



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

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Your ref:

Regulatory Budgets Consultation
Better Regulation Executive
3rd Floor
Dept of Business, Enterprise and Regulatory Reform
1 Victoria Street
London SW1H 0ET

Dear Sirs,

Regulatory Budgets: A Consultation Document

The ICAEW welcomes the opportunity to respond to the above consultation.

The ICAEW has been a consistent champion of the Government's Better Regulation agenda. However, we believe that the achievements to date are relatively limited. We welcomed the announcement of the intention to introduce regulatory budgets. We also recognise that the proposals are radical and that a fully effective system will take time to implement. We are concerned that there is a 'credibility gap' that needs to be bridged. Government needs to demonstrate its commitment to reducing regulatory burdens by engaging with stakeholders so as to ensure that a robust and reliable framework of regulatory budgets is created and long-term burdens reduced.

It has long been a concern of the ICAEW that the UK government and the EU commit to new regulations without evaluating fully:

- the true costs of policies;
- the effects on businesses; and
- the economic circumstances prevailing at the time of implementation.

The proposal to have a total budget approved by the Cabinet which covers all regulation, including policy costs, has great merit. If it is effective it will necessitate government to prioritise on regulatory proposals. The EU is currently engaged in the administrative burdens reduction programme through to 2012. We believe that if the regulatory budgets system, pioneered by the UK, is a demonstrable success, the UK should encourage the EU to adopt it so that similar pressures are applied at EU level.

Business' Views of the Current UK Regulatory Environment

The ICAEW researches its business members' attitudes to business issues in its annual *Enterprise Survey*. Respondents are mainly chief financial officers, finance

directors, or other directors, in businesses of all sizes, from FTSE 100 companies to micro entities. In 2008 for the first time we included members overseas – in the rest of the EU, the Far East (Malaysia, Singapore and Hong Kong) and the US.

The 2008 survey had findings relevant to this consultation. Firstly only 45% of UK chartered accountants rated the domestic regulatory and tax environment as “business friendly” compared with 48% for the rest of the EU, 66% for the US and 87% for the Far East.

Secondly among our UK members Employment legislation, Employment tax, Business tax changes and Health & Safety regulation are the most complained about and most costly to implement. Among the members in the rest of the EU the same four issues are broadly identified as hindrances although Business tax changes and particularly, Health & Safety legislation are significantly less of an issue. In all four areas the UK scores significantly worse than the US or the Far East.

It is apparent from our survey that the UK’s regulatory and taxation environment presents significant competitive challenges for UK businesses.

Attached is our response to the issues raised in the consultation as well as the specific questions.

If you require any further information please contact the undersigned.

Yours faithfully

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ICAEW Representation

ICAEW REP 128/08

REGULATORY BUDGETS: A CONSULTATION

Response submitted in November 2008 by the Institute of Chartered Accountants in England and Wales to a consultation on Regulatory Budgets issued by the Better Regulation Executive, Department for Business, Enterprise and Regulatory Reform.

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INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales (the Institute) welcomes the opportunity to comment on the consultation paper, *Regulatory Budgets* issued by the Better Regulation Executive, Department for Business, Enterprise and Regulatory Reform.

WHO WE ARE

2. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 130,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.
3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.

MAJOR POINTS

4. A Matrix is required linking departments with broad regulatory categories

The draft findings of the Anderson Review reveal the complex network of government departments and regulators involved in individual aspects of regulation affecting business. The Review found that “Businesses consider employment law to be one area (a view echoed in the Enterprise Survey above) but regulations are generated from 5 different departments (Department for Work and Pensions, Home Office, BERR, Government and Equalities Office and H M Revenue and Customs)”.

The review found that:

- 51% of SME employers find complying with employment law a challenge
- 41% of SME employers find it difficult to understand what their obligations are under employment law.

The review revealed similar findings for Health & Safety with 4 government departments generating regulations and 5 involved in enforcement.

The consultation proposes that each department be given a regulatory budget. The ICAEW believes that this will not achieve the change in business perception of individual regulatory demands as mentioned above. We therefore suggest that within the system of departmental regulatory budgets a matrix is established which monitors the costs under the above broad headings. We believe that it will add to the credibility of the system if the government can say that the regulatory cost of Employment Law has not increased in the budgetary period.

Given that two of the four topics which currently cause businesses most difficulty largely originate in the EU (Employment Law and Health & Safety) it

is vital that EU originating regulations are included within the scope of regulatory budgets.

5. Exclusion of HM Revenue & Customs

Section 4.5 of the consultation document states that tax measures are outside the scope of regulatory budgets because tax (as well as not being regulation in the classic sense) is already controlled through the financial budget process. HMRC already have targets to reduce the administrative burden on business and a programme to deliver that reduction. Those targets are in place until the end of 2010/11 and HMRC will be focusing on what it should be doing after that to maintain downward pressure on administrative burdens and compliance costs in the context of their broader agenda to deliver a better service for its customers.

We understand the rationale for this approach but it raises a number of issues which need to be addressed.

1. In section 2.7 of Annex A of the excellent KPMG report for HMRC on Administrative Burdens (20 March 2006) under the title "What the model does and does not cover" says

"The model only covers the administrative burden, the costs of doing something to comply with an administrative requirement set by tax regulation. It does not cover the much wider concept of compliance costs; in particular it does not cover:

- the cost of businesses dealing with change, whether of regulation or business model
- the cost of uncertainty
- the cost of working out whether to do something, more specifically the cost of working out not to do something

These are very important aspects of the total compliance cost and the perception of "red tape" .

The statement above goes to the heart of our concerns. The focus of the HMRC project is on the cost of the administrative burdens imposed rather than on the wider policy costs. The 2008 Enterprise Survey findings that "business tax changes" were regarded as a hindrance by 55% of respondents supports this point. The move to departmental regulatory budgets will place greater emphasis on total policy costs. We believe that this emphasis should apply equally to HMRC and we recommend that this aspect of the proposed policy is reconsidered and that HMRC is tasked with taking account of the wider costs.

2. The KPMG report has provided a valuable baseline for the measurement of administrative burdens. Whilst we appreciate that it was always intended to be a "one-off" project, we think that it would have been even more effective and useful if the project had been continued and measured the admin burdens imposed by tax policy changes that have been introduced subsequently.

3. The activities of HMRC come within the review of the Public Accounts Committee, the Treasury Committee and the Regulatory Reform Committee and there is therefore an element of public scrutiny of the regulatory burdens

imposed. Nevertheless, the departmental regulatory budgets system will provide improved opportunities for independent scrutiny by parliamentary committees. We recommend that the regulatory costs imposed by HMRC's are subject to clear lines of accountability and independent scrutiny in the same way as envisaged in these proposals, thus providing an added incentive for HMRC to participate actively in reducing the regulatory burdens on business.

4. There is a perception that HMRC has escaped lightly from these proposals and we are concerned that this could damage the credibility of the wider project. We accept that this perception is not justified, although as noted above we think that HMRC's targets should be linked more closely to this initiative. To help ensure that stakeholders have confidence in the wider proposals, we think that the reasons for HMRC's omission, namely that it is subject to its own demanding targets, should be explained in much more detail than they were in the consultation document.

6. Other Exemptions/ Scope for Flexibility

The proposal for departmental regulatory budgets is radical and we welcome the willingness to "think outside the box". However we are concerned at the number of other exemptions and the scope for flexibility particularly:

1. Climate change is excluded. Climate change will be an increasing concern for business and we see no reason in paragraphs 1.22 and 1.23 why it should be excluded. Government has other "key cross-Government priorities" which are not excluded.

2. We feel that having three mechanisms available to provide flexibility in response to emergencies and "unforeseen circumstance" is just too many and we would suggest that only one – a "centrally managed exceptional provision", which is a usual feature of commercial budgeting, would be sufficient.

3. Two other areas of concern

- ☐ Local authorities are excluded. Local authorities are responsible for the implementation and monitoring of many regulatory requirements.
- ☐ Hampton regulators governing boards are invited to opt into the regulatory budgets system.

The ICAEW believes that unless the above concerns, particularly the exemptions and options for flexibility, are addressed the credibility of the new regime will be devalued.

7 Measurement of the cost of regulation

The proposals will rely upon the "recently strengthened Impact Assessment regime" to provide the cost of regulation. The new Impact Assessment (I A) regime is still largely untested - we have concerns that sufficient post implementation reviews have been undertaken to test the effectiveness of the new IAs.

In addition the ICAEW has advocated that IAs need to be independently verified. The ICAEW will continue to advocate greater independence for the Better Regulation Executive and in particular the IA system. However we

recognise that this is a long term goal and in the meantime the attention will be focussed on making the Regulatory Budgets system effective.

8. Administrative Burdens reduction

The consultation proposes to integrate future work to reduce administrative burdens into the system of regulatory budgets from 2010 onwards. The ICAEW has advocated that policy costs should be included in the consideration of the cost of implementing new legislation / regulation. Accordingly we agree that subsuming the administrative burdens programme in the regulatory budget system would be the correct decision. However we would like to see the Administrative Burdens Reduction programme continue to be monitored and the results published. As the departmental regulatory budgets system becomes established attention will focus increasingly on that programme. In the meantime the Administrative Burdens programme maintains pressure on departments as well as contributing to the EU Administrative Burdens Reduction Programme which runs to 2012.

SPECIFIC QUESTIONS

9. Q1. Do you consider that the Government should proceed with a system of regulatory budgets as a way of managing the costs of new regulation?

Our research amongst ICAEW members suggests that the government's Better Regulation initiative has been a limited success. Provided the system of regulatory budgets is robust and palpably acts to restrain government's propensity to regulate the investment will be worthwhile. The acid test will be whether UK business perceives that government is helping them to compete rather than imposing additional regulatory burdens. In this sense the regulatory budgets system must be quickly established.

10. Q2. Do you think regulatory costs should be scored at the point of enactment or when they come into effect?

The ICAEW believes that regulatory budgets should be scored at the point of enactment. Implementation of regulation is frequently phased in (for example the 2006 Companies Act) which makes budgeting and monitoring difficult. Businesses start preparing for new regulation in advance of the date it comes into force.

11. Q3. What, in the range of three to five years, would be an appropriate budget period?

The ICAEW believes that the budget period should be three years. This facilitates alignment with the Comprehensive Spending Review periods. It also gives departments a shorter focus for complying with budgetary targets. Departments should publish annual reports on the cumulative costs incurred with forecasts for the remainder of the three year period.

Scrutiny of regulatory budgets and annual progress reports should be undertaken by the Regulatory Reform Committee and each departmental parliamentary committee.

12. Q4. What are your views on the possible system to manage regulatory budgets outlined in paragraphs 2.9-2.31? Would this deliver a credible and effective system of regulatory budgets?

In setting the regulatory budgets the government's primary consideration should be the additional costs to business in the context of the economic growth over the budget period. Budgets should incentivise departments to constantly search for cost reductions in order to pay for new regulatory costs.

As stated above the proposals need to be credible if they are to work. There should be no exemptions and flexibility should be strictly controlled. In our comments above we suggest a matrix so that business can see the budgetary picture for broad categories such as "Employment Law". Within that matrix, a system of departmental trading of regulatory budgets would be allowed.

We do not support overlapping final years. This should ensure the three year budget is absolute. Transparency requires that departments breach the budgets are required to publicly explain the reasons for the overspend.

The regulatory budgets system needs to be totally transparent. This requires regular reports (at least annual) in Departmental Reports and central reporting particularly of the matrix mentioned above.

Given the radical nature of the proposals we support the shadow roll-out to all departments and regulators commencing from April 2009. We also support further initiatives to exempt SMEs from new regulations, as they are disproportionately impacted by regulation and lack the resources to ensure compliance.

As mentioned above we support the integration of administrative burdens within departmental regulatory budgets but we would want to see continued reporting of the progress towards achievement of the 25% reduction target by 2010

13. Q5. Which forms of government action should be within scope of regulatory budgets?

The ICAEW believes that all regulations which impose a cost (policy cost or administrative burden) must be included in the budgets. This makes the inclusion of EU legislation essential.

There should be no exemptions. Any effective budget system applies pressure to cut costs and exemptions merely provide opportunities to defeat the system. A system of centrally monitored (and accounted for) exceptional provision within the overall budget is the maximum flexibility required.

14. Q6. Do you agree with the outline of this approach to EU and international originating regulations? Are there other issues to be addressed in the context of EU and international commitments?

We believe that it is right to include EU legislation to make the system credible. We are concerned how this might work in practice. What will be the basis for evaluation of the costs of EU legislation? We believe that, as EU Directives require UK legislation, the IA accompanying the UK legislation should measure the costs to be imposed on UK businesses. This will be

consistent with the methodology used of UK originated legislation. As there are often trade-offs between policy costs and administrative burdens this will allow great choice in implementing EU regulation.

15. Q7. Is the approach outlined in paragraphs 3.14-3.22 to costs arising from specific regulatory actions appropriate?

See Main points 4 to 9

16. Q8. What are your views on the approach set out in paragraphs 4.6-4.14 for treating independent regulators in a regulatory budget?

As we comment in Point 1 of our comments UK businesses view regulation as a whole category such as “Employment Law”. Consequently we do not believe any independent regulator should be excluded, particularly any regulator contributing to the four key areas mention in our introductory remarks.

17. Q9. Do you agree with the proposed categories of costs to include in a regulatory budget as outlined in Chapter 5?

We believe that regulatory costs should include all the costs associated with regulation impacting on business.

Public sector and public service delivery costs are distinct from the departmental regulatory budget.

18. Q10. What are your views on the proposed assessment methodology outlined in Chapter 6, including whether budgets should set on a gross or net basis?

We agree that the proposed budgetary system should be transparent, accessible, rigorous and consistent in its application. We support the proposition that regulatory budgets are set on gross cost estimates. Benefits should not be netted off against costs. We agree that benefits from regulations tend to be more uncertain and difficult to value in monetary terms than costs.

Research conducted by the ICAEW suggests that businesses respond to new regulatory requirements in different ways but largely according to the resources available. Generally larger businesses invest in systems and processes to minimise the on-going costs of compliance. Smaller businesses often invest less in systems and processes resulting in increased on-going compliance costs. This is one reason we support greater use of exemptions for SMEs. However transitional costs are as much a cost to the business and should be incorporated within the regulatory budgets system.

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