“Why deregulate?”
Forum: Productivity reform in Australia and New Zealand – Barriers and opportunities, 24 November 2020
Speech Transcript

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Background:
On 24 November 2020, members from Australian and New Zealand Productivity Commissions joined a livestream forum with a range of expert speakers to discuss policy reforms to drive productivity. The forum, hosted by the Queensland Productivity Commission, was a joint event of the Australian, New Zealand and state productivity commissions.

Thanks for the opportunity to talk at this event today.¹

Today I am going to make the case for why governments should focus on deregulation, not just on doing regulation better. At the outset I should declare a special interest, since I have just taken up the role as the head of the Australian Government’s Deregulation Taskforce in the Department of Prime Minister and Cabinet. Caveat Emptor.

The role has taken on renewed urgency given the need to get Australians back into work following the COVID-19 shock. Deregulation is a key driver of the government’s JobMaker plan for economic recovery (Morrison, 2020). Deregulation removes barriers to resource reallocation, which is particularly important given recessions in Australia appear to accelerate underlying structural change (Fahrer and Heath, 1992). On top of those trends, COVID-19 itself is a supply side shock that is changing our economy (Brennan, 2020). The fewer barriers to this happening, the quicker Australians will get back into jobs.

Deregulating to boost growth follows naturally from deregulating to respond the shock itself. During the COVID-19 health crisis, all levels of government made practical deregulation measures that allowed resources to flow where they were most needed. Shop trading hours were deregulated in Queensland, Western Australia and South Australia so people didn’t have to spend so long in the queues. Trucks were allowed along roads and out of normal hours to re-supply shops in the face of shortages. Unnecessary professional requirements were removed so nurses could more easily come back into the workforce. Changes were made to promote the use of telehealth so patients didn’t need to meet face to face. The government also allowed companies to use international standards for hand sanitiser so that production

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could increase quickly. Workplace rules were relaxed to allow COVID-19 affected businesses to reduce hours and reconfigure tasks so workers could stay in jobs – including allowing waiters to deliver food to homes instead of just tables. Businesses were relieved of regulatory burdens that made them more resilient – such as loosening insolvency reporting – as well as reducing the need for face to face contact, such as enabling the use of electronic signatures and online shareholder meetings.

In many ways, such flexibility in responding to changing circumstances is a sign of good regulatory policy. During a pandemic, the cost-benefit trade off shifts – some economists have pointed out that the benefits of a vaccine are so large that normal clinical trial processes should be amended (Berry et al, 2020). But some of the regulations may not have been worth it even before COVID-19.

So a very interesting policy question is - why were they in the system in the first place?

**Productivity slowdown**

The government’s focus on deregulation precedes COVID-19, even if it has been spurred on by it. Multi-factor productivity growth – the kind of productivity that makes us richer because we work smarter without consuming resources – has been slowing since the 1990s (Campbell and Withers, 2017).

This productivity slowdown is not just local. Productivity in the US has been trending down since the early 2000s. The CBO estimates that non-farm business sector total factor productivity is one third lower for the most recent decade compared to the one just preceding (CBO, 2019). The US matters for many reasons, not the least of which is that we tend to view it as a proxy for the productivity frontier.

The potential reasons for the productivity slowdown have been explored in many books and articles, with explanations ranging from mismeasuring the impact of technology change (for example, Brynjolfsson; and Oh, 2012; or not, Byrne et al, 2016), running out of ideas (Gordon, 2016), lags in technology showing up in statistics (for example, Brynjolfsson et al 2017) to reduced dynamism (Campbell, 2019).

No single explanation dominates convincingly, perhaps there are multiple reasons. Some economists both here (Tunny and Scott, 2000) and overseas (Andrews et al 2016, Coffey et al, 2020) point to the regulatory burden as one possible reason. Regulations are essential for helping society to better align individual incentives with social outcomes, such as protecting workers and consumer safety. But when they get in the way of what consumers want and businesses want to deliver, they are like taxes that raise no revenue. The key regulatory policy question is whether the benefits are worth the costs.

There are good reasons to think that some parts of the regulatory landscape are no longer fit for purpose, and in some cases, may never have been – so deregulation can boost growth.

**Some theory**

How we think about regulation has gone through significant changes since I’ve been an economist. Cost of the economics profession up until the 1960’s viewed regulation as another instrument of government, along with taxing and spending. This ‘welfare-theoretic’ or ‘public interest’ theory of regulation followed the work of Pigou (1920). By targeting market failures to improve incentives, technocrats could fine tune the economy. All regulators need to do is solve the math.
Things changed following the economic crises of the 1970s as price controls and other regulations failed to deal with stagflation and falling living standards. Models of regulation developed by Stigler (1971), Posner (1974) and Peltzman (1989) and others explicitly incorporated the incentives of regulators into regulatory policy, allowing for government failure. In these models regulators could be subject to information failures just like the markets they are regulating (for a survey see Crew and Kleindorfer, 2002). In fact, budget and other constraints may be worse for regulators than for the private sector participants they regulate. Or regulations could be set to support special interests, or even the interests of the regulators themselves. For example, if the regulators are disproportionately sanctioned for insufficient regulation of rare but significant negative events then they may be overly-prescriptive towards risk taking.

Paying attention to incentives faced by regulators is particularly important since, unlike taxing and spending, the amount of regulation is not limited by a budget – indeed, there is very little costing of regulation done at all. Bouts of focused deregulation, such as our taskforce deep dives, can be seen as a practical response.

The ‘public choice’ school helped build the foundations for the great deregulatory projects across many developed countries in the 1980s and 1990s, including our own financial market deregulation and National Competition Policy (for a good history see Allen et al, 2020).

The next significant contribution is the market design literature, informed by ‘consumer failure’ insights from behavioural economics. Behavioural economists think regulations can be done better if they take account of some of the more important cognitive biases, such as loss-aversion, hyperbolic discounting and reliance on heuristics (for a review see Kahneman, 2011). While some economists fear that these models can justify a new era of paternalism, they can just as easily be seen as promoting ‘nudges’ over existing heavy-handed regulations (Thaler and Sunstein, 2008). Simple deregulation can be default programs that automatically enrol people into aid programs or reducing paper work for obtaining licences (Benartzi et al, 2017).

This new view of regulation starts from what users need – what the Minister Assisting the Prime Minister and Cabinet, the Hon Ben Morton MP, responsible for deregulation, refers to as ‘standing on the factory floor’ (Morton, 2020). Regulations need to assist rather than impede users. The economics of market design view regulations a means of facilitating trades through efficient contracting, not just sanctioning or policing them. Market designers look for regulatory reforms that can allow “stable” trades, so that users aren’t stuck with things when they would prefer something else.

Market designers tend to work in areas where traditional pricing arrangements are ruled out such as school admissions, kidney transplants and job applications (Roth, 2018). Market design extends deregulation to parts of the social sector that have otherwise been reserved for traditional command and control allocation. In Australia, we are in the process of shifting from a highly regulated and prescriptive government system of disability services to the more market-based NDIS. Behavioural insights are also particularly important in addressing the specific needs of potentially vulnerable clients, including ensuring appropriate agents for those with limited capability and easily understandable measurement of quality for services.
New technology opens up tremendous opportunities to replace existing regulation with more effective market solutions. Indeed, if you think of regulation as a technology used by government to run society, then regulators themselves are in open competition with new information technologies. Regulation is increasingly seen as a transaction cost that can assist businesses and even consumers to contract (Biggar, 2011). In many ways, Uber is also a private sector market designer. Their innovations in matching drivers to customers and quality assurance technologies has replaced the case for lots of state based taxi regulation. Poor or asymmetric information has supported the need for lots of regulation in the past, suggesting the information age should be triggering lots of regulatory redundancy.

**Some practice**

How are we bringing this intellectual tradition to regulatory reform in practice?

I’ll finish up with taking a close look at occupational licensing, something the PC has had a lot of interest in (Productivity Commission, 2015).

Occupational licensing can help ensure consumer and worker safety – internalising externalities as Pigou first intended. No one should be allowed to perform unsafe electrical or plumbing work anywhere. But the benefits of occupational licensing need to be tested against the costs. We should continually test all regulation for fitness of purpose and against lower cost alternatives.

One area where occupational licenses needlessly drive up costs is when workers are required to apply for another licence to do the same activity across a state border. Sometimes this involves additional fees, delays or other requirements, inhibiting occupations from sparkies to teachers, architects - even painters in some states. Such impediments particularly harm the shift to a more modern digital economy, since some occupations that don’t need to physically cross state borders, such as architects, still need to bear the costs of a second licence. These are fees that are born by businesses and workers because regulators haven’t been able to reconcile their differences or flexible enough to regulate interstate work. Many Australian workers probably wonder why they can easily drive across borders with their state drivers licence, but not their occupational licence.

Such restrictions are particularly costly right now given COVID-19 has meant some parts of the country are growing, such as mining regions, while others are not, particularly those dependent on tourism and education. Estimates by PWC suggest 60,000 workers would benefit from not having to pay additional licence fees, while another 40,000 would take up jobs across borders. (These are lower bound estimates likely to rise as we gather more data.) Such restrictions can also limit competition. Often workers wanting to bid for interstate competition require a local licence, but they don’t want to bear the cost of a licence without guaranteed work.

So just last week National Cabinet made an in-principle decision to adopt widespread automatic mutual recognition – or AMR - of occupational licensing from 1 July 2021 (Morrison, 2020). Draft legislation to amend the Mutual Recognition Act 1992 will be released soon, by the end of this year.

While commensurate with the economic challenge we face, this deadline is ambitious when set against the history of occupational licensing reform in Australia.
While some occupations have managed national recognition, including many health professionals since 2010, but two previous attempts at widespread licensing reform have either failed or achieved modest success. Between 2009 and 2013 the government tried to standardise licenses starting with four occupations through the National Occupational Licensing regime, or NOLs. While hopes were high at the beginning, NOLs eventually fell over in the face of the difficulty of standardising licences across the country. Some states were concerned standards would be too high, others too low - a single standard may be uniform, but need not be simple. Some states feared signing up to regulations they didn’t need; ‘deregulation’ risked over-regulating.

States then reverted to a ‘state by state by occupation’ approach, perhaps the best example is the east coast electricians’ arrangements. While successful for electricians wanting to move between Queensland, Victoria and NSW, other states and occupations have been reluctant to join. Partly this may reflect the difficulty in achieving and maintaining a ‘white list’ of occupations that are to be mutually recognised. Regulators need to dig into the details of each license to decide ‘equivalence’. Licence by licence. Obviously this is an intensive process, with new licences and revisions to old ones making it a perpetual process. These painstaking steps continue to be taken in a number of occupational areas, generally in response to industry-specific reviews.

This third go at more ambitious mutual recognition is different.

Treasurers are leading this process supported by a working group co-led by NSW with members from all jurisdictions. Reflecting the commitment of National Cabinet, there is a real sense of common purpose and desire to get this done.

Under the proposed national Automatic Mutual Recognition – or AMR - all occupations subject to the Mutual Recognition Act are automatically in, except if they are on a ‘black list’. The black list focuses regulators on areas where they disagree and asks them to explain why exempting the occupation from AMR is necessary to protect consumer and worker safety. Most importantly, the blacklist approach also doesn’t require the scope of work to be aligned, workers are able to do in one state what their licence allows them to do in their home state – and no more. That is, if you are registered to perform an occupation in one state, the starting point is that you should be able to perform the same activities in another state.

Rather than put in place another layer of regulation, AMR encourages regulators to cooperate with each other to enable workers who have met requirements in one jurisdiction to work seamlessly across Australia.

Rather than reducing standards, AMR should improve protections. Under existing mutual recognition arrangements it’s possible for regulators to rescind a licence in a home state if a worker breaks the terms. But if they have already been mutually recognised in another they can continue to work in another state. Similarly, in some circumstances a worker can potentially infringe in one state after another, continually shopping their lower, and possibly dangerous, standards. AMR can fix up these loopholes because the principle of automatic mutual recognition also implies a principle of automatic non-recognition. With the right sharing of information, and incentives, regulators should be able to police infringements wherever they take place, and quickly. Workers subject to disciplinary proceedings won’t be entitled to AMR. With workers with different licences operating easily across states,
information will need to be presented to consumers in ways that they can readily access and understand.

There is still a way to go before AMR is up and running, but the signs are positive. This most recent attempt at occupational licensing reform incorporates some elements of all the theory I’ve outlined. Occupational licensing does improve worker and community safety, but we can reduce the costs if we design systems that recognise the incentives regulators face and present information meaningfully to consumers.

Conclusion

Nothing in this speech is new, so in that vein I will finish up by recycling a PJ O’Rourke quote former PC Chair Gary Banks once used to describe community attitudes to regulation (Banks, 2003). The ‘mystery of government is not how it works, but how to make it stop’. Obviously none of us here want to make it stop, but thoughtful deregulation can help make it run a little better.