



Regulatory Reform – achieving real benefits for small business

THE ISSUE

Regulation is consistently cited by small firms as one of the top issues affecting their business, which is not surprising given that small businesses are burdened disproportionately by regulatory requirements.¹ In light of this burden, Government has recently introduced a far reaching plan to reduce the £19.7 billion per annum of administrative costs regulation imposes on business² - the Administrative Burdens Reduction Exercise (ABRE).

In view of this initiative, ACCA's Small Business Committee,* which comprises the top commentators on small business issues, heard presentations from the authors of the National Audit Office (NAO) reports at a recent Committee meeting; *Evaluation of Regulatory Impact Assessments 2006-07* and *Reducing the Cost of Complying with Regulations: The Delivery of the Administrative Burdens Reduction Programme 2007*. ACCA's Small Business Committee have made the following recommendations:

RECOMMENDATIONS

- 1. The Impact Assessment (IA) process must be used to challenge the need for new regulations and IAs must always be initiated at the very start of the policy cycle.** The ABRE requires Departments not only to reduce existing burdens but also to deliver a net reduction in regulation. This in turn requires a reduction in the flow of new regulations. Currently, IAs often do not question the need for intervention; indeed the recent NAO review of Regulatory IAs (RIAs) stated that the 'Do Nothing' option was *'often not identified as a realistic alternative.'*³ In order to deliver the promised 25% net reduction target for administrative burdens by 2010, IAs must be used to question the need for intervention.
- 2. Departments must adopt the mindset that the ABRE is not simply a numbers exercise but a root and branch initiative to reduce the impact of regulatory administrative burdens on businesses. The objectives of this exercise can only be achieved through fundamental reform of the way that government thinks about and implements regulation.** To reach the ABRE targets Departments will produce simplification plans each year. These plans will detail the reforms to be enacted during that year. There is a concern that this manner of reform may encourage Government Departments to act in a piecemeal manner picking what appear to be the *'low hanging fruit'* in an incoherent manner. This may prevent Departments from undertaking strategic longer term reforms, which may be of greater benefit to business.
- 3. Major legislative amendments, particularly Government amendments, should be complemented with a revised IA, which include revised costs.** Regulations often undergo significant revision during their progress through Parliament. The impact these changes have on those regulated and the regulators can be significant and so should be tracked and identified through a revised IA.
- 4. Freeing entrepreneurs to make more decisions about their own time will be a wholly positive move and deliver social benefits across the economy. However, it may not create the level of GDP growth predicted.** The Government's rationale for cutting administrative burdens on business by 25% is the potential to increase UK GDP by £16 billion;⁴ a laudable aim but one that remains unproven. This estimate is based on the premise that there is a clear link between regulation and productivity. Many academics are equivocal about this link. Ambler and Chittenden (2007) state that there are *'arguments both ways and little definitive evidence'*.⁵ Indeed recent research by the Federation of Small Business suggests that owner-managers, if relieved of some of their time consuming administrative responsibilities, are as likely to use that time on community work or spend it with their families as they are to work in their business.⁶

5. **An 'independent challenge function' within departments, as recommended by the NAO, and external peer review must be introduced into the IA process to ensure that the costs of regulation on businesses are calculated correctly.** It is fundamental to the integrity of IAs that they provide an accurate assessment of the costs and benefits of new regulations. However, this is the weakest area of IAs⁷ particularly when considering the impact of regulation on small firms. Ambler et al (2007) found that during 2005 and 2006 *'fewer than 8% of RIAs quantified additional costs for SMEs. The majority ... conclude that there are no disproportionate effects for small firms.'*⁸ But academic compliance cost studies⁹ have consistently suggested that SMEs bear a disproportionate burden from regulation and so very often there are additional costs for smaller businesses. These weaknesses must be addressed. In a positive step the new IA summary sheet compels departments to include annual costs for micro, small, medium and large organisations. However, this exercise will only deliver improvements if departments complete rigorous economic appraisals of costs and begin to understand the disproportionate burdens regulation imposes on smaller organisations. Therefore, an independent challenge function within departments, as recommended by the NAO, and an external peer review would assist this process. This challenge function would review the completed IA, questioning the conclusions of the IA and the figures presented therein.
6. **A robust IA process at EU level should be introduced.** The EU is the instigator of many regulations that impact on SMEs. Indeed the think-tank *Open Europe*,¹⁰ using the British Chamber of Commerce' RIA Barometer figures, calculated that between 1998 and July 2004 some £30.1 million of the £38.9 million business costs identified by RIAs involved the implementation of EU legislation.
7. **Government should improve civil servants' knowledge of the issues facing small businesses and the general business context, so that 'business sensitive/ready' regulations are designed and implemented.** Greater understanding will lead to regulations that are both easy to adopt and comply with by small firms. Anecdotal evidence seems to suggest that departments which deal more closely with businesses, those that produce, implement and enforce legislation, have a better appreciation of business practices and produce better IAs. These departments benefit from a positive feedback mechanism between themselves and business. Departments with a 'hands off' approach to regulation lack this feedback mechanism.
8. **'Pilot testing' should be introduced as this would allow regulators to better understand the potential impact of interventions.** It is a significant weakness that most regulations are not pilot tested as this process would ensure clarity as to how new regulations interact with existing requirements. Whilst pilot testing may not be appropriate and would, in some cases, be a costly exercise – in the right circumstances it could improve regulatory intervention.
9. **Civil servants should take steps to minimise the impact of 'survivor bias' by establishing mechanisms to research the experiences of failed and start-up businesses in respect to regulatory compliance.** One of the major issues facing small business policymakers is that, whilst it is easy to study existing SMEs, it is much harder to study potential or failed businesses. This survivor bias can lead to distorted priorities for reform across all aspects of SME policy, including regulatory interventions.
10. **Reduction of the duplication of regulation and the conflicts between regulations should be a priority for Government as reduction would save Government money whilst lessening the burden on SMEs.** The issue of duplication (the same information required by different government departments) whilst not a primary concern for SMEs in the UK¹¹, is an irritant. Conflicting regulations also lead to significant confusion for SMEs. Greater co-operation across Government on SME matters is required.

ACCA'S INVOLVEMENT

ACCA (the Association of Chartered Certified Accountants) is the largest and fastest-growing global professional accountancy body with 296,000 students and 115,000 members in 170 countries. We aim to offer first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accounting, finance and management. ACCA works to achieve and promote the highest professional, ethical and governance standards and advance the public interest.

ACCA has over 100 years' experience of working with and providing professional advice to small and medium-sized firms; in the UK over 56% of ACCA members (over 25,000) work in or for SMEs.

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END NOTES

¹ ACCA (2005), *Putting Small Businesses First*. Small Business Manifesto, ACCA, London.

² The business administrative burden of UK tax regulation is £5.1 billion per annum (KPMG 2006), those imposed by the Financial Services Authority (FSA) amounts to £855 million per annum (Real Assurance Risk Management June 2006 and December 2006) and the rest of Government imposes £13.7 billion per annum after deducting government estimates of “business as usual” costs (HM Government 2006). This equates to a cumulative total of administrative burdens in 2005 of £19.655 billion per annum, or approximately 1.6% of GDP.

³ Page 10, National Audit Office (July 2007), *Evaluation of Regulatory Impact Assessment 2006-07*, Session 2006-2007, HC 606, London.

⁴ Better Regulation Taskforce (2005), *Regulation – Less is more. Reducing Burdens, Improving Outcomes*, Cabinet Office, London.

⁵ Ambler, T. and Chittenden, F. (2007), *Deregulation or Déjà vu? UK deregulation initiatives 1987/2006*, British Chamber of Commerce, London.

⁶ Federation of Small Business (2007), *What would you do with 7 extra hours?* FSB, London.

⁷ The NAO (July 2007) reviewing the assessment of costs and benefits felt there was room for improvement in 14 of the 19 RIAs in their sample, and four RIAs had serious weaknesses. 10 RIAs presented evidence of costs and benefits using mainly a qualitative data, with four of those presenting wholly qualitative descriptions of the likely impacts.

⁸ Ambler T., Chittenden F. and Xiao D. (2007), *The Burden of Regulation: Who is watching out for us?* British Chamber of Commerce, London.

⁹ Studies from the UK include: Baldwin, 2004; Chittenden et al, 2002; 2003; 2005a; 2005b; Collard and Godwin 1999; Collard et al 1998; Kauser et al 2005; KPMG 2006; Lancaster et al 2001. From across the world: Business New Zealand and KPMG, 2005; Confederation of Swedish Enterprise, 2004; Crain 2001; European Commission 2004; Klun, 2004; OECD, 2001.

¹⁰ Open Europe (2005), *Less regulation: 4 ways to cut the burden of EU red tape*, Open Europe, London

¹¹ Blackburn R., Eadson W., Lefebvre R. and Gans P. (2006) *SMEs, regulation and the role of the accountant*, ACCA Research Report No. 96, CAET, London.