch, Grilo and Thurik, 2007). This implies a deep knowledge of the relevant characteristics of businesses in different sectors, size, classes, and life cycles. Our argument is, if governments want to regulate businesses in an effective way – and that's what governments need to do in order to guarantee public goals – legal obligations will have to be tailored to the relevant characteristics of the business sectors.

For that reason, we will in part focus on the determinants of business effects which can be influenced by government – policy makers, law makers and inspectors – rather than on the determinants which can be influenced by the entrepreneurs themselves. This implies that we assume, competition will force businesses to comply in a cost effective or efficient way. It will be demonstrated that this major assumption has consequences for definitions and methodology.

4 What's the Problem with Compliance Costs?

There are many reasons to discuss the issue of compliance costs (Nijssen 2003), viz.:

- Compliance costs are hidden costs.
- Unnecessary compliance costs are a brake on economic growth.
- Compliance costs are regressive in nature: the burden is relatively most heavy for small businesses.
- Strong political field of influence.
- Confusion of perspectives.

4.1 *Hidden Costs*

Apart from the direct financial costs like taxes, premiums etc., the compliance costs incurred by businesses (and citizens) are, in fact, hidden costs. No explicit account of information compliance costs (administrative burden) and substantive compliance costs can be found in any administration kept by businesses. Even more serious is the fact that the compliance costs for businesses are not included when compiling the National Budget.

Officials who are responsible for designing new legislations and regulations are generally badly informed about the “off budget” effects of regulations. Apart from taxes, premiums etc. again, estimates of costs and benefits of legislations and regulations are limited to the consequences for the National Budget (“on budget” effects) usually. In this respect, Van der Bij refers to internal and external regulation costs (Van der Bij, 1994, pp. 227 ff). Regulation costs, which are included in the National Budget, are termed internal regulation costs, the remaining regulation costs, which remain outside the budget,¹ are termed external regulation costs. Consequently, when estimating the budget, calculations are usually based on considerably low budgetary price and thereby little incentive for reduction of costs of regulation is left.

Nowadays, this problem is internationally recognized. The perceived intrusiveness of government regulation in many OECD countries could be detected only through anecdotal information, partial indicators and general impressions. Systematic efforts to track and account for regulatory effects are uncommon despite recognition that the scope of regulation is broad indeed.” (Hopkins, 1997, p. 274).

¹ Van der Bij gives the example of what he terms external regulation costs, those connected with pay roll tax administration and compiling annual tax report.

4.2 Compliance Costs Are Regressive in Nature

Compliance costs place a relatively heavy burden on medium and small sized businesses. For this reason, policies are being developed, both nationally and internationally, to aim at eliminating or preventing unnecessary compliance costs – in particular for small and medium sized businesses (OECD, 1997; EIM/ENSR, 1995). Sandford argues that tax compliance costs have undesirable distributional effects. They are capricious in their incidence, regressive and fall with disproportionate severity on small firms in particular. Moreover, small firms suffer from a disadvantaged position being created by the state. Additionally, tax compliance costs fall much more heavily on the self-employed than on employees (Sandford, 1995, p. 95). Table 1 presents the disadvantaged position of small firms.

From Table 1 it appears that administrative burdens of small firms (1–9 workers) are 9.5% of value added, and only 1.1% for businesses with 100 or more workers. The main reasons for this regressiveness are administrative burden being fixed cost mainly and the low value added of small firms. Small Dutch firms (1–9 workers) create about 20% of the total value added, but incur almost 70% of the total administrative burden. The comparable figures for businesses with 100 and more workers are respectively 50% of the total value added and only about 16% of all the administrative burdens (Boog, Jansen and Tom, 2002).

To understand the problems of starting businesses and what happens thereafter, Table 2 presents some figures.

Table 1 Administrative burden as a percentage of value added for the Dutch private sector, according firm size; 2000

Industry	1–9 workers	10–99 workers	100 and more workers	total
	percentages			
Agriculture, hunting, forestry, fishing	9.0	0.7	0.5	7.2
Mining	1.1	0.1	0.0	0.1
Manufacturing	8.3	2.6	1.1	2.2
Public utilities	9.0	0.9	0.4	0.5
Building	9.6	2.7	1.5	4.0
Trade and reparation and trade	10.5	2.2	1.6	4.4
Hotel and catering industry	11.2	4.5	2.1	7.0
Transport, storage and communication	7.1	2.1	0.9	1.9
Financial sector	6.2	1.6	0.6	1.3
Business-to-business services	10.3	0.8	1.4	2.7
Health care and welfare	9.0	2.1	1.5	3.0
Culture, sport, broadcasting	13.6	2.0	1.1	6.9
Total	9.5	1.8	1.1	3.0

Source: Boog, Jansen and Tom, 2002

Table 2 Administrative burdens in euros according to life event for a sandwich bar and a painting business: The Netherlands 2007

Life event	Sandwich bar: One-off costs	Sandwich bar: Structural costs	Painting business: One-off costs	Painting business: Structural costs
Start business	241	1,898	146	1,553
Hiring first employee	830	486	742	486
Hiring 4 additional employees	480	140	480	140
From one-man business to a private limited company	788	4,514	781	4,514
Total life events all in one year	2,339	7,038	2,149	6,693
Additional, when starting from a benefit situation	216	0	216	0

Source: Tom, Suyver, and Boog, 2007

The situation for these two cases was even worse in 1998. From 1998–2007, the one-off cost went down by about 24–27% and the structural costs with 8–9% as a consequence of reduction policy (Tom et al., 2007). Too high an administrative burden for starting a business and hiring the first employee might have a negative effect on the total number of starters and employment.

The Global Entrepreneurship Monitor reports too provide indications for differentiation into young and established businesses for over 40 countries. Of the 13 individual factors of the GEM reports, the following factors with regulation reference are particularly relevant for young businesses (GEM Report, 2006):

- Protection of intellectual property
- Policy 2: Regulation and taxes
- Market Openness 2: Market entry barriers
- Market Openness 1: Market changes

Legal protection for intellectual property, free enterprise, low-hindrance regulations and low market entry barriers are basic prerequisites for the development of founding companies. In relation to these three factors, the countries to the fore of the GEM ranking should be particularly highlighted as positive examples: USA, Singapore, United Arab Emirates, Iceland, Belgium, Finland and Australia. For established companies, it is more important to defend their market positions, to be able to erect high market entry barriers against newcomers and to impose high compliance costs on young companies by setting high regulation standards. The GEM Report therefore comes to the conclusion, in relation to industrial countries, that countries with better (poorer) structural

conditions tend to present a higher (lower) founding quota (GEM Report, 2006, p. 27).

4.3 Brake on Economic Growth

The hidden costs of regulation in general should not be underestimated. Businesses take measures to comply with the regulations imposed upon them by the government. Such measures are accompanied by significant costs. To an increasing extent, it is becoming recognized that unnecessary compliance costs may have adverse effects on economic growth and employment.

Which mechanism is causing the negative effects of unnecessary compliance costs on economic growth in general and small businesses especially? Compliance costs are primary costs for businesses. Businesses will have a direct cost-reduction if their compliance costs decrease. This cost-reduction leads to higher profits and, by consequence, to more investment. Besides, the cost-reduction will be passed partially in prices. Lower prices will improve the competitive position. As a consequence, exports will grow. Finally, trade unions will succeed in taking part of the profits to increase wages. The increased wages will lead to a higher consumption. In the end, the production of businesses will increase, due to all these factors: higher investments, more export and more consumption. In the short term, employment of clerically jobs could decrease slightly. However, in the longer term, this job loss could be compensated by other jobs. In the long run, the effect on employment is expected to be zero (De Wit and Nijssen, 2002).

4.4 Ideologically Charged Policy Discussions

Generally speaking, policy discussions about compliance costs are characterized, on the one hand, by their highly practical content and, on the other, by their very ideological content. The “Leitmotiv” for many discussions can be best described by mottos such as “cut the red tape burden” and “Bürokratieüberwälzung”.

One illustration of the tone of the political debates on this subject in the US is revealed by the remarks made by Senator John Glenn: “...Together, I believe, these expanded agency requirements provide the greatest opportunity for progress in the war against red tape”.² The focus is often one-sided, aiming to reduce the costs of compliance, but paying little attention to the benefits for

² Floor remarks of Senator John Glenn, 141 Cong. Rec. S 5276 (April 6, 1995) in: The Paperwork Reduction Act of 1995: Implementing Guidance for OMB Review of Agency Information Collection, Office of Information and Regulatory Affairs, Office of Management and Budget, June 1999, page 54

society. Another aspect is that, through the ties with the compliance costs the political objectives and the regulation itself have become, indirectly, the subject of discussion.

As a result of the above one-sided approach, policy aiming at reducing compliance costs, now unnecessarily finds itself in a political field of influence. This is an adverse effect on the effectiveness of the policy.

4.5 Confusion of Perspectives

The main problem is perhaps the confusion of concepts related to compliance costs caused by an unclear mix of two different perspectives. The most dominant perspective in the literature is the business perspective; the other, the public policy perspective. Our position is, we need the policy perspective to reduce, avoid or take away unnecessary compliance costs successfully.

The dominance of the business perspective is easy to understand. Compliance costs are cost of businesses. However, only a minor part of these costs can be influenced by businesses and it is to be expected that businesses will do their utmost to keep the cost of compliance as low as possible by complying in an efficient way. Competition will force them to do so. This is what we call the endogenous part of compliance costs. It does not make sense to integrate the endogenous part of compliance costs in reduction policies. The core of the business perspective is that compliance costs are the costs that would disappear if there was no legal obligation. Of course, this argument makes sense. However, it appears very difficult to measure compliance costs from this perspective. To calculate the business economic costs of complying with legal obligations, it is necessary to reckon all the different specific conditions of the regulated businesses. For instance, we should know about the relevance of legal information obligations as management information for the businesses themselves. Or, we should know about the benefits of complying for the businesses themselves. Or, we should know which part of compliance costs are avoidable from the perspective of the law, e.g. asking for tax advice or inefficient compliance. Or, we should know the opportunity costs of complying with the law. For instance, if an entrepreneur would comply with his legal information obligations during underloaded hours, his compliance costs would be zero.³

The most important question, however, is about the value added of answering these questions from the perspective of an efficient policy addressed at taking away or avoiding unnecessary compliance costs. The origin of compliance costs is the public sector. So we need information about the exogenous

³ Some argue, opportunity costs will never be zero, because alternative opportunities will always be there, like product innovations or working upon the market.

determinants, from the perspective of the businesses, of compliance costs. That's the very reason why the Standard Cost Model (SCM) standardizes the way of compliance of businesses into a 'normally efficient way of compliance'. To stress the business perspective (endogenous determinants of compliance costs) might be even counterproductive. This could give the public sector which is responsible for business regulation, an argument to lean back, saying it is entrepreneurs' responsibility first to keep compliance costs as low as possible. The public sector should give the business sector the optimum exogenous framework conditions regarding compliance costs, which enables the businesses to keep the endogenous part of compliance costs as low as possible. This should be one of the cornerstones of high quality regulation.

5 What's at Stake in the World of Regulation and Compliance?

It is an important area. Businesses are the lifeblood of the economy. Independent of government, they respond to market signals in a far more efficient manner than central planning ever can achieve. Increasingly too, private business is carrying out tasks which were previously in the province of the public sector. But simply because they are independent of government, this does not mean they are independent of society. They need to be regulated as well as to act as government agents in certain cases. Both of these aspects impose costs on business, costs that reduce the size of the potential national cake available for consumption and investment, and, in an increasingly global market place, could reduce the competitiveness of business in their market place. Reducing the business burden is not simply about pandering to the special pleas of an enclave within society: it is about significantly increasing the prosperity and welfare of society in general. Similarly the move to better regulations is not simply about reducing the business burden: it is also about getting better, more effective regulation which achieves the intended purpose at a minimum cost. The essence of this book is the lower the level of unnecessary compliance costs, the higher the degree of compliance!!!!

5.1 Doing Things Better

In this book, we have attempted to describe this process, to look at the problems involved, to forecast its future developments and to derive relevant policies. These insights are intended as a resource for those engaged in forming regulations in all countries, particularly those involved with reducing the compliance costs. The contributors are all leading experts in the field, many of whom have direct policy experience, while others are academics. Interest in reducing the compliance costs is not simply limited to countries in Europe nor even advanced market economies. It has become, as we have said, a global

issue. But simply because it is an idea whose time has come, it does not mean that all countries are treading the same path, nor that they should tread this same path. Different countries are at different stages of development, have different regulatory regimes and different depths of such regimes. Arguably, many countries do not need less, but more regulation. It must be clear from the outset that simply reducing the level of the business burden has never really been the goal of those concerned with this activity. It is about doing things better. That whatever burden is imposed should be administered in the most efficient way and, in particular, with respect to the compliance costs it puts on firms, but also on individuals. It is also saying, yes regulation is important, but so too is business. There is a trade off to be made. At times, this means reducing the business burden; at times, it may mean increasing it. But, it will always mean regulating as efficiently as possible, where the impact on business is part of the calculus.

5.2 Where Do We Stand?

This is why the movement for better regulation is at differing stages in different countries. At the forefront is the EU and certain countries within the EU, who are committed to controlling, and initially at least, reducing the business burden. Central to this process is the measurement of the business burden, being the costs of the regulated businesses. A high degree of compliance of the regulated businesses is the first and indispensable step towards the achievement of the public goals. As the book has emphasized, this is then the trigger for an examination of the whole policy making process, from conception to implementation. Some countries have, temporarily at least, simply skipped the measurement stage. In many cases, as emphasized, this is appropriate and the move to better conception and implementation of policies is welcome. Indeed, such is the importance of this not just to firms but to the whole of the country, that it seems to us a valid focus for development aid which has to date met with rather limited success in promoting developing countries economic growth and poverty reduction. Such is the quality of regulation in many developing countries as described in this book, that it should be possible to substantially increase the extent to which the regulation achieves its intended purpose, whilst at the same time, substantially reducing the regulatory burden and perhaps simultaneously substantially reducing the size of the shadow economy. Nonetheless, at some stage, it becomes necessary to measure the administrative burden. If you are trying to travel from Copenhagen to Barcelona, then in the initial stages of the journey, just heading south may be sufficient, but after a point, a map with distances and locations becomes essential. Here, it seems likely that the methodology being developed by the EU will eventually become the template for other countries across the world.

5.3 Better Regulation as a Learning Curve

What is more, the SCM methodology and the move towards better regulation has been both a learning curve to administrators and a reawakening for them as to the importance of business and the entrepreneur. The administrators have been forced to put themselves in the shoes of the person bearing the administrative burden, in modeling step by step all aspects of that burden. Because of this, it becomes apparent that traditional obligations placed on firms and individuals can be organized better. This is why, at this stage of the process, it is feasible to focus on cost reductions which to a considerable extent can be achieved by getting rid of 'regulatory slack', i.e. doing existing tasks more efficiently and removing parts of the administrative burden which no longer have relevance, or at least, sufficient relevance to warrant their continued existence. This is the archetypal win-win situation, but it is a stage with a finite life. Thereafter, a stage will come at which easy cuts in the administrative burden can no longer be made, but rather such costs will entail the abandonment of regulation that fulfils a genuine purpose or substantive obligations with related substantive compliance costs which are very close to the public goal to be achieved itself. At that stage, it will need to be asked more specifically whether the gains from reducing compliance costs further outweigh the welfare costs from reducing regulations, i.e. a cost-benefit analysis.

Nor does this necessarily imply government simply targeting an administrative burden of a certain magnitude, with regulation unchanging. The world changes, the need for regulation changes, much of the impetus is in an upward direction. Increased prosperity brings with it increased concerns for health, safety, environment and the general standards of product quality. New products are continually appearing on the market, at an increasing rate. These products, as with Genetically modified foods and mobile phones, are technology driven, with new technologies about which, in many cases, we are not yet in the possession of full information as to their full effects. These products need to be regulated. Increasing concerns with the environment require governments to ensure that business behaves in accordance with a code of practice which is likely to become increasingly stringent. But this does not mean that it is inevitable that the compliance costs are set to rise at some point in the future, nor even that further reductions in this burden are impossible.

That's exactly where the instrument of Regulatory Impact Assessment (RIA) can be very helpful. RIA being a tool by which governments integrate benefits and costs of public policy into a balance that achieves the country's priorities. RIA has evolved into a framework for public-private cooperation that can greatly improve the relationship between public and private sectors in effective and efficient public policy. The private sector should ensure that it is a constructive partner in this consultation process.

5.4 How to Facilitate Reduction of Compliance Costs?

The book has highlighted several possible developments which may facilitate reduced compliance costs or, more specifically, administrative burden. The first of these is IT and, more generally, technology. The administrative burden is in a large part about the costs of providing information and, above all, IT has facilitated the flow of information and will continue to do so in the future. But, even amongst firms, and especially amongst ordinary citizens, IT skills are not evenly spread and care needs to be taken to ensure that future developments do not further disadvantage those on the wrong side of the digital divide. Here, education is important.

Secondly, there is the possibility that what are current obligations with current reporting flows could become voluntary, depending upon the goodwill of firms and citizens and also social pressure to ensure that they are complied with. Corporate Social Responsibility (CSR) or self-regulation are key words in this context. There are obvious problems with this and if some firms choose not to comply, this may trigger a race to the bottom. But in addition, many obligations carry information valuable to the consumer, or, in the case of intermediate goods, to other firms. This information will still need to be conveyed to the purchaser and simply stating the information on the packaging may not be a sufficiently credible signal. This is why firms invest in ISO9000 and ISO14000 to signal their management quality or environmental credentials. These are expensive accreditations to acquire, but for many firms in many markets, these accreditations are far from optional, and even now, they too in a sense are part of the compliance costs imposed on business by semi-public organizations.

Thirdly, we emphasize again that this is a dynamic process and we now focus on several dimensions of this process. Firstly, increasingly in the age of globalization, much of the regulatory burden placed on business stems from international treaties and organizations. There are two particular dangers here: (i) That there may be the temptation to move to a one-size-fits-all approach, which is not applicable to a world as diverse as ours at the beginning of the 21st century; and (ii) International agents concerned with this process are divorced from the process of implementing the regulation and, to an extent, divorced from the impact on and the needs of business. Hence, they may not care as much as entrepreneurs and supporters of better working markets would like. There is also the Lucas critique which implies that when we change the policy environment, economic agents will behave in ways which could not be predicted from their past behavior (Lucas, 1976). In other words, there will be unexpected consequences of the move to better regulation. Many are likely to be beneficial, e.g. the literature argues that excessive regulation is a factor pushing business into the shadow economy. Will the move to better regulation cause a reduction in the size of the shadow economy? But to paraphrase Rumsfeld, what is there we don't know that we do not know?

Fourthly, it has to be emphasized once more how important the policy environment is. However relevant all theoretical insights are, however useful the SCM method and other approaches, without sufficient and enduring support at the political level, it will not work. In this book, it was demonstrated on several occasions that the way any country or group of countries (as in the EU) is dealing with this issue strongly depends on the intensity and willingness of politicians to make the issue of compliance costs and of the administrative burden central in their overall policies. The better this link is realized, the better also the results that can be expected. Furthermore, the multilevel aspects have become better known, both upward and downward. Initially, the orientation was strongly national, but now, the relevance of this approach both at the supranational level like the EU and at the local and regional level (municipalities) has become much clearer. In the near future, this multilevel situation should get more attention.

Finally, as mentioned earlier, the current approach to better regulation even in, e.g. the Netherlands where it is fairly advanced, will continually evolve and this includes our approach to measuring the regulatory impact. This is, in part, because of the changing environment in which business and government operates in as noted above. But it is also because we will be moving closer to our target of reducing the regulatory burden towards its optimal level and, as we approach Barcelona, moving south will no longer be sufficient as a strategy. At some stage, it will become necessary to consider not just the regulatory burden but also the regulatory advantage, i.e. a cost-benefit approach. Nonetheless, it remains our view that the SCM will continue to provide the best foundation for evaluating regulations and thus will be the foundation for regulatory impact analysis in the foreseeable future.

6 Structure of the Book

The book is structured as follows: After this Introduction, we will continue in *Chapter 1* with the issue that today, compliance costs of businesses are part of the political agendas of many countries from the EU, the OECD and even developing and transition countries. It will be demonstrated that this has not been the case always by highlighting the major phases between the first recognition by professionals about 200 years ago until the establishment of monitoring systems in the beginning of this century.

Chapter 2 will focus on the increasing number of countries which have been starting policies to reduce administrative compliance costs. Also, at the level of the EU, such initiatives have been taken. This chapter puts in picture an international comparison of mainly European countries regarding administrative compliance costs and reduction policies. The focus will be on the compliance costs for the business sector.

To get a full understanding of the phenomenon of compliance costs, a theory about origin and functionality of regulations is being presented in *Chapter 3*. Only if we understand where businesses regulation is coming from and what we want to achieve and by which means, can we combat unnecessary compliance costs of businesses in an effective way.

There are a considerable number of techniques and models for estimating the level of impact of regulations as will be demonstrated in *Chapter 4*. Cost benefit analysis is considered particularly important for regulatory analysis. However, there is no definition of compliance costs that has gained wide acceptance. Disagreement exists about whether certain elements should be included in the calculation of compliance costs. This chapter offers a critical explanation of a variety of techniques that are in common use and then summarizes those that are adopted by governments around the world.

How to measure compliance costs is the issue of *Chapter 5*. Adequate measurement needs sound definitions. The container concept ‘compliance costs’ will be analyzed in this chapter. In this chapter, the Standard Cost Model (SCM) will be explained. Also, a new module of the SCM to measure substantive compliance costs will be introduced. One of the crucial aspects of the understanding of SCM is to discuss for which target group the results are. Is it the entrepreneur to help him/her reduce his/her own compliance costs? Or, is it the politician or the law maker to facilitate improving the quality of law by avoiding or taking away unnecessary compliance costs? The answer to this question has a big impact on how to measure compliance costs.

In the USA there is a longstanding experience with reducing compliance costs as will be illustrated in *Chapter 6*. Many consider regulatory relief for small business and implementing regulatory objectives a zero-sum game. The U.S. Regulatory Flexibility Act (RFA) of 1980 directly challenges the zero-sum game proposition by requiring regulatory agencies to search for non-zero-sum solutions for regulations having a significant impact on a substantial number of small businesses. This chapter evaluates the Regulatory Flexibility Act.

Chapter 7 presents the case of Tanzania. Tanzania’s dilemma of poverty in the midst of plenty is captured in the concept of the “missing middle”, featuring failure of micro firms to graduate into small and medium enterprises that would create a demonstration effect of the benefits of formalization. Tanzania needs efficient mechanisms for contract enforcement to stimulate economic linkages and encourage commercial bank lending. Tanzania needs an efficient labor market, focusing on skills improvement and competence rather than mandatory legislation as the basis for higher returns to labor. Tanzania, and countries with similar problems, need more efficient systems of information on the business sector and registration of movable and immovable property. Implementation of the program for Business Environment Strengthening for Tanzania addresses these problems. This chapter highlights the hassles and vicissitudes of change management in a regulatory reform process in a developing country environment, and the instruments that are available to handle the challenges involved.

Chapter 8 stipulates the opposite developments of globalization and ‘Europeanizing on the one hand, and the need for customized regulations on the other. The average citizen and entrepreneur is afraid that the most essential part of the regulation, the flexibility and the content, based on his own responsibility, will be under threat. There is no doubt whatsoever that there are great efficiency benefits to be reaped there. It would be wise to harvest these. Time will learn with what speed and to what extent this change will have to be made. It will be necessary to reduce the burden of regulations, but in doing so, to pay attention not only to quantitative but also qualitative objectives.

Laws and regulations have their limitations will be the issue of *Chapter 9*. In abundance, they might become futile, particularly due to regulatory capture. Business Impact Assessment is called for to reduce costs of doing business in Dubai and to improve the quality of regulations. Corporate social responsibility (CSR) is also viewed to improve the general business environment. This chapter highlights the impact of regulations on businesses in Dubai and the situation of CSR in the market environment. The chapter calls for CSR (self-regulation) and argues that when fitted in sound public–private partnership framework could achieve general improvement of the business environment in Dubai.

Chapter 10 discusses government regulation and the consequent compliance costs for the private sector from the perspective of transaction cost economics. In many cases, government regulation is shaped as legally binding standards. In order to comply with these standards, private sector firms meet various types of transaction costs, such as the bonding costs that the principal/agent relationship of government regulation brings about. On the other hand, good standards may reduce transaction costs. Therefore, optimal design of government regulation requires the design of standards with the lowest possible transaction costs. Due to network externalities and economics of scale, and in order to guarantee a level playing field, good coordination and unifying standards within the EU can be beneficial. This chapter provides examples of such standards.

Chapter 11 focuses on regulatory reform from the perspective of developing countries in general. Many countries today have placed regulatory reform programs at the core of their governance and microeconomic strategies. Within those reforms, regulatory impact assessment (RIA) has become a prominent tool by which governments integrate benefits and costs of public policy into a balance that achieves, over time, the country’s development priorities. The spread of RIA into less developed countries is largely due to intense pressures to stimulate growth, particularly pro-poor growth. Although RIA began as a set of analytical methods, RIA has evolved into a framework for public-private cooperation that can greatly improve the relationship between public and private sectors in effective and efficient public policy. Yet business representatives have not, in general, built capacities to assess proposals from governments, nor the capacities to collect relevant and timely information that can support the process of discovering the right solution. The private sector should ensure

that it is a constructive partner in the consultation process by supplying timely, relevant, and reliable information through the consultation process.

The reasons for giving special treatment to enterprises, compared with other stakeholders, are extensive and will be the central issue of *Chapter 12*. This chapter is from a Swedish perspective. Companies and entrepreneurship, as such, enjoy no special status. Instead, what counts is the sum total of direct and indirect repercussions of political decisions. This is what dictates their being given special treatment, in terms of the consequences of new and amended business regulations. Business owners are a political minority and will most certainly remain so and few politicians know what everyday life in business is, although many politicians mean well. The politicians' main concern is, of course, the budget but what is self-evident when the state is a stakeholder is deemed by decision-makers to be less obvious where other stakeholders, such as business, are concerned. In a market economy, it is necessary to ensure that companies can compete on equivalent terms. This is why an early RIA is so important. It should be an analysis that, in the initial phase, is confined to direct effects on companies but is used to assess the effects on society as a whole in the subsequent phase.

In *Chapter 13*, the public policy process is viewed as a continuous source of compliance costs. Explanations are sought for the phenomenon that a substantial part of these costs could have been evaded or prevented and for the fact that it is an arduous task to expel unnecessary (or unwanted) compliance costs afterwards. Main drivers behind unnecessary compliance costs are described per stage in the policy process. The key factor for improving policies and reducing compliance costs is adequate information.

Regulation matters, is the device of *Chapter 14*. It organizes markets and societies and is, therefore, a cornerstone of freedom and welfare. But regulation may also cause problems, unnecessary burdens, unintended side-effects and costs. The aim of this chapter is to give evidence that – and how – regulatory systems can be built to become more effective than most of them are today. With a heuristic approach, this chapter is looking for successful measures and trying to identify patterns. The conclusion is, that a regulatory system should be built on evidence-based solutions, acceptance within the businesses by consultation, the monitoring and steering of the regulatory process, independent scrutiny and legitimacy and a political program to make the cross cutting issues powerful.

Chapter 15 describes the institutions for cutting administrative burdens in the Netherlands, based on the following criteria: measurement, reduction targets, coordinating minister, and incorporation in the regulatory process. The chapter examines how the institutions helped to change the policy culture. Moreover, it is argued that the institutions can effectively be applied in other countries and for a broader scope of better regulation including administrative burdens for citizens and substantive compliance costs.

ICT solutions to reduce administrative burdens will be the central issue of *Chapter 16*. The paper based functional hierarchy appears to be one of the

important origins of the administrative burden. In such a functional hierarchy, the knowledge of the professionals on the one hand and the information of the clients on the other are two important resources. Both resources need to be managed for the organization to be effective and efficient. Two trends are witnessed. First, ICTs create an interorganizational information infrastructure that is becoming interoperable. Second, professional knowledge is becoming modularized, with organizations starting to share their professionals and their knowledge in focusing on core competencies, outsourcing all other activities (and the relevant knowledge) and creating shared service centers. This results in a radical transformation of organizations. This transformation of the organization results in potentially high levels of reduction of the administrative burden, without reducing the number and the level of norms and regulations. But to achieve such a transformation, we need a breakthrough comparable with the digging of the Canal of Suez.

Chapter 17 examines the contemporaneous relationship between the exchange rate regime and structural economic reforms over a period of 30 years for a broad “world sample” and an OECD country sample. The central question is whether structural reforms are complements or substitutes for monetary commitment in the attempt to improve macroeconomic performance. The empirical results, on the base of panel data techniques, suggest that, on average, an exchange rate rule positively correlates with the overall structural reforms and trade liberalization in particular. On the other hand, no significant and robust impact of exchange rate commitment on labor and product market reform was found. The results are similar for both the wider, more heterogeneous world sample and the panel of OECD economies. They contradict the hypothesis that exchange rate commitments may have slowed down the pace of structural reform, but neither provide robust evidence that losing the possibility of an exchange rate adjustment promotes labor and product market reforms.

Finally, in *Chapter 18*, a new developed RIA coordination system will be presented. Measuring compliance costs of businesses e.g. administrative burden is hot stuff, from scientific view point as well from policy praxis. Also, the number of persons involved has increased considerably from a small inner circle of scientists and ministerial experts to rather larger numbers of politicians, public officers and private consultants, specialized in public advisory. Almost by consequence, the debate about concepts, definitions and methodology starts again, every time new participants join the debate. In these debates, there are mostly two key questions. First, are there arguments to introduce the public goals of regulations in the measurements or could the measurement be restricted to the costs of the regulated parties (businesses, citizens etc.) only? Second, which methodology is most appropriate to measure benefits and costs of regulations? This chapter tries to bring more transparency in order to stimulate a more impartial discussion about the topic deregulation and its consequences. Important elements of this transparency are an adequate categorization of the separate cost and benefit effects, a systematic evaluation of these cost and benefit effects, and finally, an evaluation of the available

techniques/methodologies. Such transparency could be guidance for all who are involved in the law making process and the measurement of compliance effects.

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