UK- The Netherlands

Indicators of Regulatory Reform in the EU – Some Initial Thoughts

This paper first of all describes EU experience with the use of indicators up till now. Given this context, it then considers what use might be made of indicators of better regulation, and the attempts that have been made so far to construct such indicators. Because of the widespread influence of regulation, indicators of regulatory quality could potentially be very useful, but, for the same reason, unambiguous indicators are particularly tricky to construct. Finally, the paper lists some potential indicators, both of the regulatory process and of regulatory outcomes.

The context: broader work on indicators in the EU

The Lisbon European Council mandated the Commission and the Council to develop indicators to measure progress on the Lisbon agenda of economic reform. The Commission tasked EuroStat to produce indicators, and they update them periodically throughout the year. ECOFIN took on this work for the Council and handed the work on to the Economic Policy Committee who set up the structural indicators working group.

The EPC originally envisaged a hierarchy of indicators, covering three tiers. The top-level indicators were to cover large-scale areas covered by the Lisbon process, to be examined by Heads of State and Government. These now feature in the annual Spring Report. The second tier were to cover economic indicators within economic processes such as the Broad Economic Policy Guidelines. The third tier would comprise the specific indicators relating to issues covered by Council Working Groups.

A list of about forty top tier "structural" indicators was taken up for use in the Commission's Spring report (in consultation with the EPC). This analyses progress on the Lisbon strategy in detail and covers the five domains of Employment, Innovation & Research, Economic Reform, Social Cohesion and Environment, as well as some general economic background indicators.

The Member States' Cardiff Reports include a section on regulatory reform but there is little or no prescription about what should be included: since Cardiff is a peer review based on the open method of coordination they can at most encourage uptake by other Member States. Each MS annexes its own list of indicators, chosen independently, mostly headline ones, to its Cardiff Report. The Commission (DG Markt) also produces a Cardiff Report on the functioning of product and capital markets using indicators provided by EuroStat extracted from the Competitiveness Council Conclusions. The MS Cardiff reports, the Commission Cardiff report, other analyses, and the country fiches to the Commission's BEPG implementation report are incorporated into the EPC's Annual Report on Structural Reform, which then feeds into the Spring Council alongside the Commission's Cardiff report.

Thus, the Commission's Spring report and the EPC's Annual Report on Structural Reform both feed into the Spring Council. Indicators are not seen as telling the whole story but are used to illustrate or enhance the qualitative conclusions arrived at by the various groupings.

The Use of Indicators of Better Regulation

The Lisbon Council recognised the importance of regulatory reform as a necessary means for improving European competitiveness when it mandated the Council and Commission to develop a regulatory reform strategy. This was elaborated by the Gothenburg Council in June 2001, which emphasised the importance of good regulation in securing environmental, social and economic goals. This mandate was amply fulfilled by the Mandelkern Group's report in November 2001 and by the Commission's Action Plan of June 2002 for improving and simplifying the regulatory environment, together with its February 2003 Communication on regulatory simplification. The importance of better regulation to the EU was re-affirmed and the necessary institutional conditions were established by the Inter-Institutional Agreement on Better Regulation, on which political agreement was reached in June 2003 and which, after signature during the Italian Presidency, will enter into force in 2004.

Although some important details are still to be elaborated, the strategy and tools for better regulation in the EU are, therefore, largely in place. What remains is the continuing and vital task of ensuring that these tools result in a simpler and more efficient regulatory environment in Europe. Thus, there is potentially an important role to be played by indicators of better regulation, in assuring Council, Parliament and the European public that regulatory reforms are going ahead and producing results.

It is the diffuse and pervasive influence of regulatory quality that makes regulatory reform so important for macro-economic performance and for sustainable development. But it is this same quality that makes it unusually difficult to identify indicators that can unambiguously show the effects proceeding from the regulatory framework. For this reason the structural indicators used so far in the EU do not include measures of regulatory quality (although some of the indicators, for example those for employment, patents and the network industries, can be seen to be heavily influenced by regulatory conditions).

The Mandelkern Group appreciated the importance of indicators when it commissioned Per Samuelson, supported by a sub-Group of experts, to produce a paper on indicators of regulatory quality. This provided a useful description of the issues and possibilities involved, making the important distinction between indicators of the quality of the regulatory process and indicators of the quality of the regulatory outcome. It did not attempt to develop operational indicators and its main insights were incorporated piecemeal into the Mandlekern Group's report, which, in developing a regulatory reform strategy, had a different emphasis.

It is worth, at this point, noting the pioneering work of the OECD in identifying and listing the institutional requirements for good regulation, which it has continued to use extensively in its country peer reviews and other work. The OECD also devised composite indices showing the regulatory freedom of the product and labour markets in OECD countries as of 1998. This was meticulous work based on descriptions of the operation of these markets supplied by the countries concerned. Nevertheless, both in the interpretation of the data and in the construction of the indices there had to be a subjective element. Influential though these studies were, the Secretariat has not been asked to repeat them.

Possible Indicators of Regulatory Quality

As mentioned already, one can distinguish indicators of the quality of the regulatory process and indicators of the regulatory outcome. Both are of interest.

Indicators of the quality of the regulatory process

A good regulatory process is not an end in itself. But if we are satisfied that regulation is based on a fair consideration of the evidence, including consultation with those whom it affects, then we can be more confident that regulation is being pursued only if it is necessary and if it has, on balance, a beneficial effect. And a systematic process of regulatory simplification indicates progress in reforming any obsolete or inapproriate regulation.

One way of assessing the quality of the regulatory process is to see if it embodies the institutional features necessary for good regulation, for example, a systematic regulatory reform programme, the use of impact assessment, consultation on regulations, a programme of regulatory simplification. This was the approach taken by the Experts Group chaired by Dr Karkatsoulis that produced a report in June 2003 for the Ministers of Public Administration on the implementation of the Mandelkern report. This was a valuable piece of work and showed that the practices recommended by the Mandelkern Group were being taken up by the Commission and by the vast majority of the Member States. It will bear repetition in the future, both to check on further progress and to expand the Member States considered from the EU15 to the EU25. Nevertheless, because of the relatively slow pace of change of institutional developments, this aspect will not need regular, periodic monitoring.

To see if the regulatory process is operating in an efficient way that is likely to produce good results, we need to go beyond a check on the institutional design, and look at how the process is operating. For example, if there is a system of regulatory impact assessment, what proportion of legislation is covered by it and how thorough is the assessment? Indicators that could be looked at in this way, for both Member States' domestic legislation and for the Commission's legislative proposals could include:

- Proportion of legislation subject to Regulatory Impact Assessment

- Quality and thoroughness of impact assessment
- Proportion of legislation subject to (formal) consultation
- Measures of regulatory simplification as a proportion of total legislation
- Proportion of the law book subject to codification

Few of these measures are able to be captured by simple statistics. There needs to be an element of qualitative assessment, to see to what extent these measures represent good regulatory performance in the particular circumstances of the country or institution, for example if they meet the goals set by the country itself. Thus, these indicators might be particularly suitable for peer review and for use by countries when compiling their own progress reports.

Intermediate Indicators: Ease of Compliance

Ultimately, regulations are designed to improve outcomes in the economy, environment and society. We shall consider in the next section the extent to which it is possible to trace the influence of the regulatory system on these macro variables. However, one can get valuable insights into the operation of the regulatory system by looking at intermediate indicators that show how easy it is for businesses and citizens to comply with regulations. In particular cases, indeed, one may be able to show that a costly or time-consuming process is necessary to achieve a particular social goal. But if we look at standard procedures or "life episodes" then, it ought to be the case that a well-designed regulatory system will impose the minimum burden of compliance.[1] Possible indicators could include:

1) Time, cost or number of permits necessary to start up a new company
2) Skills, professional qualifications or registration requirements to enter a particular business
3) Time spent dealing with tax and social security law
4) Time or cost spent dealing with inspections (fees, management time, number of inspections, number of different inspectors, form filling, etc)
5) Time or cost spent on compliance with Health & Safety, Fire Safety laws, etc
6) Time spent on data collection, surveys, questionnaires, etc by government, regulators, local authorities, etc
7) Time or cost spent in statutory consultation of employees

[1] This type of indicator has been used quite frequently, for example in the OECD study already referred to. Regular comparisons using this type of indicator are produced by the World Economic Forum in its Competitiveness Report and by the Heritage Foundation in its Index of Economic Freedom and will in future be produced by the World Bank in its Analysis of Doing Business. These are useful as showing what can be done, but none reflect a full range of regulatory effects.

8) Time, cost or number of permits necessary to employ the first employee
9) Time, cost or number of permits necessary to employ the nth employee
10) Time, cost or number of permits necessary to sack an employee
11) Restrictions on or legal rights to part-time, fixed-term or temporary contracts
12) Time, cost or number of permits necessary to expand premises, change their function or acquire new premises
13) Requirements for placing products on the market
14) Time, cost or number of permits for exporting non-military equipment
15) Sectors with price controls
16) Time and cost of patent applications
17) Bankruptcy law requirements.
18) One could also look for proxy measures for the cost to the private sector of operating within the regulatory system. For example one could try to identify the number of people in the private sector working on regulatory compliance – compliance officers, accountants, tax advisers, lawyers. In general, one would expect that the simpler and clearer the regulatory system, the less the need for such professionals to make it work. Even if cross-country comparisons were not straightforward, movements over time could be a good indication of how regulatory complexity was developing.

In deciding which indicators to use and how to measure them, it would be important to standardise so far as possible across countries. It would also be important to consider in advance whether the measure was picking up the effects of domestic legislation and administrative practices or the effect of Community legislation. Changes over time to indicators related to trade or the single market, for example, particularly if they seemed fairly uniform across countries, could probably be attributed to changes in the burdensomeness of European legislation.

It would also be a matter for decision whether one kept to a list of individual indicators or combined them into a few composite indicators, e.g. of employment regulations. The greater simplicity and power of composite indicators would have to be set against the loss of transparency and the subjectivity that would be introduced by any method of aggregation.

Another approach to this type of indicator is to use surveys, usually of businessmen, asking them about their perception of regulations, the time taken to comply with different regulations, or to rank regulations according to how burdensome they seem. Such surveys are always interesting but are unlikely to be satisfactory as more than supplementary indicators. There are all the usual problems with surveys: possible biases in the response rates; halo effects, whereby experience with one regulation influences perceptions of regulation in general; greater weight given to more topical regulation. When conducted internationally there is the additional problem that the initial starting point and expectations will vary considerably from country to country, which will influence the perceptions of what might, objectively, be identical changes. Where surveys are detailed enough to take account of the situation in particular sectors and where their quantitative results can be validated by face-to-face interviews, they will be more reliable: more general surveys are likely to yield only impressionistic results.

Indicators of regulatory effects

Ideally, one would like to be able to identify the effects of the regulatory system on the main macro targets, such as economic growth or employment. In practice, this is extremely difficult. Since these variables are already monitored as structural indicators, it would seem best not to duplicate that effort, but to ensure that in interpreting movements in these variables, due consideration was given to structural changes brought about by changes in regulation.

However, there are some partial indicators where the influence of the regulatory system would be expected to be particularly strong and these could be monitored to show how the effects of the regulatory system were developing. None of them will provide unambiguous evidence of regulatory effects, even in their limited domain, and for some of them one might have to make explicit allowance for the effects of the business cycle. Nevertheless, taken together, they could give an indication of whether the regulatory system was improving its performance. Examples of this type of indicator are:

- Sectors with barriers to entry/restrictions on number of competitors/licence holders
- Variation in annual hours worked by employees (a broader spread indicates greater choice and less rigidity of employment patterns)
- Variation in unemployment rate by age (a narrower spread indicates fewer regulatory barriers – e.g. a relatively high youth unemployment rate usually indicates excessive employment protection)
- Size of public enterprise sector as a percentage of the non-agricultural business GDP (excluding health, social services, education, etc)
- Concentration ratio (by sector)
- Imports as a percentage of GDP (for the EU as a whole)
- Foreign direct investment as a percentage of total fixed investment
- Number of start-ups as percentage of all firms (or relative to GDP)