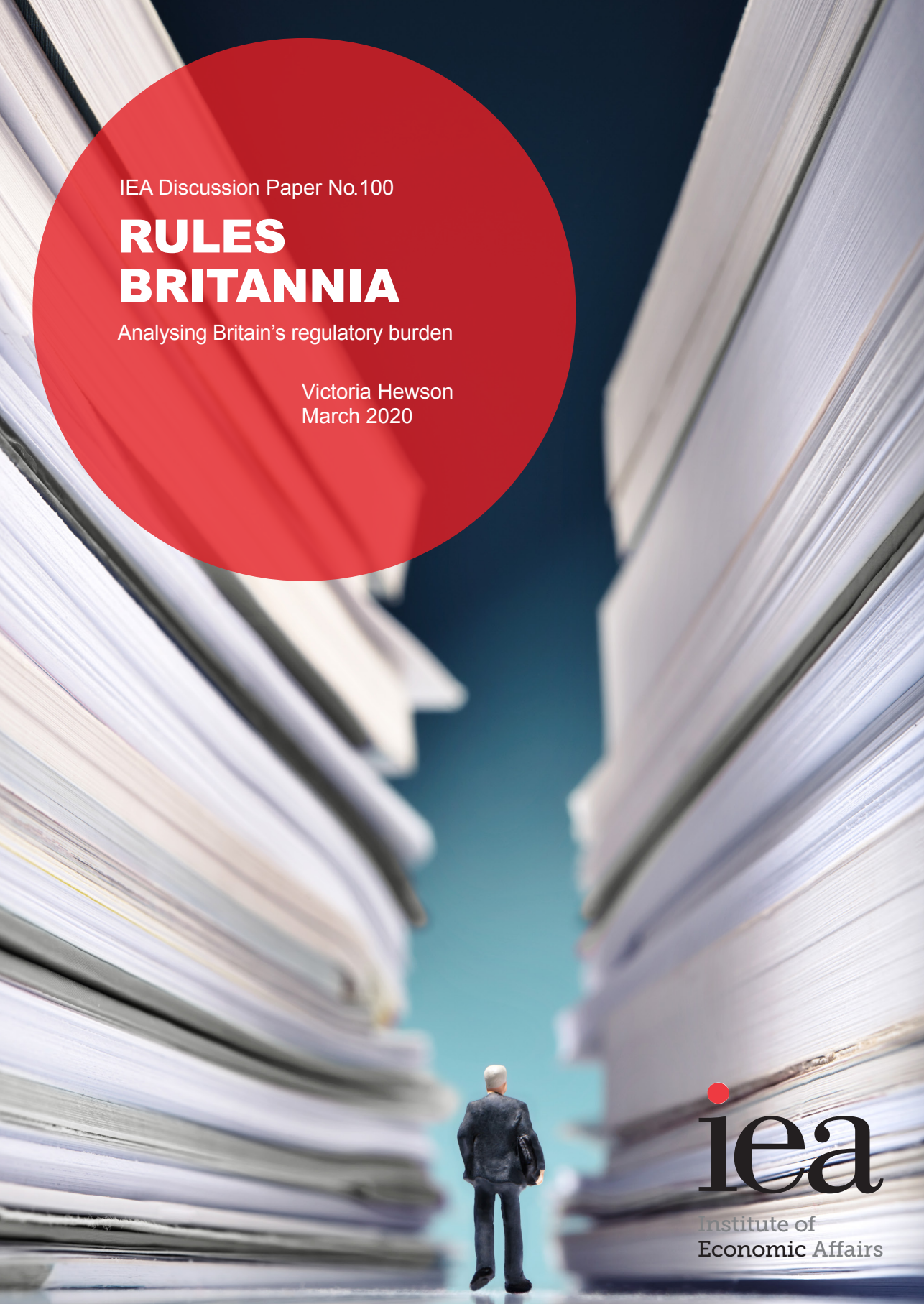

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RULES BRITANNIA

Analysing Britain's regulatory burden

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Foreword

The Institute of Economic Affairs has established a new programme – Regulatory Affairs. The programme is dedicated to analysing regulation and regulators in the UK.

As the UK moves towards regaining independence in law-making and regulatory policy, after leaving the EU, there have been calls to use this new independence to tackle red tape and roll back regulation. But as EU regulation has only formed part (though a large part) of the regulatory burden in this country, a more fundamental and evidence-based examination of regulation and regulators is needed.

This first paper from the programme addresses some high level questions: What is regulation? Why regulate? Who regulates? Is it working? Do we know what it costs? What are the implications for the rule of law?

As a starting point, the paper establishes that regulation is a wide ranging and amorphous concept. Coupled with a broad definition of market failure, used as justification for regulatory interventions by government and policy makers who claim to support free markets, regulation is in effect a powerful tool for government to try and achieve particular policy objectives.

Successive waves of regulatory reform initiatives have focused on procedural matters, such as carrying out impact assessments and consultations. Ways of testing whether a regulatory intervention is necessary or desirable in the first place, or successful after implementation, have been neglected.

Regulators' objectives have been expanded to include considerations of equality and equity, and their fields of influence run into every aspect of economic and civic life. This gives established businesses ever greater

opportunities for lobbying to influence regulation in their favour. The rule of law is undermined by weak mechanisms for accountability and legal review, extensive regulator discretion, complexity, and unpredictability.

Cost-benefit analyses applied by government are unsatisfactory as they include only the direct costs of compliance and do not attempt to capture the dynamic impacts on innovation and competition. Using the high-level methodology previously applied by the Better Regulation Executive, the total cost of regulation in in the UK today would be estimated at about £220 billion per year. Such estimates are of limited value, however, as it is difficult to calculate macro costs and benefits, and dynamic effects on markets, or quantify the costs to individual freedom and democracy.

The next steps for the programme are:

- Creating a database of regulators, their powers and accountabilities.
- Producing detailed studies of individual regulators to assess their performance, starting with the Information Commissioner, in a briefing to follow this paper.
- Informing the debate on regulatory aspects of the following: the negotiation of the future relationship with the EU in the course of 2020, free-trade agreements with other countries, and the proposed development of free ports.

Introduction

In our political discourse there is much discussion of red tape, frequently phrased in terms of ‘challenges’ and ‘bonfires’ to reduce and cut it. Supporters of free markets often have a general feeling that there is too much regulation or that it is too intrusive, badly formulated and ineffective. However, proponents of these positions are often lacking in empirical evidence so are susceptible to accusations of either exaggerating the impact of regulation or not caring about the environment, workers, children or consumers, when often the opposite is true. Supporters of free markets value and recognise the importance of all of these and believe that market solutions, and less state regulation, would improve the situation for them, as well as improve prospects for economic growth.

As the UK leaves the EU it will adopt an independent regulatory policy with the ability to repeal and amend EU rules, and to introduce new regulations in fields of EU competence. This freedom will have to be exercised within the parameters of international commitments such as WTO rules, free-trade agreements (including whatever is agreed with the EU) and other international agreements. It will also have to be done in full consideration of the impact on trade with the EU that will come from diverging at a national level from its regulations. Additional consideration needs to be given to the impact on Northern Ireland, which will remain bound to EU goods regulations at least until 2024 when it will have the option to vote to exit that arrangement.

Regulation has been a tool of EU integration. The implications of this driver being removed from UK regulatory policy should not be underestimated. The former Chancellor of the Exchequer signalled the government’s intention to ‘liberate businesses’ from the ‘overbearing bureaucracy’ of

EU laws and design 'smarter, more flexible regulations'.[1] But apart from the Brexit aspect, this sounds sadly familiar, and calls to mind similar rhetoric and initiatives of successive governments since at least the 2000s, including the then Chancellor himself when he was Business Secretary.

There is no doubt though, that regulation is a major source of concern for businesses, although the concerns tend to differ between the strategic interests of larger businesses with legal and lobbying firepower, and small and new businesses for whom the costs of regulation represent barriers to entry and growth. The perception that unelected officials in entrenched positions are enforcing rules that only seem to increase in scope and prescriptiveness whichever party is in power, contributed to the feelings of dissatisfaction that led British people to vote to leave the EU in 2016. There is a risk now, with EU laws being transposed *en masse* into UK law and regulators pouring cold water on suggestions of reforms, that the innate stickiness of the regulatory state will assert itself and the opportunity for meaningful change will be lost.

The Regulatory Affairs Programme will examine regulators and regulation across a range of sectors and test the performance of the UK's regulatory measures and institutions. This will help in understanding the scale and scope of regulators' powers and where they are operating effectively, as against their own remit and in objective terms. It will provide both an empirical and normative basis for challenging existing regulators and regulations.

We start this paper with a high-level review of regulation as a concept, and set out the principles that will underpin the work of the programme. This will be followed by a series of studies of regulation in specific cases, covering particular commercial activities such as financial services and energy, economy-wide or horizontal regulators such as the Competition and Markets Authority (CMA) and the Information Commissioner's Office, and civil society regulators such as the Electoral and Charity Commissions.

1 Chancellor Announces 'Brexit Red Tape Challenge'. *Financial Times*, 30 September 2019.

What is regulation?

What is meant by regulation? There is no settled definition; the concept of regulation is amorphous, and there is perhaps no clear boundary between regulation, law and policy. For the purposes of this paper, and for the work of the programme, we will be flexible on the definition but will operate broadly on the basis that regulations are rules that apply to specific sectors or activities, often (though not always) made by executive power or lower order rule-making bodies in order to implement laws passed by a legislature. This may be contrasted with the idea of laws setting out binding requirements that apply to an entire population, which are passed by a legislature or developed through the common law.[2]

The concept of regulation is broader than simply the legal rules, however, and includes guidance, notices and decisions (sometimes called 'soft law'), as well as less formal interactions and negotiations between regulators and the regulated. The formal legal framework of rules has been described as the 'scaffolding' supporting regulation: 'the law provides the sanction of last resort against which compliance is sought through negotiation, bargaining and threats. Regulation in practice is better understood as operating in the shadow of the law' (Veljanovski 1991).

This approach of using bargaining and threats to pursue a policy goal has been seen recently after the Christchurch terror attacks[3] in the effort by governments to change the practices of digital platforms by agreeing, at international level, 'a set of collective actions' with tech firms. The implication here is very strongly that if the collective actions are not delivered, formal

2 Although this distinction is also not clear cut, or perhaps even meaningful, as the formal legal rules that form part of regulation are also law, though the associated guidance, and interactions are not.

3 https://www.christchurchcall.com/

legal steps will follow.[4] These approaches are in tension with the rule of law (examined further below) and competition (as large incumbent providers are able to strengthen their relationships with lawmakers and regulators and influence policy in ways that are favourable to them) (Hewson 2019a).

Regulations can be detailed and complex, with legal requirements running to thousands of pages in the case of, for example, the financial services rule books or chemicals regulations. In the UK, regulations can be made by Act of Parliament but are often promulgated either by way of statutory instruments drafted by government departments under the powers granted to ministers under an Act, or by regulators themselves under powers delegated to them. A large proportion[5] of our regulation has been passed at EU level, and was either directly applicable as regulations, or implemented in UK law by Act of Parliament or statutory instrument.

This account of regulation is focused on rules of behaviour that should be adhered to or the rule breaker could be met with sanction. The concept of regulation can be extended to strategies to direct behaviours in a wider 'regulatory environment' where 'technological management' can be deployed to remove non-compliant choices from the possible actions of the regulatee (Brownsword 2019). This paper will focus on regulation where compliance or non-compliance is within the control of the regulatee, but the implications of advances in digital technologies and artificial intelligence for the technological management approach to regulation, in combination with some of the failings of regulators discussed below, are significant and will be of interest to the programme.

4 It is also a familiar regulatory life cycle: moral suasion, followed by self-regulation, increased lobbying for formal rules, which are then enacted and become an entrenched and accepted part of the affected sector, with any defects in the regulatory structure being met with more regulatory solutions.

5 The National Audit Office reported in 2016 that in the 2010-2015 Parliament, of the 951 regulations validated by the RPC, 297 (31 per cent) originated in the EU.

Why regulate?

People who generally support free markets justify regulation on the basis of market failure, internalising externalities and correcting information or competence asymmetries (Stigler 1975). Competition law and the authorities that oversee it are justified on these pro-market grounds. The CMA is required by law to 'promote competition … for the benefit of consumers'.[6] It describes its objective as 'Competition that works for everyone'. The government's Better Regulation Framework, which government departments and regulators are supposed to follow, states that 'generally, identifying a market failure would serve as the rationale for intervention'.

The definition of market failure in economic terms has been understood to mean situations in which outcomes are not Pareto efficient[7] (where it is impossible to benefit one individual without injuring another). More generally it has been described as markets that are not perfectly competitive, where there are asymmetries of information, under-provision of public goods or externalities. Either of these represent such a high bar that in reality few, if any, markets can ever approach this ideal, so 'market failure… is ubiquitous and the scope for government intervention unlimited' (Bourne 2019). Classical liberals, and committed supporters of free markets, do not consider perfectly ordered markets to be necessary to deliver the benefits of economic freedom, or to be an outcome that the state can or should seek. The IEA's primer on classical liberalism explains (Butler 2015):

> Classical liberals believe that economic freedom is the best way to create general prosperity. Economic freedom allows people to adjust spontaneously to each other's needs and cooperate for their mutual

6 Enterprise and Regulatory Reform Act 2013 (http://www.legislation.gov.uk/ukpga/2013/24/contents/enacted).

7 See for example the OECD Statistics Directorate, Glossary of Statistical Terms.

> benefit – creating and spreading value in the process. The rules that create this spontaneous order are those of property, contract, honesty and justice. Between them they create an economic order of incomprehensible scale and complexity - far larger and more complex than any conscious agency could grasp, embracing the whole world.

The market failure analysis rests on 'unrealistic assumptions about behaviour in regulatory agencies, amongst politicians and amongst the electorate as a whole' and so 'takes us down an intellectual rabbit hole' where the ability of markets to provide regulatory services because they are valued by market participants is ignored (Booth 2019).

In practice, however, the term 'market failure' has, in the regulatory context, effectively come to be used to mean markets failing to deliver a particular outcome that is considered to be beneficial, such as low prices or the ability to easily move between providers of a service.[8] This is a way for politicians who are nominally in favour of free markets to seek to regulate towards their social or distributive objectives, while appearing to still take a pro-market position.

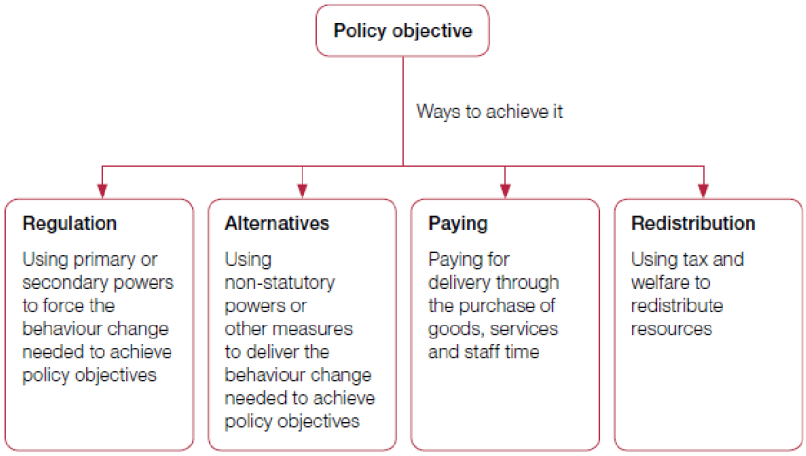
For those who reject free markets in principle, regulation is not just a way to redirect or cure defects in the functioning of markets. Here, no market failure justification is required; the only questions are how and by whom an activity should be regulated.

In political science, it has been suggested that regulation was pursued at EU level as member states feared a 'race to the bottom' as a result of elimination of trade barriers in the single market, and that the EU developments provided 'an additional source of legitimisation for national processes' (Lodge 2008). Because the cost of regulation is largely borne by the firms and individuals who have to comply with it, it is a way of pursuing policy without being constrained by budgetary limitations. This has especially been the case in EU rulemaking, where even the cost of enforcement and administration falls on member states and not on the Commission. Given the limits on the financial resources available to it, 'the only way for the Commission to increase its role was to expand the scope of its regulatory activities' (Majone 1994).

8 For example: Dominic Raab Vows to Put BILLIONS in Your Pockets If He Becomes PM. *The Sun*, 2 June 2019.

In the UK, regulation is used both to address market failure and pursue wider political goals. The NAO in its Short Guide to Regulation states 'Regulation is used to protect and benefit people, businesses and the environment and to support economic growth … [R]egulation is primarily used to address market failures. The characteristics of some markets mean that, left to their own devices, they risk failing to produce behaviour or results in accordance with the public interest (for example clean air) or policy objectives'. In this sense regulation is one tool that the state has to pursue its objectives, alongside taxation and spending and direct ownership and control of assets, as illustrated in Figure 1. Regulation is used to exercise influence or control over the economy, but, 'is distinct from direct government provision of services [such as through nationalisation] because it relies on using incentives to drive behaviour change in individuals and organisations outside of government's direct oversight' (NAO 2017).

Figure 1: Ways of achieving policy objectives



Source: National Audit Office (2017)

In the May government's Industrial Strategy White Paper, regulations were cited as one of the 'policy levers' available to the government in pursuit of the so-called Grand Challenges.

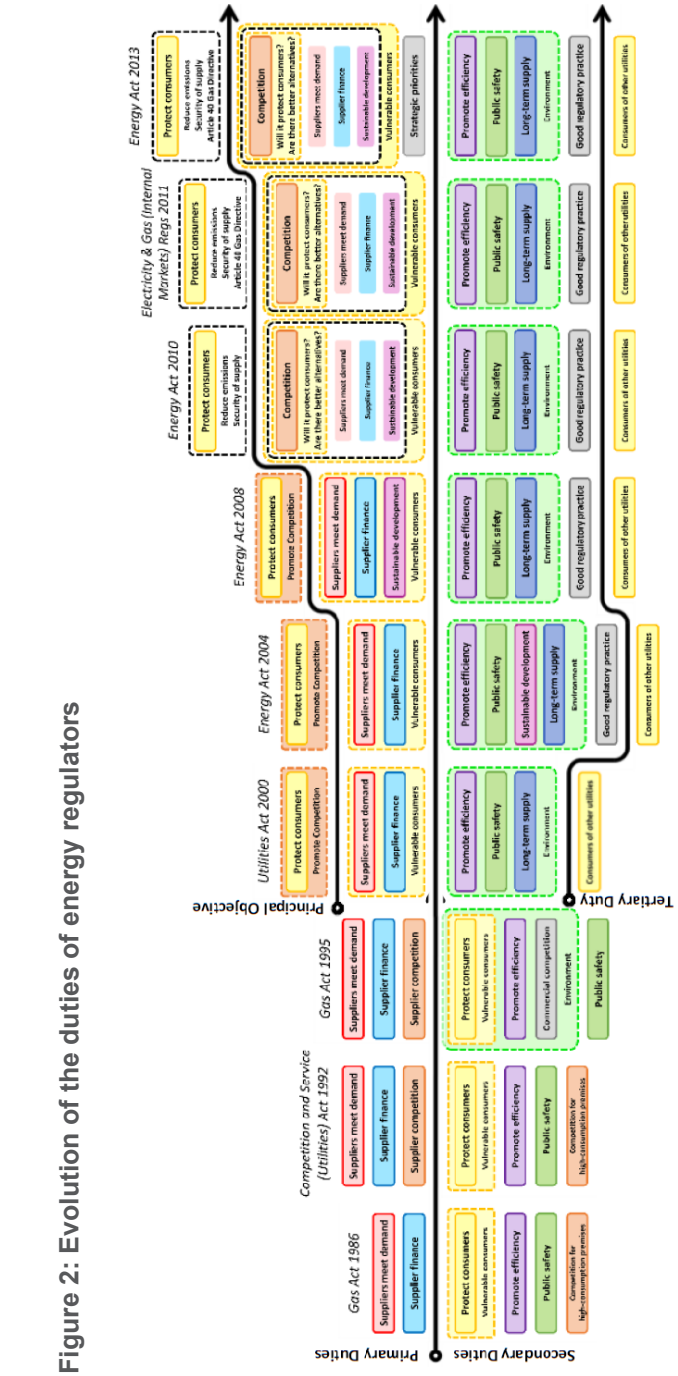
Current examples of objectives of regulations in effect in this country include: protecting consumers,[9] safeguarding health[10] and the climate,[11] encouraging investment in a particular sector,[12] creating a 'level playing field' in the market[13] and promoting equality and fairness.[14]

There are also centralised requirements that apply across public sector bodies which regulators are required to pursue. The Equalities Act 2010, for example, imposes a Public Sector Equality Duty (PSED). This mandates public bodies to have due regard to the need to eliminate unlawful discrimination, harassment and victimisation, advance equality of opportunity between people who share a protected characteristic and those who do not, and foster good relations between people who share a protected characteristic and those who do not. The PSED means that while not specifically tasked with anti-discrimination or equalities regulation, these matters must inform regulators' activities. They must follow certain specific requirements imposed by secondary legislation with respect to objective setting and reporting. A 2013 report for the Government Equalities Office, part of the then government's Red Tape Challenge, was critical of the vagueness of the 'due regard' duty and considered that it encouraged 'useless bureaucratic practices which do nothing for equality'. However it went unreformed and a later review by the Equality and Human Rights Commission was (perhaps unsurprisingly) more satisfied with the operation of the PSED (EHRC 2018).

Although the Principles for Economic Regulation published by the Department for Business, Innovation and Skills in 2011 state that regulators' activities should be focused and proportionate, the objectives of regulators in practice are ever-expanding, as illustrated in Figure 2 by the evolution of the duties of energy regulators.

9 Ofgem: https://www.ofgem.gov.uk/about-us/who-we-are
10 Public Heath England: https://www.gov.uk/government/organisations/public-health-england/about
11 The Committee on Climate Change: https://www.theccc.org.uk/about/
12 Ofcom: https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2017/encouraging-investment-in-full-fibre-networks
13 The Consumer Rights Act 2015: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/274853/bis-13-1356-consumer-rights-bill-supply-of-digital-content-impact-final.pdf
14 The Equality and Human Rights Commission: https://www.equalityhumanrights.com/en/about-us/who-we-are

Figure 2: Evolution of the duties of energy regulators



Source: Harker and Reader (2018).

In recognition of this, there are numerous initiatives and regulations in place that set out to discipline and formalise regulatory interventions and reduce their volume and cost. The government's Better Regulation Framework requires that before regulations are made, a Regulatory Impact Assessment (RIA) should be undertaken. RIAs should follow the cost-benefit analysis approach of HM Treasury's Green Book.

Since around 2005 the UK government has operated measures to reduce and simplify regulatory burdens, to reduce the stock of existing regulations as well as stem the flow of new ones. A 'one-in, one-out' rule where the costs of new regulations were to be off-set by the elimination of regulation of at least equal cost was introduced, and later increased to 'one-in, two out', and then 'one in, three out'. In 2015 the government adopted a Business Impact Target, reflecting the Conservative Party manifesto pledge to save business £10 billion in regulatory costs in the following Parliament. The Small Business, Enterprise and Employment Act 2015 requires government to publish a target for the cost to business of new, amended and repealed regulations and to report on progress against it. In order to calculate the aggregate costs, government departments and in-scope regulators are required to provide an assessment of the economic cost of their Qualifying Regulatory Provisions, in accordance with a prescribed business impact target (BIT) methodology. RIAs which show a business impact of +/- £5 million must be validated by the Regulatory Policy Committee, to try and address criticism of past cost assessments as unreliable and inconsistent. The idea was that such costs transparency would incentivise regulators to develop policies and guidance to reduce burdens on business, driving economic growth and productivity.

The BIT for the Parliament commencing in June 2017 was a saving of £9 billion. Figures published just before the 2019 General Election show that this target was met on a pro rata basis,[15] though there has been criticism from the NAO and elsewhere[16] that the calculation

15 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/844736/business-impact-target-end-parliament-report-2017-2019.pdf

16 https://www.regulation.org.uk/deregulation-regulatory_budgets.html.

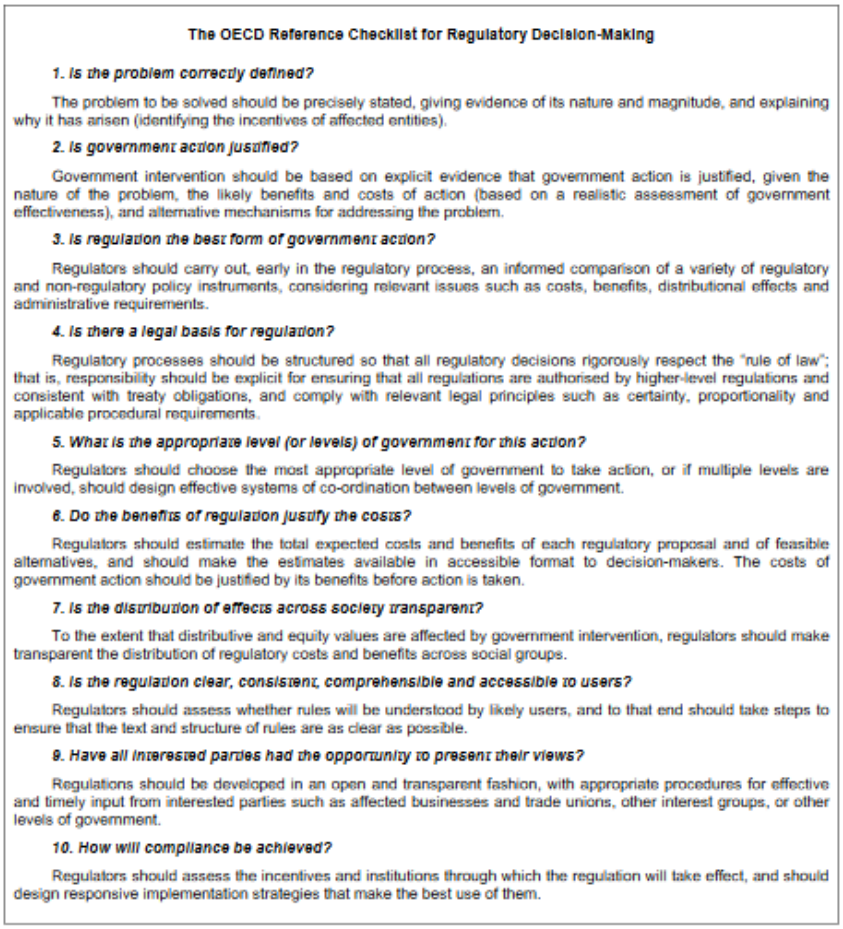
of the net savings is questionable, not least because of the exclusion from its remit of highly significant sources of regulation, such as EU, tax and minimum wage laws, the costs of which could wipe out any cost reduction in in-scope regulation.

The EU has also had a Better Regulation framework since 2002, focused on improving transparency, involving citizens, and assessing the expected and actual impact of action.[17] The Regulatory Fitness and Performance (REFIT) programme, launched in 2015, aimed to make EU law simpler and to reduce the costs of regulation while still achieving benefits.

Regulatory reform initiatives have thus focused largely on form and procedure. Much energy has been devoted to analysing principles-based versus risk-based approaches, optimal consultation and transparency practices, and costs formulations that focus on immediate transition and compliance costs, all proceeding from the assumption that a regulatory intervention is necessary or desirable in the first place. As part of its longstanding programme on regulation, the OECD has formulated a checklist for member countries to refer to, to support regulatory quality and transparency (set out in Figure 3).

17 https://ec.europa.eu/info/law/law-making-process/planning-and-proposing-law/better-regulation-why-and-how_en

Figure 3: OECD reference checklist for regulatory decision making



The OECD Reference Checklist for Regulatory Decision-Making

1. Is the problem correctly defined?

The problem to be solved should be precisely stated, giving evidence of its nature and magnitude, and explaining why it has arisen (identifying the incentives of affected entities).

2. Is government action justified?

Government intervention should be based on explicit evidence that government action is justified, given the nature of the problem, the likely benefits and costs of action (based on a realistic assessment of government effectiveness), and alternative mechanisms for addressing the problem.

3. Is regulation the best form of government action?

Regulators should carry out, early in the regulatory process, an informed comparison of a variety of regulatory and non-regulatory policy instruments, considering relevant issues such as costs, benefits, distributional effects and administrative requirements.

4. Is there a legal basis for regulation?

Regulatory processes should be structured so that all regulatory decisions rigorously respect the "rule of law": that is, responsibility should be explicit for ensuring that all regulations are authorised by higher-level regulations and consistent with treaty obligations, and comply with relevant legal principles such as certainty, proportionality and applicable procedural requirements.

5. What is the appropriate level (or levels) of government for this action?

Regulators should choose the most appropriate level of government to take action, or if multiple levels are involved, should design effective systems of co-ordination between levels of government.

6. Do the benefits of regulation justify the costs?

Regulators should estimate the total expected costs and benefits of each regulatory proposal and of feasible alternatives, and should make the estimates available in accessible format to decision-makers. The costs of government action should be justified by its benefits before action is taken.

7. Is the distribution of effects across society transparent?

To the extent that distributive and equity values are affected by government intervention, regulators should make transparent the distribution of regulatory costs and benefits across social groups.

8. Is the regulation clear, consistent, comprehensible and accessible to users?

Regulators should assess whether rules will be understood by likely users, and to that end should take steps to ensure that the text and structure of rules are as clear as possible.

9. Have all interested parties had the opportunity to present their views?

Regulations should be developed in an open and transparent fashion, with appropriate procedures for effective and timely input from interested parties such as affected businesses and trade unions, other interest groups, or other levels of government.

10. How will compliance be achieved?

Regulators should assess the incentives and institutions through which the regulation will take effect, and should design responsive implementation strategies that make the best use of them.

In the UK's war on red tape, little attention seems to be given to the first three (and perhaps the most vital) of the items identified by the OECD for assessing regulatory good practice:

- Is the problem correctly defined?
- Is government action justified?
- Is regulation the best form of government action?

There seems to be a perception that if only the right experts could be appointed in the right structures, then surely market failures could be eliminated, and it's simply a question of finding this state of regulatory equilibrium. Public choice economics, as advanced by Buchanan and Tullock, indicates that this is unlikely to be the trajectory of regulatory interventions. In reality, regulation is likely to lead to government failure replacing or adding to market failure, and to well-funded and highly focused interest groups being able to exercise greater influence, leading to rent seeking and regulatory capture.

New regulations were enacted and regulators created in the course of the privatisations of utilities, telecoms and railways in the 1980s and 1990s on the basis that the monopoly power of the newly created utility and railway operators needed to be kept in check. It was advocated at the time that as competitive markets developed, the need for regulators to control the prices and operating models would recede and they would gradually be retired. Professor Stephen Littlechild, an architect of the economic regulation of privatised industries, wrote in 1983:

> Competition is indisputably the most effective means... of protecting consumers against monopoly power. Regulation is essentially a means of preventing the worst excesses of monopoly; it is not a substitute for competition. It is a means of 'holding the fort' until competition arrives.

Despite the deregulatory initiatives of successive governments, rather than regulators being stood down as competition took their place, the volume and reach of regulators and regulation has actually been expanding, and in many ways this acts against competition in markets by imposing proportionately greater costs on smaller and newer businesses. Operators of firms in formerly nationalised industries no longer have any expectation of a reduced role for their regulators and it has been suggested that regulation of the energy sector is such that there is in effect no real energy market at all (Helm 2017).

Clearly for industries that were never nationalised the post-privatisation basis for economic regulation has never applied and regulation has grown to replace market and ex post legal solutions to discipline producers and protect consumers, as a matter of policy choice. In financial services, for example, the City was essentially self-regulating until the 1986 'Big Bang' swept away the restrictive practices of the Stock Exchange that underpinned

its self-regulation. This brought more competition, but a comprehensive statutory regime was considered necessary, partly as a result of EU legislation on financial markets. More generally, the enforcement and oversight role of the CMA now includes a range of powers and responsibilities in respect of consumer laws such as unfair trading, as well as conventional competition enforcement. Numerous regulations of goods and services prescribe mandatory contract terms and rights for consumers. Regulations now both establish rules that actors in the market must follow and provide for regulators such as the CMA to bring enforcement action against those considered to have violated the rules.

This kind of regulation is still broadly consistent with the idea of regulation to address market failure and the imbalances of power and access to justice that may prevent consumers from being able to pursue their rights in the courts. Other aspects (such as the Public Sector Equality Duty) are more obviously political or redistributive in nature and seek outcomes that the courts, in interpreting and applying the law, cannot be concerned with. It is not clear however that such interventions in the name of fairness for consumers actually deliver better welfare outcomes. Moreover, they may have anti-competitive effects by raising barriers to entry and crowding out innovation and diversity in how goods and services can be delivered to consumers. There is also a risk of 'learned helplessness' with consumers becoming infantilised, expecting that the state will take care of protecting their (and their children's) interests such that they do not need to conduct their own assessment of providers' suitability and terms of business. This moral hazard not only risks leading to a diminution in people's natural capabilities, but also may lead to them inadvertently being exposed to more risk, as relying on regulation and regulators in substitution for their own prudence and judgment will in many cases not offer the assumed protections (Hewson 2019b).

Who regulates?

> The greatest danger to liberty today comes from the efficient expert administrators exclusively concerned with what they regard as the public good.
>
> F. A. Hayek (1960)

The volume and complexity of regulations in modern states means that it would not be possible for them to be passed as primary legislation, subject to debate and voting in Parliament. It is also considered to be beneficial to have regulators who are independent from government, staffed by experts in the field, to oversee the implementation (by way of producing subsidiary rules and guidance) and enforcement of regulations (Majone 1994). This is seen to legitimate the delegation of powers from elected representatives and improve the quality of decision making, both by the regulator itself and as a result of advice they provide to ministers on future law and regulation. Taking technical matters out of politics is held to reduce the risk of decision making and administration being carried out in a politically opportunistic way. However, the design of regulatory structures is itself a political act, and it has also been suggested that the concept of regulatory independence appeals to politicians because, once established, these structures are hard for successor governments to unpick (Deller and Vantaggiato 2014). This both encourages investment by creating a stable environment that is not subject to electoral cycles and entrenches the preferred approach of the government that is able to establish it.

Regulators are established and given powers by statute. Regulators can take many forms, such as executive agencies, non-departmental public bodies, and non-ministerial departments, which have varying powers and governance structures. Powers can include making rules, producing

guidance, collecting and maintaining data, investigating breaches and issuing sanctions such as fines or suspensions for non-compliance.

Regulators' decisions, and the decisions of ministers establishing them are subject to judicial review by affected parties but only on narrow, procedural grounds and not 'on the merits'.[18] Some regulators have specific appeal mechanisms, such as a special tribunal or reference to the ordinary courts but in the absence of such a designated route, there are few remedies available to counter poor decision making.[19] The Parliamentary Ombudsman provides a service to resolve complaints about government departments and other UK public organisations, but it is not an appeals mechanism.

> In the UK, regulators are appointed not elected. It is possible to have elected regulators; the Public Utility Commissioners in some states in the US are elected, and in some cases this has been shown to deliver more favourable outcomes for consumers in the regulated market. However part of the purpose of independent regulators in the UK and EU system is to remove the subject matter of their role from 'majoritarian' influence (Lodge 2008).

In its influential 2007 report on UK Economic Regulators, the House of Lords Select Committee on Regulators recommended that:

- Independent regulators' statutory remits should be comprised of limited, clearly set out duties and that the statutes should give a clear steer to the regulators on how those duties should be prioritised.
- Government should be careful not to offload political policy issues on to unelected regulators.

This was in response to concerns that regulators were being given general and ill-defined duties to act 'in the public interest'. The Committee noted

18 Although increasingly with the development of human rights law, more substantive review is possible, which also has implications for democratic accountability, as the suggestion is that judges can substitute their own view of the 'right' decision, based on a particular reading of human rights.

19 In instances where an appeal process is available and a decision can be reviewed on the merits, the complexity of the rules and associated guidance and forms and the regulators' own failures to understand the laws and rules that they are responsible for enforcing have come to light, see for example *Grimes v Electoral Commission*.

that ‘The scope of regulators’ duties is more likely to be kept manageable if one recognises that matters of social equity and distributive justice are often best addressed, essentially by Government and Parliament, through other means such as the tax system.’

One of the first deliverables of the Regulatory Affairs Programme will be to inventory regulators operational in the UK and their statutory objectives to assess whether these recommendations have been put into effect.

The recent development of the role of some regulators (unofficially assumed or formally appointed) as advocates for regulation in their field or funders of activism by others suggests that this may not be the case. It also acts against their ability to conduct fundamental appraisal of their effectiveness by way of Post Implementation Reviews (described below) and contributes to the phenomenon of ‘policy laundering’ or ‘sock puppetry’ (Snowden 2019).

Regulators comprise a diverse collection of entities and acronyms, and we have set out a basic taxonomy in Appendix 1. While regulations can be made and enforced by local government, and by private, self-regulatory bodies, the Regulatory Affairs Programme will focus on national, central government bodies.

Is it working?

> One of the great mistakes is to judge policies and programs by their intentions rather than their results.
>
> Milton Friedman (1975)

The question of whether our regulatory state is working goes to the heart of the much rehearsed political debate on red tape. Are regulations stifling innovation and driving small businesses into the ground or are rapacious corporations seeking deregulation so they can exploit people and the environment with impunity? Perhaps a better way to approach the issue, and a question that the Regulatory Affairs Programme intends to consider in depth is: are the stated policy objectives being achieved, and if so at what cost?

Many initiatives are in place to assess these questions, both before and after regulations are passed. Government departments and regulators undertake cost-benefit analysis-based impact assessments (IAs) before taking action; numerous initiatives and mechanisms are in place to provide transparency and accountability; think tanks and academic studies have also sought to measure the extent and cost of regulation. But the costs assessed by regulators and the Regulatory Policy Committee include direct costs to businesses only. The estimated costs often seem to be based on superficial analyses, resulting in minimal costs being asserted that do not reflect the ever greater legal and administrative costs that result from successive layers of regulation. IAs do not include wider costs from effects on competition or innovation. They do not, and perhaps cannot, include the cost to individual freedoms and the rule of law.

To assume that governments and regulators are capable of correcting market failures attributes to them the possession of information and

qualities of judgment and disinterestedness that no person or body possesses. In many cases the problems that regulations seek to address arise not because of market failure but because of the absence of a competitive market (often as a result of government intervention), so the 'market failure' justification comes under some strain. The interventions it is used to justify rarely move towards actually improving the operation of the market in question.

The value of having decisions made by experts and taken out of politics has been questioned by public choice economists on the basis that such experts themselves can never be free of bias and self-interest and are vulnerable to 'capture' by vested interests seeking to influence regulation in a direction that benefits incumbency. Fears have been raised more recently that the increasing number of regulations and complexity of the regulatory state, and the inability of government and regulators to manage it and voters to hold them to account, threatens democratic legitimacy. At the same time, 'increasing the complexity and increasing the responsibilities of regulators may be a deliberate tactic employed by special interests to reduce the effectiveness of regulatory enforcement' (Tanzi 2011). For established businesses, rather than competing in the market, regulation can be used strategically (Veljanovski 2010):

> Investing in rule change can be as lucrative as maximising profits within the rules. It often 'pays' the industry to invest in trying to influence and respond to legislators and regulators to gain favourable regulation, or to minimise the impact of unfavourable regulation.

Nigel Lawson (Chancellor of the Exchequer at the time) recalls that the establishment of the new regulatory system for financial services after the Big Bang was not intended to 'seek to achieve the impossible task of protecting fools from their own folly, but should rather be no greater than is necessary to protect reasonable people from being made fools of'. The regulatory system that emerged, however, 'was far more cumbersome and bureaucratic than any of us in government had envisaged. Paradoxically, the involvement of practitioners in the regulatory process, which was intended to avoid this, probably exacerbated it' (Lawson 2016).

Insufficient or weak regulation is widely blamed for financial scandals and crises, but it can be argued that poor law-making and regulatory decisions of the state exacerbate scandals and instability, and that private, market-led regulation could deliver better outcomes (Booth 2019).

Despite the guidance in the government's Better Regulation Framework that regulation should not be presumed to be the answer to a problem, and that non-regulatory alternatives should also be considered, the NAO has found that policy makers favour regulation because they have poor knowledge of alternatives and wish to demonstrate they are taking decisive action. It is an obvious feature of democratic politics that politicians will wish to be seen to be taking action in relation to matters of concern to voters. The focus on form and procedural propriety by those who seek to hold the regulatory state to account distracts from these substantive questions.[20]

Department for Business, Energy and Industrial Strategy (BEIS) guidance provides that Post Implementation Reviews (PIRs) should assess whether a regulation:

- has achieved its original objectives;
- has objectives that remain appropriate;
- is still required and remains the best option for achieving those objectives; and
- could be achieved in another way which involves less onerous regulatory provision to reduce the burden on business and/or increase overall societal welfare.

PIRs are sometimes mandated by the statute under which a measure was brought in, but they are rarely and patchily carried out (NAO 2016).

20 See for example the House of Lords reports from 2006.

How much does it cost?

The cost of regulation to the UK economy as a whole was estimated by the Better Regulation Task Force to be around £100 billion per year in 2005, based on extrapolation from work in other countries that concluded that regulation costs between 10 and 12 per cent of GDP. If regulation had remained at a similar relative level, this would put the annual cost today at around £220 billion. This measure does not include benefits of regulation, such as improvements to the environment, economic gains from competition law enforcement or consumer confidence. Conversely, RIAs estimate direct costs of compliance and administration and do not include wider economic costs, but they do attempt to quantify wider economic and societal benefits from proposed measures. Establishing a meaningful, macro-level cost of regulation across the UK economy is a challenge that the Regulatory Affairs Programme will return to.

One of the most influential methodologies for estimating the impact of regulation on aggregate economic output was 'The Cost of Federal Regulation to the U.S. Economy, Manufacturing and Small Business' by W. Mark Crain and Nicole V. Crain, published in 2014 as a report for the US National Association of Manufacturers. It applied a 'top-down' approach to try to capture the cumulative impact of federal regulation in the US beyond the direct costs of compliance, in recognition that indirect costs arising from reduced investment were not being included in official measures. They used panel data for OECD countries from the World Economic Forum's Global Competitiveness Report to estimate GDP effects of regulation and found an impact of $2.028 trillion in 2012, an amount equal to 12 per cent of GDP. They also found that the costs fell disproportionately on smaller businesses.

The Crain and Crain methodology was used by the Institute of Public Affairs in Australia to calculate the cost of regulation as part of its Cutting Red Tape Project (Novak 2016).

There have also been efforts towards measuring the volume and restrictiveness of regulation. The RegData project at the Mercatus Center of George Mason University (Al-Ubaydli and McLaughlin 2014) uses a custom-made computer programme that leverages data science and machine learning and examines the regulatory text itself, counting the number of binding constraints or 'restrictions', words that indicate an obligation to comply such as 'shall' or 'must'. This creates a more precise metric because some regulatory programmes can be hundreds of pages long with relatively few restrictions, while others have only a few paragraphs with a relatively high number of restrictions. It can be applied to industries and time periods to 'examine the growth of regulation relevant to a particular industry over time or compare growth rates across industries'. The outputs from this measurement can be used in various ways: with quantified regulations for all industries users can test whether industry characteristics—such as industry growth, dynamism, employment, or a penchant for lobbying—are connected to industry-specific regulation levels'. This powerful tool has been applied in the US, Australia and Canada.

The Regulatory Affairs Programme will be exploring these models, but before considering the macro-economic costs we will establish an empirical base of what the current regulatory state comprises and whether the regulators and regulations concerned are delivering positive outcomes. We are also concerned not only with narrow economic costs and benefits, but also with wider implications for freedom and democracy, which are not easily captured by economic modelling tools.

Rule of law

There is a great deal of jurisprudential debate as to the definition of the rule of law. For Hayek (1944), the rule of law meant that:

> government in all its actions is bound by rules fixed and announced beforehand — rules which make it possible to foresee with fair certainty how the authority will use its coercive powers in given circumstances and to plan one's individual affairs on the basis of this knowledge… the discretion left to the executive organs wielding coercive power should be reduced as much as possible.

Joseph Raz (1979) set out a list of requirements:

> [A]ll laws should be prospective, open, and clear; laws should be stable; the making of laws should be guided, open, clear, and general rules; the independence of the judiciary must be guaranteed; natural justice must be observed; courts must have reviewing power over some principles; courts should be accessible; and the discretion of crime-preventing agencies should not be allowed to pervert the law.

Some argue that the concept goes further than these formal and procedural elements (known as a 'thin' conception of the rule of law) and includes substantive justice and moral or human rights (known as a 'thick' conception of the rule of law and endorsed by such distinguished thinkers as Dworkin and Lord Bingham). But proponents of the 'thick' conception also accept that the procedural framework aspects described by Raz, or something close to them, are an intrinsic part of the rule of law. While there are differing views as to whether substantive matters such as adherence to democracy and human rights are part of it, the rule of law is broadly accepted as a

foundational principle of a free society.[21] Hayek held it to be an absolute requirement, without which a society cannot be considered to be free (Hayek 1960). Raz considered it to be a virtue, but one among many that a legal system can strive for, and which can be subject to qualifications and trade-offs in pursuit of other values. Even if one accepts that departures from the rule of law by government may be justifiable, the burden of proof that such justification exists and that the proposed action does not exceed it should be strict and rest with the proponent of the measure.

It seems clear at the outset that many regulatory measures and institutions offend against principles of the rule of law. Formal rules are complex and voluminous, making it difficult for individuals to exercise their rational autonomy and form judgments on the courses of conduct available to them.[22] There is a lack of substantive mechanisms for review of regulated entities. Regulators often have broad discretion in enforcement of rules that are so wide ranging and difficult to comply with that they must be selective in whether and how they act on violations.[23] Limited resources constrain what regulators can do, but the prospect of providing them with sufficient resources to comprehensively monitor and enforce the rules that they are responsible for is also unappealing in a free society. As a result we have a regulatory state that is both intrusive and ineffective, imposing burdens that reduce freedom and threaten the rule of law, yet failing to achieve welfare gains that might justify such intrusions.

21 Although Marxists, for example, would reject this.

22 The availability of independent legal advice mitigates this, but the cost of obtaining legal services contributes to the advantage that large, established businesses have in regulated fields.

23 See for example the Regulatory Action Policy published by the Information Commissioner's Office.

Conclusion and next steps

Even if one accepts the prevailing expansive definition of market failure, the question remains as to whether state intervention by way of regulations, taxes or by government provision of goods and services is the way to correct such failures. The state does not itself possess the complete information needed to achieve what the market cannot, and (no matter how many 'independent' regulators it appoints) is not free of self-interest, or influence from vested interests. An abundance of complex regulations and powerful regulators threatens the rule of law and, therefore, the legitimacy of government measures. It is also counterproductive to other aims of governments such as counteracting the dominance of large firms, which ultimately benefit from the barriers to entry that arise from regulatory complexity. But this does not mean that the state has no role to play and there should be no regulation; rather that regulation and regulators should be challenged and assessed against criteria of effectiveness and respect for, at least, the basic principles of the rule of law.

The Regulatory Affairs Programme will:

- Create a database of regulators, their powers and accountabilities.
- Produce detailed studies of individual regulators to assess their performance and the necessity/value of the regulations they oversee.
- Inform the debate on regulatory aspects of the negotiation of the future relationship with the EU in the course of 2020, free-trade agreements with other countries and the proposed development of free ports.

It is hoped that the programme will develop into a hub for contributions from different specialisms and sectors in recognition of the wide scope of

the topic, as programmes such as the Regulatory Transparency Project in the US and the Cutting Red Tape Project in Australia have done.

The programme will endeavour to show that deregulation is possible and identify where and how it should be targeted. The regulatory database will expose the sheer quantum of the problem - as well as providing a resource that does not currently exist. Our research papers will examine, in a systematised manner, individual regulators or industry sectors where multiple regulators operate, offering specific assessment and recommendations as we go. In combination, the work will inform the media and the wider public about current levels of regulation, the trajectory of regulation, and the impacts of excessive regulatory intervention which could be making us poorer and infringing our fundamental freedoms.

Appendix 1: Taxonomy of regulators

The UK government lists 408 currently operational agencies and other public bodies, 20 non-ministerial departments and 12 public corporations.[24] In 2008, the Taxpayers' Alliance calculated that there were 1,148 'semi-autonomous organisations formally sponsored or overseen by British Governments' (Farrugia and O'Connell 2008).

Body or Organisation	Description
Formal terms as defined by the Cabinet Office	
Central Government	Central Government covers all administrative departments of the State and other central agencies whose effect extends over the whole economic territory (in this case the whole of the UK).

24 https://www.gov.uk/government/organisations

Devolved Administration	Devolution in the UK created the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly. Varying levels of power have been transferred from the UK Parliament to the devolved legislatures. Pursuant to the EU legislation that underpins the classification of public bodies, the ONS has determined that the devolved administrations fall within the Central Government classification. The powers to establish public bodies in devolved areas has been transferred to the devolved administrations, so their ultimate form and governance structures will be determined by the devolved administrations themselves.
Local Government	Local governments make and carry out decisions on local services. Many parts of England have two tiers of local government: county councils and district, borough or city councils. In some parts of the country, there's just one tier providing all the functions, known as 'unitary authorities' (including cities, boroughs or county councils). As well as these, many areas also have parish or town councils. Some of these have established their own public bodies: non-profit institutions controlled by local government and whose competence is restricted to the economic territories of the local government. Examples include Transport for London.

Public Sector	The 'public sector' is defined by the Office for National Statistics ('ONS') with reference to the European System of Accounts 1995, in accordance with EU requirements for governments to produce accurate public sector finances and national accounts. The National Accounts (or Sectoral) classification of entities as public or private depends on the level of government control over the general corporate policy of the entity being classified. This can be direct or indirect and may be evidenced by indicators that include: the ability to appoint those in control, or those who determine the policy of the entity; and/or a right to be consulted over such appointments, or to have a veto over appointments; and/or the provision of funding accompanied by rights of control over how that funding is spent; and/or a general right to control the day-to-day running of the body.
Public Body	A 'public body' is a formally established organisation that is (at least in part) publicly funded to deliver a public or government service, though not as a ministerial department. The term refers to a wide range of entities that are within the Public Sector. This does not include forms of public entity that do not require staff to carry out their functions, such as public funds or trusts.
Arm's Length Body	A specific category of public bodies that are administratively classified by the Cabinet Office. ALBs include: Executive Agencies ('EA'), Non Departmental Public Bodies ('NDPBs') and Non Ministerial Departments ('NMDs').

Non-Ministerial Department	A public body that shares many characteristics with a full department, but without a minister and acts separately from any sponsoring department. NMDs operate similarly to normal government departments in the functions they perform (though usually they are more specialised and not as wide ranging in the policy areas they cover). They generally cover matters for which direct political oversight is judged unnecessary or inappropriate. They are usually headed by a senior civil servant as Chief Executive, with an independent Chair and non-executive directors for the board. Some are headed by a permanent office holder, such as a Permanent Secretary or Second Permanent Secretary. Examples include bodies as diverse as the Supreme Court and HMRC.
Executive Agency	A public body that acts as an arm of its home department. Executive Agencies are clearly designated (and financially viable) business units within departments which are responsible for undertaking the executive functions of that department, as distinct from giving policy advice. They have a clear focus on delivering specified outputs within a framework of accountability to ministers. While they are managerially separate, they are independently accountable within their home department, which also reports to Parliament on their agency-specific targets. Due to this close working relationship, executive agencies are part of their department, and do not have the same level of legal separation from their home departments that other categories of public bodies often possess.

Non-Departmental Public Body	A public body that operates separately from its sponsoring department. Can be Executive or Advisory. NDPBs have a role in the process of national government but are not part of a government department. They operate at arm's length from ministers, though a minister will be responsible to Parliament for the NDPBs. The category also includes NDPBs with advisory functions, and Independent Monitoring Boards. Examples include the Committee on Climate Change, the Competition Appeals Tribunal and the Independent Commission on Civil Aviation Noise.
Public Corporation	Any public entity that is at least 50 per cent funded through commercial activities will be classified by the ONS National Accounts system as a Public Corporation.
Task Force and Department's Office	Distinct entities that form part of government departments. They are usually set up for a specific project or initiative, with dedicated teams with departments. They do not have executive agency status (and do not have the governance structures or the operational autonomy of an executive agency). They are staffed by civil servants and work within the rules and processes of their relevant home department. A small number of offices and taskforces are cross-cutting (and bring together staff and policy responsibilities from different departments). Some offices have non-executive Chairs and/or members who provide strategic direction, advice and leadership. These are usually appointed by ministers.

Working Group	Part of government departments, they are not independent advisory entities such as Advisory NDPBs or Expert Committees (both of which are operationally independent in terms of the advice they gather, analyse and present). Working groups comprise Stakeholder and Public Sector groups. Stakeholder Working Groups are internal entities that advise departments on the basis of representation from specific sectors, industries, professions and communities. They comprise a majority of representatives of organisations and (generally) not individuals appointed in a personal capacity because of their specific skills and experience. Public Sector Working Groups are departmental or inter-departmental working groups comprised mainly of civil servants and or wider public servants that advise their departments on specific (sometimes cross departmental) issues. In both instances there can be an independent chair and independent members, but the majority must be comprised of representatives/ ex officios.
Expert Committee	Usually non-statutory groups, providing independent expert advice on key issues from within the department. Like many of the NDPBs that possess an advisory function, Expert Committees are comprised of external (non-civil service) specialists that form committees to advise ministers on particular policy areas. However, they are not ALBs like NDPBs. They are funded from within a department budget, administrated and resourced by civil servants from within the department, and are not subject to the same levels of review or scrutiny that ALBs require.

Statutory Office Holder	A position established under legislation (in some instances by a prerogative Order in Council) and sometimes as a separate legal entity or corporation sole, with a specific remit to conduct activities or deliver services within the public sector but which is an individual and not an organisation. The statutory office is a position held by one person, the statutory office holder, though the office may be provided powers to request additional resources if required (these would usually be provided by a department or by Parliament) or to employ staff. Examples include the CIC Regulator and the Public Appointments Commissioner.
Parliamentary Bodies	Public bodies set up by, and usually reporting directly to, Parliament (typically via one of its Committees) and not to a government department or minister. They often deliver functions or services that are viewed as of particular importance to Parliament, or requiring even greater distance from ministerial control. They are often set up with similar structures and powers as other public bodies, though their governance processes are usually more focused on political independence and accountability to Parliament. Usually they will be staffed by public servants, with senior appointments made by or with Parliamentary involvement or oversight. Statutory Office Holders can be established as parliamentary bodies as well as by departments. Examples include the National Audit Office and the Parliamentary Standards Authority.

Informal terms	
Quango	An acronym that stands for Quasi Autonomous Non-Governmental Organisation. It broadly covers all ALBs.
Tsar	Independent policy adviser from outside government, appointed by a minister. Appointments of Tsars became popular in the 1990s under the Blair government and hundreds have been appointed since. While it is recognised that they often make useful contributions, concerns have been raised about transparency and governance in their appointments (Levitt and Solesbury 2013).

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