

# **Effective Policy Making**

## **Workbook Three:**

### **Identifying the Way Forward**

## INTRODUCTION

This workbook is the third in a series of five which seeks to provide a practical overview of the key steps in the policy development process as outlined below:

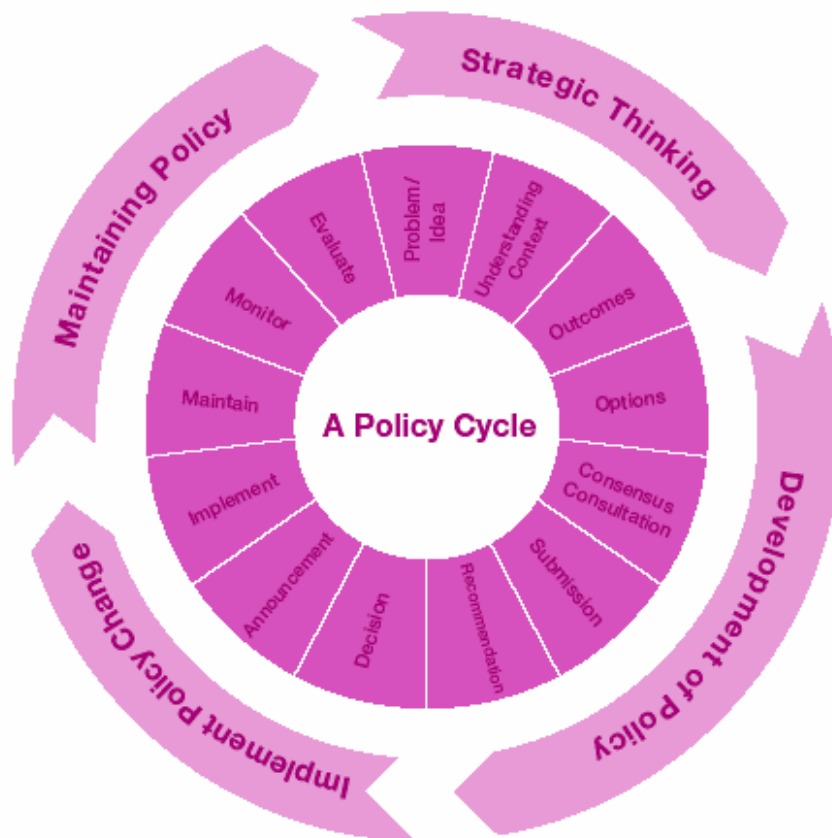
<b>Workbook:</b>	<b>Key Areas Addressed:</b>
<b>1. Justification and Set-Up</b>	<ul style="list-style-type: none"> <li>Establishing the Need for Policy Intervention</li> <li>Planning Your Approach and Engaging Stakeholders</li> </ul>
<b>2. Developing and Analysing the Evidence Base</b>	<ul style="list-style-type: none"> <li>Gathering the Evidence</li> <li>Analysing the Evidence</li> <li>Presenting the Analytical Report</li> <li>Agreeing the Aims and Objectives</li> </ul>
<b>3. Identifying and appraising Policy Options</b>	<ul style="list-style-type: none"> <li>Identifying Policy Options</li> <li>Costs, Benefits and Risks</li> <li>Appraising the Options</li> </ul>
<b>4. A Practical Guide to Impact Assessments</b>	<ul style="list-style-type: none"> <li>Defining the Aims</li> <li>Screening the Policy</li> <li>Assessing the Impacts</li> <li>Consultation</li> <li>Prioritising the Impacts</li> <li>Agreeing Recommendations and Implementation</li> <li>Decision and Publication of Report on Results of Impact Assessments</li> <li>Monitoring and Evaluation</li> </ul>
<b>5. From Consultation to Announcement</b>	<ul style="list-style-type: none"> <li>Formal Consultation Exercise</li> <li>The Submission</li> </ul>

Announcing the Decision

Each workbook seeks to provide practical guidance and draws on existing guidance material and best practice, in particular [\*A Practical Guide to Policy Making in Northern Ireland\*](#). The workbooks are intended as an introduction and a reference point for more detailed guidance. They are structured around the key stages of the policy process to enable policy makers to dip into the guidance as appropriate.

In using the workbooks it is important to acknowledge that the policy process is cyclical and continuous as demonstrated in Figure 1 below. Policy makers rarely if ever start with a clean sheet and as we work through the process it is often necessary to consider the other stages. Therefore, it is advisable that before using the workbooks you familiarise yourself with the contents and the key messages of the Practical Guide.

**Figure 1: The Policy Cycle**



### **What is Policy Making?**

Policy making is the process by which the administration translates its vision into actions to achieve desired outcomes. Good policy making is therefore essential if government is to achieve its aims and deliver real change and benefits.

There is no single uniform approach to policy making which can be applied to all areas and all departments. The range of factors and the environment within which policy makers operate can vary considerably. The policy maker may be addressing a regional, local or even international issue. They may need to consider any number of social, economic or environmental factors. There may also be considerable variation in the resource consequences of the policy and the number of groups or individuals which the policy may impact upon. However, there are a number of broad steps or stages which can be applied to most policy areas and these are outlined in this series of workbooks. The key is to tailor the policy process to needs.

**CONTENTS****3.1 OVERVIEW****3.2 IDENTIFYING POLICY OPTIONS****3.3 COSTS, BENEFITS AND RISKS****3.4 APPRAISING THE OPTIONS**

### 3.1 Overview

This workbook aims to work you through the process of developing options, appraising those options and identifying the way forward. This stage of the policy process must take account of the evidence base and the objectives identified for the policy.

Although the appraisal of options is addressed in this workbook, a key part of identifying the preferred way forward is the appraisal of impacts which is considered in Workbook Four. As such, this workbook should be utilized alongside Workbook Four. It should be noted that a full Impact Assessment is not required on each option. However, an initial consideration of the potential impacts, or screening the options in line with the screening tool in Workbook Four, may help to identify potential impacts, the feasibility of the proposals and the non-monetary costs and benefits associated with individual options.

## 3.2 Identifying Policy Options

Having gathered your evidence and agreed your objectives, the next stage is to identify your policy options. It is essential that policy makers consider a wide range of options, as comparison of alternatives helps to draw out the merits of various approaches.

### **Engaging stakeholders**

As in previous stages, where possible, policy makers should involve the widest range of internal and external interests appropriate in identifying and assessing options. Involving those who will implement or evaluate the policy is key to assessing the practicality of proposals. Involving external stakeholders at this stage does carry the risk of raising expectations, and this needs to be considered in managing this stage of the process.

### **Basic requirements of the policy**

Before generating options, it is useful to consider the policy goal and to think about the policy in terms of:

- things it must do
- things it must not do
- things it could do

This can be used as part of the criteria to initially screen the options to identify those you wish to consider in more detail and those you may wish to discard.

### **Identifying a wide range of options**

It is useful to begin by identifying a 'long list' of options or possible solutions. This should include not only the conventional solutions, but also any more innovative suggestions, however outlandish they may at first appear. These can be narrowed down at a later stage.

In order to identify possible options it is useful to consider the following:

- how the issue has been addressed previously;
- how other administrations have addressed this or similar issues;
- identify best practice solutions;
- what are the key political actors and stakeholders proposing;
- identify the full range of policy instruments or projects that may be used to meet the objectives.

At this stage, the options should be described in broad terms.

However, each option should clearly outline:

- how it will achieve, or contribute to, the policy goal;
- how it fits with existing or planned policies and any existing requirements and obligations on those who might be affected;
- how it could be delivered; and
- indicative costs.

Where the broad policy direction is already determined (for example, when transposing a European Directive) the policy maker should focus on options for implementing the desired solution most effectively.

### **Narrowing the range of options**

Only those options which meet the basic requirements of the policy and appear to offer a practical solution should be considered in further detail. Take forward only the realistic options. Some options may be in fact deliverable but only on an unacceptable timescale, or at high cost. Ministers will always have a timing preference and a price in mind.

The number of options to be subjected to detailed consideration will vary but should generally be in the range of three to six including consideration of the status quo – commonly referred to as the “do nothing” base case option. The status quo option represents the

genuine minimum input necessary to maintain services at, or as close as possible to, their current level. Even where it is not considered to be a realistic option, it should be included to provide a benchmark.

### **Output**

The output for this stage should be detailed policy options. As a minimum, fully worked policy options will detail:

- The anticipated outcome(s);
- What will be delivered;
- Who will deliver it;
- The key roles and accountability;
- How it will be funded;
- How success will be measured; and
- How it fits with other policies and wider strategic priorities.

### 3.3 Costs, Benefits and Risks

For each option it is necessary to consider the costs, benefits and risks associated with the option. Detailed guidance on identifying and analysing costs, benefits and risks is available through [HM Treasury's Green Book](#) (See Chapter 5 and Annex 2). Departmental economists can provide advice and guidance and should, where possible, be engaged as early as possible in the process.

The process of identifying and quantifying the full range of costs and benefits of each option can be broken down into three broad steps:

1. Identify and quantify the monetary costs and benefits of each option;
2. Identify the risks in relation to implementation and costs; and
3. In light of the identified risks, adjust the monetary costs and benefits for '*optimism bias*'.

#### **Step 1: Identify the Costs and Benefits**

Policy makers need to consider two broad types of costs and benefits over the lifetime of the policy/project, breaking these down annually<sup>1</sup>:

#### **Monetary**

**Costs and Benefits:** These are the hard costs and savings associated with developing and implementing the programme and arising from the policy. This should include the costs and savings to the administration, other sectors and private individuals. It should, where appropriate, also consider

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<sup>1</sup> Where appropriate, policy makers may also wish to consider opportunity costs. Economists define the "opportunity cost" of any good or service as the value of other goods or services that we must give up in order to produce it. Departmental economists can provide advice on this area.

the cost of the proposal to the wider economy.

### **Non-Monetary**

**Costs and Benefits:** Not all costs and benefits can be expressed in monetary terms. For example there may be environmental, health or social impacts. The Impact Assessment Tool (Workbook Four) is a useful tool to help identify the full range of non-monetary costs and benefits associated with the policy.

Where possible a monetary value should be attached to these impacts, though this may not always be possible. In the first instance policy makers should consult departmental economists who can provide advice and guidance in this area.

Initially, the policy maker needs to identify all the costs and benefits anticipated over the lifetime of the option. Template 1 below provides a framework to record the monetary costs and benefits; Template 2 provides a framework to record the non-monetary costs and benefits. There are a number of approaches to attributing a value to non-monetary costs and benefits; for this reason, Template 2 provides a column to attach a value to non-monetary costs and benefits. Departmental economists can provide assistance in this regard and guidance is available in Annex 2 of [HM Treasury's Green Book](#). It is recognised that often it will not be possible to identify a monetary value; however, it is still important to record the cost and/or benefit to ensure it is fully considered. In such cases impacts should be described qualitatively.

3.

IDENTIFYING THE WAY FORWARD

Template 1: Overview of Monetary Costs and Benefits by Year

Option Number:												
Option Title:												
Year	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	TOTAL
<b>Capital Costs</b>												
<b>A Total Capital Costs</b>												
<b>Revenue Costs</b>												
<b>B Total Revenue Costs</b>												
<b>C Total Costs (A+B)</b>												
<b>Benefits</b>												
<b>D Total Benefits</b>												
<b>Total Cost/Benefit (C-D)</b>												

Template 2: Overview of Non-Monetary Costs and Benefits by Year

<b>Option Number:</b>							
<b>Option Title:</b>							
Year	Year 0 - 2		Year 3 - 6		Year 7-10		TOTAL
	Overview of Cost/Benefit	Value (£)	Overview of Cost/Benefit	Value (£)	Overview of Cost/Benefit	Value (£)	
Non- Monetary Costs							
<b>A</b>	<b>Total Value of Non-Monetary Costs (where this can be determined)</b>						
Non-Monetary Benefits							
<b>B</b>	<b>Total Vale of Non-Monetary Benefits (where this can be determined)</b>						
<b>Total Cost / Benefit (A-B)</b>							

**Step 2: Identify the Risks and Uncertainty**

All policy work involves some degree of risk. Risks are things that may happen at some point in the future and have the potential to impact on the policy and the realisation of objectives. Risks can occur or emerge in the external or internal environment; they may be the result of the impact of other policies and political developments; or they may be associated with finance, resourcing and funding, the project timescales or more general issues with regard to the operational delivery of the policy.

It is essential that risks are identified and actively managed in order to reduce their likelihood of happening or their impact on the policy or programme. It is difficult for an individual policy maker to identify every possible risk; it is therefore good practice to engage relevant stakeholders in this exercise. A vital first step in the analysis is to identify and analyse the important risks, and to show how they compare under each option.

Questions which need to be considered at this stage include:

- What risks are associated with the option?
- Which sector(s) does the risk impact on?
- Which of the three pillars of sustainable development (social, environmental or economic) does the risk impact upon?
- Is the risk time-bound?
- What are the consequences or impact of the risk? Are these significant?
- What is the likelihood of the risk occurring?
- What is the likelihood of the risk resulting in the above consequence(s)?
- Can the option be amended to minimise the likelihood of the risk occurring?

- Can the option be amended to minimise any negative consequences of the risk?

In order to assist in evaluating the level of risk associated with each option, the template below provides a framework for presenting the outcome of the risk assessment in a graphical format. Assign each risk a number and record it in the relevant box. In addition, once a final option/solution has been agreed, the template can also be used to prioritise the risks.

PROBABILITY	Low			
	Medium			
	High			
		Low	Medium	High
		IMPACT		

### Assessing Uncertainty

However well risks are identified and analysed, the future is inherently uncertain. So it is also essential to consider how future uncertainties can affect the choice between options.

In assessing uncertainty, the policy maker is considering how vulnerable the option is to unavoidable uncertainties in the future and how changes in a number of variables may impact upon the potential value of the proposal. Examples of variables that are likely to be both inherently uncertain and fundamental to assumptions regarding the feasibility and costs and benefits of options are the growth of real wages, forecast revenues, demand, prices and even environmental change.

Techniques which can be applied include sensitivity analysis and scenario planning. Both the [HM Treasury's Green Book](#) and the [Northern Ireland Practical Guide to the Green Book](#) provide more detailed guidance on this subject. Departmental economists can also provide advice in this regard.

### **Mitigating Risk and Uncertainty**

Following the identification and analysis of risks and uncertainty, appraisers need to look next at strategies to prevent and mitigate risks and uncertainties. The following may be adopted:

- Consulting early;
- Avoiding irreversible decisions;
- Carrying out pilot studies;
- Building in flexibility from the start;
- Taking precautionary action;
- Transferring risk through contractual arrangements (insurance being an example);
- Developing less risky options, such as making less use of leading edge technology;
- Reinstating, or developing different options; or
- Abandoning the project because it is too risky.

### **Step 3: Adjust the Costs and Benefits for 'Optimism Bias'**

There is a demonstrated tendency for project/policy appraisers to be overly optimistic in their assumptions and to overstate benefits, and understate timings and costs, both capital and operational. If unaddressed, this can significantly undermine the potential success of the policy.

To redress the tendency to be overly optimistic, appraisers should make explicit adjustments for this bias. These will take the form of increasing estimates of the initial costs and decreasing, and delaying the receipt of, estimated benefits. [The Northern Ireland Practical Guide to the Green Book](#) provides detailed guidance on how to deal with optimism bias and once again, departmental economists can provide assistance. Spreadsheets to assist in the calculation of optimism bias are also available on the Department of Finance and Personnel (DFP) website at <http://eag.dfpni.gov.uk/optimism-bias-calculators.htm>.

Adjusting for optimism bias must also take account of the assessment of risk and uncertainty outlined below. Where there is uncertainty over the estimates of the quantitative or monetary value of the proposed option, departments should make this clear and spell out the assumptions used to arrive at the estimates. Departments should also consider presenting a range of values for their estimates, stating whether they represent extreme values or the most likely outcome.

### **Calculating Net Present Value**

The various policy options will generally have an impact over a period of years into the future. This raises the question of how future cost and benefits should be valued in today's terms. Normally people prefer to receive cash sooner rather than later, and pay bills later rather than sooner. In the public sector, likewise, we give more weight to earlier than to later costs and benefits. This is done by applying a discount rate to future costs and benefits.

Any appraisal of the options should generally include, for each option, a calculation of its Net Present Value (NPV). This is the name given to the sum of the discounted benefits of an option less the sum of its discounted costs, all discounted to the same base date.

Guidance on calculating NPV is available through the Northern Ireland Practical Guide to the Green Book and departmental economists can also provide assistance. In addition a spreadsheet to assist in calculating NPV is available on the DFP website at <http://eag.dfpni.gov.uk/npc-calculator.htm>.

The NPV is the key summary indicator of the comparative value of an option. It enables direct comparison of options with very different patterns of costs and benefits over time. For instance, it solves the problem of how to compare a low capital cost / high running cost option with that of a high capital cost / low running cost alternative.

**Regulatory Impact Assessment**

An assessment of the benefits and costs of a proposal is the central analytical component of a Regulatory Impact Assessment (RIA). Where a RIA is required, it is necessary to break the costs down in terms of policy costs and implementation costs, and by sector, for example public, private, voluntary and consumers, and to consider the distributional impacts of any costs and benefits. This should be based on the final costs adjusted to take account of optimism biases and NPV. Even when a RIA is not required, it is still best practice to consider the distributional impacts of the costs and benefits to ensure that they do not unduly accrue to any one section of society. Template 3 below provides a framework to summarise the total policy and implementation costs by sector.

Template 3: Distribution of Monetary Costs and Benefits by Sector (Regulatory Impact Assessment)

<b>Option Number:</b>						
<b>Option Title:</b>						
		<b>Distribution Of Costs</b>				
<b>Sector</b>		<b>Government</b>	<b>Public Sector</b>	<b>Business</b>	<b>Consumers</b>	<b>Total</b>
<b>Policy Costs</b>						
<b>A</b>	<b>Total Policy Costs</b>					
	<b>Implementation Costs</b>					
<b>B</b>	<b>Total Implementation Costs</b>					
<b>C</b>	<b>Total Costs (A+B)</b>					
	<b>Benefits</b>					
<b>D</b>	<b>Total Benefits</b>					
	<b>Total Cost + Benefits (C+D)</b>					

### **Sustainable Development**

Consideration of the costs and benefits is a key part of testing the sustainability and long-term impact of a proposal. Template 4 below provides a framework to summarise the monetary costs and benefits under the three pillars of sustainable development, these are:

**Environmental:** focuses on the wider environment. This would include issues/measures relevant to climate change and global warming, i.e. greenhouse gas emissions. It would also consider air quality, water, deforestation, use of natural resources and the impact of measures or projects on the built environment and the landscape.

**Social:** focuses on the basic needs of people. It considers and includes issues such as health, housing, education, equality, sanitation and community participation.

**Economic:** focuses on wealth creation and the economy at a national, regional, sub-regional and local level. Where appropriate it may also include reference to the wider global economy. In relation to costs and benefits it would include among other areas the provision of infrastructure or programmes to assist economic activity and/or the creation of jobs.

Not all costs will fit easily into one of the three pillars and there will be some degree of overlap. However, recording the costs and benefits in this way can be a useful means to highlight where the policy is likely to have significant impacts. This exercise should be based on the final costs adjusted to take account of optimism bias and NPV and should also reflect the outcome of the Impact Assessment Tool where one is undertaken.

Template 4: Monetary Costs and Benefits (Sustainable Development)

Option Number					
Option Title:					
		Social	Environmental	Economic	Total
<b>Capital Costs (£)</b>					
Year 1					
Year 2					
Year 3					
<b>A</b>	<b>Total Capital Costs:</b>				
<b>Revenue Costs (£)</b>					
Year 1					
Year 2					
Year 3					
<b>B</b>	<b>Total Revenue Costs:</b>				
<b>C</b>	<b>Total Costs (A+B)</b>				
<b>Benefits (£)</b>					
Year 1					
Year 2					
Year 3					
<b>D</b>	<b>Total Benefits</b>				
<b>Total Costs/Benefits (C-D)</b>					

Templates 5a and 5b below provide a framework for recording the non-monetary costs and benefits under the three pillars of sustainable development. It must be noted that the templates provide a guide and should be amended as appropriate to ensure they are relevant to the policy area.

Template 5a: Non-Monetary Costs (Sustainable Development)

Option Number:							
Option Title:							
<b>Costs</b>							
			<b>Environmental</b>		<b>Economic</b>		<b>Total</b>
		<b>Value (£)</b>	<b>Overview</b>	<b>Value (£)</b>	<b>Overview</b>	<b>Value (£)</b>	<b>Cost (£)</b>
<b>Year 0-2</b>							
	<b>Overview</b>						
	<b>Social</b>						
<b>Year 3-6</b>							
<b>Year 7-10</b>							
<b>Total Costs</b>							

Template 5b: Non-Monetary Benefits (Sustainable Development)

Option Number:							
Option Title:							
<b>Benefits</b>							
			<b>Environmental</b>		<b>Economic</b>		<b>Total</b>
		<b>Value (£)</b>	<b>Overview</b>	<b>Value (£)</b>	<b>Overview</b>	<b>Value (£)</b>	<b>Value (£)</b>
<b>Year 0-2</b>							
	<b>Overview</b>						
	<b>Social</b>						
<b>Year 3-6</b>							
<b>Year 7-10</b>							
<b>Total Costs</b>							

### 3.4 Appraising the Options

Having detailed the options, the next stage is to identify the preferred option. Assessing the options involves considering how they are likely to work in practice.

Where an Impact Assessment has been undertaken on the policy, the results should be considered as part of the appraisal process. The appraisal should also consider the costs and benefits of the option, both monetary and non-monetary, and the wider impacts of the policy in order to identify the best way forward.

It is therefore essential that you have sufficient evidence to properly consider the full range of options available. As part of the appraisal you will wish to consider your evidence base; the information on costs, benefits and risks; and the outcome of the impact assessment process. You will also wish to engage key stakeholders, particularly those responsible for delivering the policy.

There are a number of technical approaches to option appraisal. Two common approaches are Cost Benefit Analysis and the Weighted Scoring Method. Detailed guidance is available in the Northern Ireland Practical Guide to the Green Book. Professional colleagues can provide advice on which technique would best suit the needs of your policy and may also provide assistance in undertaking the option appraisal.

It is important to view option appraisal as a flexible tool, tailoring your approach to particular circumstances. The key aim of the appraisal is to identify which option offers an effective outcome with regard to the policy objectives, compared with the best value for money achievable. Take full account of the effect that each option would have for your stakeholders and delivery partners, and what doing nothing would mean.

### Output

The output for this stage should be an Option Appraisal Paper. There are a number of basic areas you will wish to consider as part of the option appraisal:

- (i) Effectiveness – will it achieve your objectives?
- (ii) Efficiency – will it achieve value for money?
- (iii) Inclusive – will it meet the diverse needs of stakeholders?
- (iv) Acceptability – will it meet with stakeholders' approval?
- (v) Policy fit – is it consistent with other major policy themes and legislative requirements?
- (vi) Powers – do you need new legislation?
- (vii) Implementation – is it practicable and deliverable?
- (viii) Timing – can you deliver it soon enough?
- (ix) Consequences – are there potential side effects?

Summarise your findings and be certain you can confidently recommend your preferred option as the best overall solution.