

# Strategies for Deregulation

## Concepts and Evidence

Steven Globerman





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## Executive Summary

Overall economic output in Alberta remains well below projections made before the late 2014 recession that battered the Alberta economy. While there are external factors influencing the provincial economy that are beyond government control, the provincial government can strengthen Alberta's economic recovery through pro-growth policy initiatives. One such pro-growth initiative is deregulation.

While there are well-known theoretical arguments for government regulation, there is also abundant evidence that government regulation often imposes substantial economic costs. Deregulation of sectors such as telecommunications and transportation has identified the substantial efficiency improvements and cost savings to consumers that can result from reducing or eliminating government red tape. The efficiency improvements go beyond reduced compliance costs and include gains from introducing new technology through increased capital investments and new business start-ups.

In principle, all regulations for which the expected social costs exceed their expected social benefits should be eliminated. In practice, applying this test to all existing regulations would be extremely expensive and time-consuming. A more expeditious initiative would involve identifying "non-functional" regulations for elimination. Suggested streamlined criteria for eliminating red tape by identifying non-functional regulations include whether the regulation under consideration effectively addresses a legitimate economic or social problem. If it does not, it should be eliminated. Regulations should also be eliminated if other laws or regulations deal with the problems they address, or if they cannot be applied in a predictable and consistent manner. Regulations are also candidates for elimination if private market institutions, such as stronger property rights, can solve relevant problems more efficiently.

The likelihood of successfully reducing red tape is enhanced by effective organization. The red tape reduction experiences of British Columbia and several other political jurisdictions highlight the importance of designating someone in senior government with a mandate to carry out the deregulation program, including overseeing the identification and elimination of non-functional regulations. Another feature of successful

red tape reduction initiatives involves tying the implementation of new regulations by relevant agencies to the elimination of some number of existing regulations following a prescribed rule, such as one that says no net costs should be created by new regulations.

Obviously, decisions about retaining or eliminating specific regulations should be evidence-based. Regulatory agencies should solicit the advice of experts, but the experts should have no direct or indirect financial interest in the outcome of the agency's evaluation. In addition, regulatory agencies should solicit opinions from stakeholders directly affected by specific regulations. Small businesses are important and usually knowledgeable stakeholders and their feedback should be regularly gathered to help identify non-functional regulations.

To be sure, some prominent and likely the more expensive regulations may not be amenable to analysis using streamlined criteria. Specifically, some regulations may not fail a screening for non-functionality while still imposing substantial costs on society. A retrospective evaluation of such regulations requires a benefit-cost analysis. To the extent that applying streamlined retrospective evaluations saves resources, regulatory agencies should benefit from an improved capability to do careful evaluations of a regulation's benefits and costs.

## Introduction

Beginning in late 2014, Alberta was battered by a deep recession. While the provincial economy has been in a recovery more recently, overall economic output remains well below pre-recession projections. While there are external factors influencing the province's economy that are beyond government control, the provincial government can strengthen Alberta's economic recovery through pro-growth policy initiatives.<sup>1</sup>

In particular, provincial government policies can influence Alberta's attractiveness as a destination for capital investment and skilled labour. Several specific policy areas have received substantial attention and detailed suggestions for reform. Tax policy, where Alberta has seen a substantial erosion of its former competitive advantage with regard to personal and corporate income tax rates, is a prominent example.<sup>2</sup> Other important dimensions of public management have received considerably less attention and fewer suggested options for policy changes. One such dimension is regulatory policy.

This study seeks to provide provincial government policymakers with an overview of "best practices" in the area of regulatory reform and, particularly, with regard to the removal of regulations that are likely to impose net costs on the provincial economy. While the primary objective is to identify policy initiatives to enhance the economic growth and industrial competitiveness of Alberta's economy by drawing on insights and empirical evidence from the literature on regulatory reform, the analysis should also be helpful for policy development in other Canadian political jurisdictions.

Government regulation plays a very prominent role in the economies of developed countries. It encompasses what economists identify as "economic" and "social" regulations (Crandall, 2008). The former refers to rules applied to prices, service quality, and entry conditions across a range of industries such as transportation, energy, and agriculture. The latter

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<sup>1</sup> In a companion study, Ken Green (2018) makes an economic case for pro-growth policies in Alberta

<sup>2</sup> For a discussion of Alberta's recent tax policies, see Eisen, Lafleur and Palacios (2017).

refers to the regulation of risks in areas such as health, occupational safety, and the environment.

Although there are well-known theoretical arguments for government regulation, there is also abundant evidence that government regulations impose substantial economic costs that take a variety of forms including reduced rates of capital investment and business start-ups, inefficient allocation of inputs, and slower productivity growth. The consequences can be substantial. For example, one relatively recent study found that regulations accumulated between 1980 and 2012 slowed US economic growth by one percentage point per year, primarily by distorting and deterring business investment that normally leads to increased productivity (Dawson and Seater, 2013). An earlier study for the World Bank (Loayza, Oviedo, and Sawyer, 2005) found that an increase of 10 percentage points in a country's regulation burden slows the annual growth rate of each citizen's personal income by one-half of a percentage point.<sup>3</sup> The Office of Management and Budget (OMB) in the United States estimated that less than half of one percent of all final rules issued by various agencies in the US government in 2016 imposed annual costs (in foregone GDP) of US\$74 to \$110 billion (in 2014 dollars). For OMB to evaluate a rule, it must be expected to cost over \$100 million and to have already been evaluated by a regulatory agency (Council of Economic Advisors, 2017).

Given the importance of a well-designed regulatory regime for economic growth and industrial competitiveness, it is important for Alberta's regime to be consistent with international best practice and informed by the success and failures of policy models implemented elsewhere. In this regard, a recent survey undertaken by the Canadian Federation of Independent Business (2018) raises concerns about Alberta's regulatory environment. Alberta stood out as a major outlier in the survey, receiving a grade of F for its regulatory environment.<sup>4</sup> Furthermore, Alberta never scored higher than a grade of D over the entire period from 2011 to 2018. It might be noted that Alberta's failing grade primarily reflected a lack of transparency and accountability, as opposed to the number and estimated costs of its regulations. However, companies doing business there have specifically identified Alberta's energy regulations as costly. For example, Green, Aliakbari, and Stedman (2018) report findings from the 2017 *Global Petroleum Survey*, which identifies the attractiveness of different states and provinces for upstream oil and gas investment. The authors note that in Alberta, 70 percent of investors cited the high cost of regulatory

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<sup>3</sup> For an extensive review of the literature on the impact of regulation on business start-ups and economic growth more generally, see Crews (2018).

<sup>4</sup> The Northwest Territories also received a grade of F.



compliance as a deterrent to investment compared to only 9 percent in Texas and 24 percent in North Dakota.

Perhaps responding to the criticism of its regulatory policies and practices, the Alberta Energy Regulator (AER) recently announced its intention to change substantially the way it regulates energy companies, including its processes, the way it makes decisions, and the way it communicates with its stakeholders (EY, 2015). Conspicuously absent from the AER's new regulatory paradigm is a commitment to retrospective evaluation of existing regulations with a view to eliminating regulations that do not serve the public interest.

Many economists have identified regular assessment of existing regulations in order to reduce red tape as a very important feature of regulatory reform.<sup>5</sup> The long-term buildup of rules in the absence of a culling process will result in an increasing number of obsolete, duplicative, ineffective or overly burdensome regulations that creates a growing hidden tax on business investment, innovation and entrepreneurship (McLaughlin, Ellig and Wilt, 2017). Given business concerns about Alberta's regulatory regime, the province is arguably a good candidate for a review of its existing regulations.

While politically challenging, some governments have attempted to implement retrospective deregulation, i.e., eliminating existing regulations based on an assessment of their actual and prospective net social costs.<sup>6</sup> The government of British Columbia made one such successful effort at deregulation, and the main features of this effort will be discussed in a later section of this study.<sup>7</sup> Another notable success was the deregulation of the US airline, railroad, trucking, and telecommunication industries under the Carter Administration.<sup>8</sup> An apparently less successful deregulation initiative is ongoing in the United Kingdom.<sup>9</sup>

The purpose of this study is to discuss how governments can address the challenge of regulatory accumulation or, more directly, how governments can successfully prune red tape.<sup>10</sup> Regulatory reform has typically

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<sup>5</sup> See, for example, McLaughlin, Ellig, and Wilt (2017).

<sup>6</sup> Arndt (2015) notes that while *ex ante* impact assessments are typically used for evaluating new regulations, most countries do not systematically conduct *ex post* assessments of existing regulations.

<sup>7</sup> The British Columbia government's deregulatory initiative is described extensively in Jones (2015).

<sup>8</sup> Other more recent US administrations have been much less successful in pruning red tape. See McLaughlin and Williams (2014).

<sup>9</sup> Bourne (2017) briefly discusses the UK experience.

<sup>10</sup> Removing red tape usually refers to identifying and removing regulations that

focused on using scientific and economic analysis to ensure that new regulations will accomplish policy objectives at a reasonable cost. McLaughlin, Ellig, and Wilt (2017) note that an equally important challenge for regulatory reform is to implement a rigorous and objective examination of cumulated regulations already on the books with the goal of eliminating those that fail to accomplish their social purpose. The primary challenge in this regard is to identify effectively and efficiently those regulations that are outmoded or inefficient. A related challenge is to implement an administrative structure that will promote the elimination of undesirable regulations. This study draws on concepts found in the literature on regulatory reform, as well as the deregulation experiences of several government administrations that have attempted to eliminate regulatory red tape.

The study proceeds as follows. The next section discusses possible criteria for pruning red tape. The section following it addresses issues related to structuring incentives and processes to promote deregulation. The final section contains a set of concluding comments and observations.

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have net social costs from the existing stock of regulations. In this essay, the terms “deregulation” and “reducing red tape” are used interchangeably.

# Identifying Non-Functional Regulations

McLaughlin and Williams (2014) divide regulations into two categories: functional and non-functional. Functional regulations address current and significant risks (or problems), mitigate at least some of those risks through compliance with the regulations, and do not have significant unintended consequences or compliance costs relative to their benefits. Those that are non-functional are missing one or more of these features. Non-functional regulations are obvious candidates for elimination, while functional regulations might still be candidates for elimination if they have net social costs.

## Benefit-cost analysis

Benefit-cost analysis is the gold-standard test for identifying whether any regulation, functional or non-functional, should be eliminated. Any economically justifiable regulation should promise a net social benefit in present value terms. That is, the expected monetary value of the stream of benefits over time discounted by an appropriate social interest rate should exceed the expected value of the stream of anticipated costs, also discounted by the social interest rate. If a prospective regulation, or an existing one, fails this test, it should not be implemented in the former case, or it should be eliminated in the latter case.

The characteristics identified by McLaughlin and Williams (2014), the absence of which makes a regulation non-functional, are readily linked to benefit-cost analysis, as discussed below. Indeed, their suggested characteristics can serve as a set of streamlined criteria for assessing the net benefits or net costs of regulations. Formal benefit-cost analysis is a time-consuming exercise. It also demands data and information that can be difficult to collect. The adoption of a less analytically demanding test for identifying regulations to eliminate can be complementary to more formal and time-consuming benefit-cost analyses. Streamlining the review of

regulations is a strategy for conserving and focusing resources on prominent regulations that are not highly likely to fail a formal benefit-cost test. Streamlining the assessment of regulations therefore makes it more feasible to study regulations having prominent economic consequences and uncertain net social benefits in a timely and careful manner. It should also accelerate the pace of the deregulation exercise.

## Criteria for streamlining assessment of regulations

Figure 1 lists a set of specific criteria that might be used to identify regulations that should be eliminated without necessarily undergoing a formal benefit-cost test. They are adaptations of criteria that have been put forward in numerous prescriptive studies of regulatory reform, as well as those suggested by McLaughlin and Williams (2014).<sup>11</sup> The first two were referenced earlier. Specifically, a regulation that does not address a legitimate problem or that fails to mitigate the problem, even if legitimate, is clearly non-functional, since it imposes costs with few, if any, social benefits. A problem might have been legitimate at the time a regulation was imposed; however, economic and technological changes may have rendered moot its legitimacy. A striking example is provided by telecommunications, for which the natural monopoly rationale for the regulation of telephone prices through rate-base, rate-of-return regulation was convincingly discredited by the growth of new communications technologies, including wireless and Internet telephony.

Rent control provides a classic illustration of a regulation ostensibly designed to address a legitimate social problem, i.e., limited housing affordability for low-income renters, but that actually exacerbates the problem it was meant to solve by discouraging the maintenance of existing housing units, as well as the construction of new units. It also creates incentives for people to rent more space than they otherwise would have if rents were determined in a free market. The consumption of extra space further limits the availability of rental options for low-income families.

Environmental regulations provide prominent examples of how the legal assignment of property rights, an element of the third criterion in figure 1, can effectively mitigate “commons problems” that are the justification for regulations aimed at preventing cost externalities. Indeed, in some cases the suspension of regulations allows for the spontaneous formation of market arrangements that help preserve environmental amenities, such as legalized hunting that discourages poaching and encourages invest-

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<sup>11</sup> See, for example, Ladegaard (2001), Government of United Kingdom Better Regulation Task Force (2003), and Competition Bureau (2016).

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## Figure 1: Streamlined Criteria for Identifying Non-Functional Regulations

- 1 The regulation does not address a legitimate economic or social problem.
  - 2 The regulation addresses a legitimate economic or social problem but does not effectively mitigate the problem.
  - 3 The legitimate economic or social problem can be addressed in a less costly manner than the current regulation, including strengthening the role of the market.
  - 4 The legitimate economic or social problem is addressed by another law or regulation at the same or different level of government.
  - 5 The regulation contradicts another law or regulation, which makes legal compliance with the regulation infeasible without violating some other rule.
  - 6 The regulation cannot be applied in a predictable and consistent manner.
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ments in expanding the stock of endangered species.<sup>12</sup> Penalties imposed by the market system, enforced by tort law, can also address many perceived problems related to workplace and consumer safety that might otherwise be justifications for regulations. For example, safety hazards discovered in consumer products can result in major losses in sales for the companies involved, which creates a strong incentive for companies to optimize the trade-off between safety and cost. Numerous additional examples can be cited of how problems can be solved relatively efficiently by market-oriented solutions rather than by regulations, thereby making the latter non-functional and candidates for elimination.

Regulations that address problems dealt with by other rules are clearly redundant, whatever the legitimacy of the risks or problems they are meant to address. As noted by criterion four in figure 1, such regulations should be classified as non-functional, since they offer no additional social benefits at the margin, but increase compliance costs. In a similar manner, as summarized in criterion five, regulations that contradict other rules or laws make legal compliance impossible for those covered by the

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<sup>12</sup> For a detailed discussion of how governments can address environmental externalities problems by creating marketable property rights, see Anderson and Leal (2001).

contradictory rules and laws. This is fundamentally unjust and causes people and companies to disrespect valid laws.

The sixth criterion in figure 1 underscores the fact that regulations whose enforcement is unpredictable because the regulations are vague, inconsistently enforced, or both, are likely to have very high compliance costs. When the application of rules by the regulator is uncertain, risk-averse organizations worried about violating regulations will likely adopt excessively costly safeguards to ensure that they are complying with regulations. They are also likely to discourage investments in assets that cannot be quickly liquidated.

The criteria listed in figure 1 are meant to expedite the deregulation process. There will certainly be regulations that are not readily classifiable as non-functional by those criteria and they may also have important economic consequences. For this latter set of regulations, benefit-cost analysis should be undertaken with the proviso that requisite resources and expertise are allocated to the analytical exercise. Whether one uses streamlined criteria or formal benefit-cost analysis to identify regulations for elimination, process is an important ingredient to the success of the deregulation exercise. The next section suggests some procedural and organizational features that make a successful deregulation initiative more likely.

# Organizing for Regulatory Reform

As McLaughlin and Williams (2014) discuss, most US presidential administrations have ended with more regulations in the *Code of Federal Regulations* than existed at the start of those administrations, notwithstanding executive proclamations that existing regulations would be reviewed and streamlined. This outcome partly reflects a failure to harmonize the incentives of the regulators with the goal of deregulation. It also reflects an inappropriate organizational structure that fails to assign clear authority and responsibility to specific offices within government, as well as to specific individuals, both of which are critical to implementing a deregulation agenda.

## Designation of responsibility and authority

Figure 2 helps organize the discussion in this section by listing a number of specific initiatives that are likely to make the deregulation process more effective and efficient. The initiatives listed in figure 2 draw heavily on the experiences of different political jurisdictions with deregulation, most notably the previously mentioned experience of the government of British Columbia. At the top of the list of recommended initiatives in figure 2 is the assignment of responsibility for deregulation to a senior government official. In 2001, the newly elected BC government appointed a minister of deregulation with the dual mandate of reforming the regulatory process and eliminating red tape (Jones, 2015). The appointment of a senior government official who has a mandate to reduce non-functional regulations, as well as regulations that fail formal benefit-cost tests, makes clear the locus of final responsibility for the relevant deregulation activities, as well as who is accountable for the outcome of those activities.

The success of the Carter Administration in its deregulation program was due in large measure to Alfred Kahn, who has been described as

## Figure 2: Organizing for Efficient and Effective Deregulation

- 1 A senior government official or government appointee should have an explicit mandate to carry out a deregulation program.
- 2 An independent commission or government department should be tasked with providing guidance and feedback regarding the identification and elimination of non-functional regulations.
- 3 The implementation of new regulations by regulatory agencies should be tied to the elimination of a given number of existing regulations following a prescribed rule or budget. Broad deregulation should also focus on reducing the stock of regulations.
- 4 Progress towards deregulation should be measured with reference to reductions in regulatory requirements.
- 5 Regulatory agencies should solicit opinions about regulations to consider for elimination, particularly from the small business community.
- 6 Regulatory agencies should invite public comment on regulations being considered for elimination. Agencies should submit their recommendations to the independent commission or government department with reasons for choosing to eliminate or maintain specific regulations. In all cases, the burden of proof should be to show why a regulation should not be eliminated.
- 7 Regulatory agencies should use best available evidence in making their decisions about retaining or eliminating regulations. Experts should be used only if they have no financial ties to the regulations being considered for elimination.
- 8 Benefit-cost analysis should be reserved for regulations with relatively large economic effects and/or that cannot be confidently eliminated using streamlined criteria.

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“Carter’s field general for deregulation.”<sup>13</sup> Kahn held the formal position of chair of the Civil Aeronautics Board (CAB) where he implemented major initiatives to deregulate the airline industry. Prior to his appointment as chair of the CAB, Kahn served as head of the New York State Public Service Commission, the regulator for electricity, gas, water, and telephones. In both positions, Kahn was a political appointee and not a member of government; however, and certainly in the case of his federal appointment, the head of government was clearly committed to regulatory reform and put someone in charge (Kahn) who shared that commitment. As such, the

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See Kahn’s obituary in Hershey (2010).



regulatory agencies that Kahn headed did not actively thwart deregulation, as might be typically expected.

While successful deregulation ordinarily requires the appointment of a senior government official with an explicit mandate to reduce red tape, it is unrealistic to expect a single government official to administer the entire deregulation process. At the same time, it is also unrealistic to expect regulatory agencies to initiate and implement deregulation activities in an unsupervised manner. As McLaughlin (2018) notes, regulatory agencies typically behave as if their job is to produce regulations rather than to produce socially beneficial outcomes. Hence, it might be beneficial to establish an independent commission or a small department within the executive branch of government to oversee the deregulation activities of regulatory agencies.

Obviously, duplication of activities between the commission or department and the regulatory agencies should be avoided to the extent possible. In the case of British Columbia, each regulatory agency was responsible for tracking, reporting, and monitoring its progress in the deregulation process. The minister of deregulation provided guidance, support, and feedback about which regulations were problematic (Jones, 2015). The criteria listed in figure 1 represent the type of simple guidelines that might be provided to regulatory agencies to help them identify non-functional regulations. The regulatory agency, on its own or following suggestions from the relevant commission or department, should evaluate specific rules that are candidates for elimination, while the commission or department would “sign off” on the regulatory agencies’ evaluations or request additional review.

## **Eliminating regulations as quid pro quo for new regulations**

Even with the oversight of an independent commission or government department, it is reasonable to expect regulatory agencies to resist participating in the elimination of regulations, even those that are evidently non-functional. Since the budgets of administrative agencies are typically tied to the scope of their activity coverage and the size of their workload, the pecuniary incentives of regulatory agencies do not align with a commitment to deregulate. One way to address this “moral hazard” problem is to require regulatory agencies to propose the elimination of one or more existing rules for every new rule implemented.<sup>14</sup> In the early years

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<sup>14</sup> Another arguably more complicated mechanism to address the moral hazard problem is for the government to set a maximum regulatory budget that does not

of British Columbia's deregulation program, two (and sometimes more) regulatory requirements had to be eliminated for each new one introduced, although sometimes even more than required were identified for elimination (Jones, 2015).<sup>15</sup>

While the British Columbia deregulation initiative was not mandated by legislation, Canada's federal government did implement a formal piece of legislation. Specifically, the *Red Tape Reduction Act* received Royal Assent on April 23, 2015. It fulfilled a commitment made in the federal government's October 2012 Red Tape Reduction Action Plan, which went into effect on April 1, 2012. The plan contained a one-for-one rule as part of its reform initiatives designed to make it easier to do business with regulators and improve service and predictability in the federal regulatory system (Canada, 2015a). Under the one-for-one rule, if a regulation is made that imposes a new administrative burden on a business, one or more regulations must be amended or repealed to offset the cost of an existing administrative burden on a business. The president of the Treasury Board is empowered to establish policies or issue directives about the manner in which the one-for-one rule is applied. The Governor in Council can make decisions regarding various elements, including how to calculate the cost of an administrative burden and the regulations that the Treasury Board may exempt from the application of the one-for-one rule (Canada, 2015b). It should be noted that no regulation is invalidated by reason only of a failure to comply with the act. Furthermore, the one-for-one rule must not compromise public health, public safety, or the Canadian economy.

This latter broad indirect exemption of activities is much more general than a strict benefit-cost defense of a regulation and potentially weakens the effective strength of the act.<sup>16</sup> The Centre for Policy Studies found that in 2011, 42 percent of all new regulations introduced in the United Kingdom fell outside the scope of the government's one-in, one-out policy, and this rose to as high as 50 percent in the first six months of 2012. As a partial result, the UK's National Audit Office estimates that \$10.4 billion of other new costs have been imposed on businesses outside the scope of the government's one-in, one-out policy, while only \$1.1 billion of costs have been reduced since 2015 (Bourne, 2017).

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necessarily increase with the workload of the regulatory agency. McLaughlin (2018) discusses the use of a regulatory budget.

<sup>15</sup> This requirement corresponds to item three in figure 2.

<sup>16</sup> In 2017, the US House of Representatives passed the *REINS Act*, which includes an amendment stating that for every federal regulation created, another must be amended or retired. The government of Canada's *Red Tape Reduction Act* was mentioned in the floor debate regarding passage of the *REINS Act* (Horn, 2017).

Bourne (2017) cautions that a focus on costs, as in the government of Canada's *Red Tape Reduction Act*, rather than on the number of regulations, is what really matters to successful deregulation. The relevant costs are those that regulations impose on private businesses and civil society organizations. Under a "numbers approach," a regulator might introduce a new regulation while eliminating an existing one with the net result of higher overall costs. The UK adopted a one-in, on-out rule in 2005 that Bourne says is better characterized as a "pound-for-pound" rule, since the rule mandated that no new regulation should impose additional net costs on private businesses and civil society organizations. The original rule was modified to a one-in, two-out rule, and then a one-in, three-out rule. When upgraded to a one-in, two-out rule, every regulation with a net cost had to be compensated for by regulatory removal or revision at double the monetary cost of the new regulation, and so on.

One of President Trump's first executive orders issued after his inauguration in January 2017 required all regulatory agencies to eliminate two existing regulations for every new one they adopt (Grubel, 2017). The objective is to ensure that the net cost of any new regulations is no greater than zero. The required number of regulations that must be eliminated for every new regulation introduced can be raised in the future by an amount determined by the Office of Management and Budget. The objective will presumably be to ensure that no net costs are introduced by new regulations. Trump's regulatory executive order has been criticized for focusing on slowing the flow of new regulations and not also on reducing the stock of existing regulations. It also limits the number of economic activities to which the order applies (Bourn, 2017).

## Focus of deregulation

The ultimate objective in reducing the number of regulations is to reduce the costs associated with regulatory requirements. In this regard, reductions in the number of regulations, or of the number of pages in the regulatory registry, may be misleading guides to the progress of the deregulation initiative. As described above, reducing the number of regulations might have no real effect on the cost burden of regulation if new regulations are introduced that effectively maintain the same number of regulatory requirements. It is therefore important for the independent commission or government department charged with overseeing the deregulation efforts of regulatory agencies to ensure that the regulations proposed for elimination focus on distinct and separate regulatory requirements.

It is not straightforward to measure the number of distinct regulatory requirements applying to different sets of businesses at any one time. Al-Ubaydli and McLaughlin (2014) discuss an algorithmic approach that uses computerized scanning of electronic regulatory registries to count the number of “requirements” imposed on businesses. A problem is that individual requirements identified may have different compliance cost implications, as well as different net social costs. Computerized counts of the number of requirements in electronic registries can give a reasonably reliable picture of whether regulatory requirements applied to a given industry are increasing or decreasing over time, but they cannot give a reliable measure of the cost reductions that are likely to be realized by eliminating specific regulations.

Hence, it is certainly appropriate to focus on costs as the relevant constraint when imposing one-in, one-out rules, or some variation, on the flow of regulations over time. Deregulation can therefore be implicitly achieved by adopting a rule that requires eliminating a number of existing regulations for every new regulation adopted sufficient to reduce the overall costs of regulation. To be sure, estimating the costs of new and existing regulations is likely to be only modestly less time consuming and difficult than doing a full benefit-cost analysis of new and existing regulations.

As a practical matter, however, while a focus on net costs seems appropriate in the context of constraining the growth of the regulatory burden when it comes to new regulations, it may impede pruning the stock of existing regulations, particularly if the difficulty of creating reliable cost estimates slows down the deregulation process. Serious deregulation requires retrospective examination of existing regulations, even in the absence of new regulations being brought forward. In this regard, the application of the streamlined criteria to identify non-functional regulations might be the first-round focus for a retrospective review of the existing stock of regulations. Specifically, the independent commission or department charged with overseeing the deregulation activity might set a target for regulatory agencies to identify and review a specific number of existing regulatory requirements within a given time.<sup>17</sup> The streamlined criteria would form the basis for making written recommendations to either maintain or eliminate individual (and non-duplicative) requirements. The commission or department would, in turn, accept or reject the agencies’ specific recommendations.

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<sup>17</sup> To avoid the UK experience, few, if any, sectors should be exempt from review.

## Expertise and advice

The public legitimacy and net social benefits of deregulation depend on information being provided by those directly or indirectly affected by regulations to the regulators and those overseeing the deregulation process. Regulators typically invite responses to public notices about new regulations after they have been codified. Symmetrically, regulators should invite public interventions for regulations that are being considered for elimination.<sup>18</sup> In many cases, owners of small businesses will be especially knowledgeable about the likely effects of eliminating specific regulations, but not necessarily aware of ongoing processes to eliminate non-functional regulations. This might be true to the extent that deliberations by agencies about regulations being put forward as non-functional are not publicly posted. The independent commission or government department charged with overseeing the deregulation process should therefore make it a point to consult extensively with the small business community to help identify potentially non-functional regulations, and regulatory agencies should be kept informed of the outcome of such consultations.<sup>19</sup>

As noted earlier, some regulations may not be appropriate for a streamlined assessment of their functionality. They may therefore require expert benefit-cost analysis. Indeed, expert opinion might sometimes be required even in streamlined assessments of whether specific regulations are non-functional. Expert opinion should be based on the best available evidence and the use of best-practice analysis techniques. It is also advisable for the experts providing opinion in the evaluation of regulations to have no financial connections to the regulatory agencies for which they are acting as experts. As a case in point, the Environmental Protection Agency (EPA) in the United States allowed scientists and academics to serve on the EPA's panels evaluating the merit of proposed regulations, while at the same time, those experts were receiving from the regulatory agency research grants relevant to the work of the panel. After his election, Donald Trump appointed an EPA head who instructed his staff to curtail this practice.<sup>20</sup> The obvious concern is that scientists who have research contracts connected to specific regulations will have conflicts of interest in evaluating those regulations.

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<sup>18</sup> Existing regulations can be challenged in court, but this is an expensive process that is unlikely to be initiated as a regular instrument to promote deregulation, especially by small business owners.

<sup>19</sup> Consultation with owners of small businesses was an important focus of the deregulation effort in British Columbia.

<sup>20</sup> Grubel (2017) discusses this case.

## Concluding Comments

Inefficient, poorly designed, or excessive regulations can impose substantial costs on any jurisdiction's economy. Those costs can include slower economic growth and stagnating standards of living. Getting regulatory policy right should therefore be a high priority for any government. As noted in the introduction, retrospective evaluation of existing regulations with a view to reducing red tape is an important part of regulatory best practice. Given evidence of investor concern about the regulatory climate in the province and the uptick of regulatory intervention in key sectors such as electricity and agriculture, Alberta is a prime candidate for regulatory reform.

While much has been written about regulatory reform, the primary focus of this literature has been on ensuring that new regulations satisfy criteria consistent with socially beneficial regulation. Much less has been written about how to deregulate efficiently and effectively. Given the substantial estimated costs of regulation and the economic benefits from reducing red tape, developing and implementing a strategy for deregulation should be an economic priority for governments, especially for governments of sub-national political districts such as Alberta, since firms find it easier to redirect investments from one province or state to another than from one country to another.

This study sets out and discusses criteria and suggested procedures to facilitate deregulation. While the gold-standard criterion is benefit-cost analysis, this test is ordinarily time consuming and relatively costly. Therefore, the study suggests a more streamlined set of criteria to identify non-functional regulations, which are *prima facie* targets for elimination. The relevant criteria for establishing when regulations should be eliminated should be codified and enforced by an independent agency or government department separate from regulatory agencies, although the agencies should be expected to carry out the retrospective analyses of existing regulations. The independent commissions or government departments can suggest candidate rules for elimination to regulatory agencies for the latter's evaluation and the commissions or government

departments should review the evaluations of the regulatory agencies. The relevant commission or government department, in turn, should report to a senior government official with a specific responsibility for the government's deregulation program.

This study also suggests a set of procedural initiatives to ensure that regulatory agencies have incentives that are compatible with the government's deregulation agenda. Prominent in this regard are rules that require a net reduction in existing regulations, or at least no increase in regulations for some period of time. Scientists and other experts providing advice to regulatory agencies about which specific regulations to eliminate should be free of any potential conflicts of interest. Conflicts can arise, for example, if the experts providing advice receive funding from an agency for research tied to one or more of the regulations being considered for elimination. The analyses carried out by regulatory agencies should obviously be based on the best available evidence. The burden of proof should rest upon those making the case for preserving a specific regulation. That is, if the agency in question wants to maintain a specific regulation, it should be able to document that the regulation fails to satisfy one or more of the criteria set out in figure 1. The agency should send out public notices about regulations being considered for elimination, as well as actively solicit advice, particularly from small businesses, about regulations that are candidates for elimination.

This study's introduction also noted that regulations, in their totality, impose substantial costs on national and sub-national economies. One might therefore infer that pruning regulatory requirements will generate substantial economic benefits. While the economic effects of deregulation will obviously depend upon what regulations are pruned and how the pruning is accomplished, the available empirical evidence supports the inference that deregulation is associated with substantial economic benefits, which should justify the resources needed to carry out regulatory reform.

There are two main sources of evidence on the economic consequences of deregulation. One is econometric studies primarily taking the form of cross-sectional models that relate alternative measures of economic performance to differences across political units in the extent of regulation of business activity in those units.<sup>21</sup> It is beyond the scope of this essay to review this literature in any detail.<sup>22</sup> While important methodological issues have been raised concerning such studies, the studies tend

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<sup>21</sup> The political units are typically countries, although some studies focus on sub-national units within a country.

<sup>22</sup> Extensive reviews are provided by the Council of Economic Advisors (2017) and Crews (2018).

to conclude that less regulated countries enjoy faster rates of economic growth, superior productivity performance, and increased rates of capital investment than more regulated countries, other things being constant.

A second source of evidence comes from studies of industries that have experienced significant deregulation. In particular, prices and unit costs are compared for periods before and after deregulation. Most of the available studies look at the reduction of regulations that limited business competition including regulations restricting entry of competitors and limiting price competition. The studies mostly pertain to the United States, which was the first country to deregulate industries such as telecommunications and transportation. However, the results for other countries that followed with domestic deregulation tend to support the US experience. Crandall (2008) reviews the overall evidence on the US deregulation experience in airlines, trucking, railroads, natural gas, telecommunications, and banking. He identifies price reductions to consumers ranging from more than 50 percent in the case of long-distance telecommunications to 30 percent or more in the cases of natural gas and the transportation industries. In the case of banking, the major gain to consumers took the form of increased interest paid on consumer deposits. Crandall notes that in some cases, the estimates of the gains to consumers are only partial estimates. While some of the lower prices reflected reduced profit margins for producers subject to more intense competition, there were also substantial gains in efficiency that contributed to the lower prices.

The most immediate, albeit partial gains, from deregulation are the reduced compliance costs for businesses. Even this limited source provides impressive gains from deregulation. For example, under the one-for-one rule, the Canadian government achieved a net reduction of 19 regulations taken off the books over a period of less than two years. This relatively limited amount of deregulation reduced the estimated net annual administrative burden on the businesses affected by over \$22 million. The OMB concluded that the cost per employee of complying with federal government regulations in the United States was higher for smaller firms (US\$11,724) than it was for firms with over 100 employees (US\$9,083).<sup>23</sup> The higher per-employee compliance costs for small enterprises offers one possible explanation for the slowdown in new business start-up rates observed in developed countries over the past two decades.<sup>24</sup>

In conclusion, while deregulation can be expected to have substantial economic benefits for Alberta if carried out efficiently and effectively,

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<sup>23</sup> See Council of Economic Advisors (2017).

<sup>24</sup> For data on new business start-up rates in a number of developed countries, including Canada and the US, see Emes, Jackson, and Globerman (2018).



it is appropriate for the government to monitor the consequences of its deregulation efforts. In particular, the independent commission or government agency should put in place a monitoring mechanism that alerts it to unintended consequences of eliminating regulations. Unanticipated and undesirable consequences should trigger a new review of the eliminated regulations in question if the consequences are substantial. At some established time in the future, the independent commission or government department should implement an overall review of the deregulation program with a view to improving its overall efficacy and efficiency..

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## About the author



### Steven Globberman

Steven Globberman is Resident Scholar and Addington Chair in Measurement at the Fraser Institute as well as Professor Emeritus at Western Washington University. Previously, he held tenured appointments at Simon Fraser University and York University and has been a visiting professor at the University of California, University of British Columbia, Stockholm School of Economics, Copenhagen School of Business, and the Helsinki School of Economics. He has published more than 150 articles and monographs and is the author of the book *The Impacts of 9/11 on Canada-U.S. Trade* as well as a textbook on international business management. In the early 1990s, he was responsible for coordinating Fraser Institute research on the North American Free Trade Agreement. He earned his BA in economics from Brooklyn College, his MA from the University of California, Los Angeles, and his PhD from New York University.

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