

**SUBMISSION**

# Kickstarting the productivity conversation

CIE submission to the NSW Productivity Commissioner

*Prepared for  
NSW Productivity Commissioner*

*27 November 2019*



## *Introduction*

The Centre for International Economics (CIE) welcomes the NSW Productivity Commissioner's recent report, *Kickstarting the productivity conversation*. We broadly agree with the key focus areas and the report identifies many worthwhile opportunities that would form the basis of a meaningful productivity-enhancing reform agenda.

As identified in *Kickstarting the productivity conversation*, a productivity-focused reform agenda is much needed to drive ongoing improvements in living standards in NSW. That said, it is important to acknowledge that every government decision affects living standards in some way, including through the impact on measured productivity outcomes. The risk is that the benefits of a productivity-enhancing reform agenda are quickly wiped out by government decisions that have not been subjected to a rigorous assessment and may not be supported by evidence.

- **In our view, the key to improving productivity performance is to make better policy decisions systematically.**

Rather than focusing on specific reform opportunities, our submission focuses on improvements to processes that lead to better policy outcomes in a systematic way. In summary, we suggest the following improvements could be made to existing policy processes in NSW.

- Ensure that best practice principles and processes are applied to all policies — this includes:
  - consideration of policy reforms as packages rather than individual components
  - applying best practice principles to all policies that have regulatory effect.
- Enhance the independence of the policy development process, including through:
  - greater use of reviews with formal independence from the government (where independent reviewers are required to follow best-practice processes)
  - clarifying that policy evaluations undertaken by government agencies are the independent advice of the agency to the government, rather than an adopted government position
  - greater use of peer reviews.
- Implement a consistent policy process for all types of policies based on best practice principles (consistent with the Policy Proposal Evaluation (PPE) process recommended by the Independent review of the NSW regulatory policy framework) to promote better consideration of a range of different options.
- Conduct formal policy reviews, such as ex-post evaluations of government programs and infrastructure decisions.
- Publicly release policy evaluations, including fully transparent cost-benefit analysis.

## *Best practice policy processes are the key to better policy outcomes*

All policy decisions involve trade-offs. Well-intentioned policies — such as those to achieve desired environmental and social outcomes — can have unintended side-effects and impose costs on sections of the community, often in ways that are not obvious or easily observable. Pursuing social and environmental objectives without adequate consideration of these costs can result in policies that are not in the best interests of the whole community, even when the policy is effective in meeting its objectives.

The best way to encourage systematically better decision-making and evidence-based policy is through the rigorous application of best practice principles and processes to **all** policy decisions. This includes the following key elements, all of which are critical.

- **Identifying and understanding the problem the government is seeking to address** — it is important that all policies start with an understanding of the problem, including the underlying causes. Too often we observe that policy development starts with a solution before the problem is identified or fully understood.
- **Clearly stating the objectives.**
- **Considering a range of options to achieve the objectives** — the best policies to address a particular problem can be identified only if a range different options are considered.
- **Rigorous cost-benefit analysis (where possible) to understand the trade-offs and identify the preferred option** — although the benefits and costs of policy proposals can be difficult to quantify precisely, quantification of all economic, social and environmental costs and benefits is nevertheless essential to help policy-makers to better understand the complex trade-offs. Quantification forces critical assumptions and uncertainties to be explicitly identified meaning decisions are made with regard to maximum amounts of information. The alternative is that critical assumptions and uncertainties are implied but not identified nor understood.
- **Public consultation to gather views and evidence from stakeholders** — public consultation ensures that all views are understood and the best available evidence is gathered. Public consultation also helps to engage and educate the community on complex policy issues and build trust in the policy process.
- **Full public release of the report findings** — this ensures that: decision makers (i.e. the NSW Government) are accountable for the decisions they make; and advisors (i.e. NSW Government agencies and/or consultants) are accountable for the quality of advice given. Public release can also: help to build public trust in government and the decision-making process; help the public to weigh up competing arguments and therefore shift the public debate beyond unsubstantiated assertions onto evidence; and help to build public support for difficult and controversial reforms.
- **Unless the best practice approach to policy development is followed, it is unlikely that future policy choices will systematically improve living standards in NSW.**

## *Suggested improvements to NSW Government processes*

The best practice approach to policy development outlined above is not new. Indeed, many elements of this approach are already in place in NSW. Best practice principles are reflected in key NSW Government policy guidance documents, including: the *NSW Government CBA Guidelines*, the *Guide to Better Regulation* and the *Business Case Guidelines*. We also acknowledge and commend the work of Treasury's Centre for Evidence and Evaluation in improving the quality of evidence to support policy decisions in NSW. That said, there is scope to further improve processes (including implementation of existing requirements) to ensure consistent application of the best practice approach.

### *Best practice principles must be consistently applied to all decisions*

For the best practice approach to policy development to systematically lead to better policy outcomes, it needs to be applied to **all** policy decisions. Currently, there are significant gaps in the coverage of regulatory impact assessment processes. Some examples are given below.

Significant changes to legislation and subordinate legislation are currently the triggers for a regulatory impact assessment. It is frequently the case that the overall policy framework is established in a new Act, while the associated regulations provide specific details on matters, such as when and how the policy framework applies.

There have been instances when the regulations have not been developed until the primary legislation has passed the Parliament. In these circumstances, a problem arises for the RIA process.

- As the impacts of a regulatory proposal will depend critically on the yet-to-be-developed details, it may not be possible to assess these impacts (including estimating the costs and benefits) in the Better Regulation Statement (BRS) for a proposed bill.
- On the other hand, once the Bill has been enacted, the Regulatory Impact Statement (RIS) for the regulations can only consider a narrower range of options (i.e. different thresholds/rates etc.). This means that the impacts of the whole policy package are never adequately considered.
- **It would be preferable for policy reforms to be considered as package.**

Even if the regulations are yet to be formally drafted when the bill is introduced into Parliament, the intended policy settings should be identified, so the policy change can be assessed as an overall package.

Furthermore, the Act/regulations can often delegate the development of guidelines or other material to support the implementation of a regulatory framework to regulators or other government agencies. These documents often have legislative effect and have a material impact on regulated entities, but are rarely subjected to the scrutiny of the regulatory impact assessment process.

- **All documents that have legislative effect should comply with best practice principles.**

*Kickstarting the productivity conversation* highlights the planning system as a key area requiring reform and provides some examples of over-regulation (i.e. where regulation covers matters that could be left to the market).<sup>1</sup> This is likely to be a symptom of a failure to follow best practice principles for all planning regulation.

While past changes to Environmental Planning and Assessment Act and associated regulations have generally been subjected to a BRS/RIS (consistent with the requirements set out in the Guide to Better Regulation), there is much planning regulation that has not followed best practice principles.

- There is little evidence of State Environmental Planning Policies (SEPPs) having been developed through a best practice policy process (as outlined above).
- Local Environmental Plans (LEPs) and Development Control Plans (DCPs) also have legislative effect, but are unlikely to have been developed to comply with the best practice principles outlined. While these documents are generally developed by councils, the powers are given to councils through NSW Government legislation. This gives the NSW Government some control over the way these plans are developed.

As these documents have not been developed to comply with best practice principles, it is possible that there are many instances where: planning controls do not align well with market failures and objectives they are intended to address; and/or restrictions and/or approval processes are not proportional to the impact of particular activities.

### ***Enhance the independence of the policy development process***

Any policy evaluation should be a balanced assessment of the relative merits of various policy options, rather than an opportunity to 'sell' a pre-decided preferred outcome.

- **The policy development process must be independent and objective.**

However, independence can be a challenge given the tension between the public service's dual role as a provider of 'frank and fearless' advice, and to serve the government of the day (including implementation of the government's agenda). Some suggestions for enhancing the independence of the policy development process are set out below.

#### *Commission independent reviews*

One way to enhance the independence of the policy development process is to commission independent reviews (i.e. policy reviews with formal independence from the government), including:

- government agencies with formal independence from the government (such as IPART)
- independent expert reviewers or review panels.

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<sup>1</sup> Office of the NSW Productivity Commissioner, *Kickstarting the productivity conversation*, October 2019, pp. 119-120.

Where policy development is effectively outsourced to independent bodies, it is nevertheless essential that the reviewer follows the best practice approach to policy development.

Reports from independent reviewers should be released publicly within a specified timeframe (such as a month). We note the Government is currently consulting on 3 IPART reviews, including one completed in 2014 and 2 completed in 2016.<sup>2</sup> It is unnecessary for the government to have formulated a response to the independent review prior to release.

### *Clarify 'ownership' of policy evaluations*

Although we support independent reviews for major policy issues, outsourcing all policy development to an independent reviewer would be impractical. Where policy evaluation is undertaken by a government agency (or a consultant on behalf of a government agency), clarifying 'ownership' of policy evaluation documents could help to enhance independence.

In many cases, it would be helpful to explicitly clarify that:

- a policy evaluation document (such as a PPE, BRS, RIS or Business Case) is the **independent** advice of the agency to the government, rather than a policy position that has been adopted by the government; and
- a Cabinet Minute is the Minister's advice to the Cabinet — the Minister and the government should not be obliged to accept the advice of the agency (as set out in the policy evaluation document). A Cabinet Minute should reflect the Minister's preferred position, even if the Minister's preferred position is not consistent with the independent advice from the agency.

Note that in many cases, the independent policy evaluation and the Cabinet Minute will be prepared by the same agency; however, this simply reflects the dual role of the public service. The key point is that by clarifying 'ownership' of the documents, there is no need for the independent ('frank and fearless') evidence-based advice to reflect the preferences of the Minister.

Clarifying the ownership of these key documents would also not preclude the agency from developing material to support the implementation of the government's preferred policy. Again, this simply reflects the dual role of the public service.

### *Independent peer reviews*

Where a policy evaluation is undertaken by a government agency (or a consultant acting on their behalf), independent peer reviews (that are published) can help to ensure the quality of the analysis to support policy recommendations are a balanced assessment of the policy options (rather than tweaked to support a pre-determined outcome).

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<sup>2</sup> NSW Office of Local Government website, <https://www.olg.nsw.gov.au/strengthening-local-government/ipart-local-government-reports-consultation-2019>, accessed 27 November 2019.

- **We note the current use of peer review and support continuation/expansion of peer reviews for major policy decisions.**

### *A consistent process for all policies*

The best practice approach to policy development outlined above generally applies to all policy proposals, regardless of whether it relates to: regulatory changes; investment in infrastructure; or other government spending programs. Yet, currently there are different processes for each one. For example:

- the process for capital spending decisions are set out in the Guidelines for Capital Business Cases
- the process for regulatory proposals are set out in the Guide to Better Regulation.

The problem is that each of these separate processes effectively pre-supposes the preferred outcome. For example, going down the regulatory impact assessment path pre-supposes a regulatory response. Similarly, a Business Case pre-supposes that some form of government investment is the best policy response.

- **Different process for different types of policies can limit the consideration of a wide range of options, which is a necessary element of the best practice approach outlined above.**
- **The CIE supports applying the approach to Policy Proposal Evaluations (PPEs) as set out in Independent Review of the NSW regulatory policy framework (the Greiner review) for all policy (not just regulatory decisions).**

We also support reframing BRSS, RISs and Business Cases as PPEs (or similar).<sup>3</sup> This frames the document as a balanced evaluation of various policy options, rather than as a document to make a case for a pre-determined policy outcome (in our view, use of the term 'Business Case' can lead to this perception).

Where there are unique requirements for particular types of policies these could be addressed once it has been established (through cost-benefit analysis) that a particular type of policy is the preferred approach.

### *Formal review processes*

CIE supports the greater use of formal policy reviews, including:

- Ex-post evaluation of ongoing government programs (to determine whether the program should continue)
- Some ex-post evaluation of infrastructure decisions (to identify lessons for future projects)
- Periodic review of regulation.

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<sup>3</sup> See the discussion on 'Repositioning Regulatory Impact Assessments to Policy Proposal Evaluations' in Regulatory Policy Framework Review Panel, *Independent Review of the NSW Regulatory Policy Framework*, Draft report for consultation, May 2017, p. 37.



We generally support the regulatory stewardship approach outlined in the Greiner review. However, it is essential that there is a formal requirement for a detailed review of regulatory reviews occur periodically, so that detailed review of controversial or sensitive regulation cannot be avoided indefinitely.

### ***Public release of documents***

As noted above, it is essential that policy evaluation documents (including peer reviews) for major decisions (including regulatory decisions and major infrastructure decisions) are released publicly to:

- ensure decision makers (i.e. the NSW Government) are accountable for the decisions they make;
- ensure advisors (i.e. NSW Government agencies and/or consultants) are accountable for the quality of advice given;
- help to build public trust in government and the decision-making process;
- help the public to weigh up competing arguments and therefore shift the public debate beyond unsubstantiated assertions onto evidence; and
- help to build public support for difficult and controversial reforms.

Public release includes full disclosure of methodology, data sources and assumptions used in the cost-benefit analysis.