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An Analysis of the Sixth Government Report on the Costs and Benefits of Federal Regulations

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Executive Summary

This paper critically reviews the draft of the Office of Management and Budget's sixth report on the benefits and costs of federal regulation. The draft report represents an improvement over previous reports in some ways. For example, it aggregates costs and benefits for regulatory programs and expands the time frame of analysis to ten years.

While there has been progress, some useful innovations from last year are not included in this draft. Unlike last year's report, this year's draft report neither lists antiterrorism regulations by agency nor provides useful summary information on a number of OMB's regulatory oversight activities, such as return letters and prompt letters.

There is room for significant improvement. We offer five recommendations—one for Congress and four for OMB—that would help hold lawmakers more accountable for the regulations they produce. Our recommendations focus on getting the regulatory agencies to produce better analysis, making that analysis more transparent and readily available, and making the regulatory process itself more transparent.

We recommend that OMB include a scorecard that summarizes the extent to which regulatory analyses comply with OMB's guidelines for regulatory analysis; provide information on regulations addressing terrorist threats; summarize useful information on a number of OMB's regulatory oversight activities, including return letters, prompt letters, turnaround time, and regulations and programs recommended for improvement or reform; and ask independent agencies to provide annual assessments of the costs and benefits of their economically significant regulations. We also suggest that Congress require agencies to comply with OMB's information quality guidelines and guidelines for regulatory analysis.

An Analysis of the Sixth Government Report On the Costs and Benefits of Federal Regulations

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1. Introduction

The Office of Management and Budget (OMB) has just released a draft of its sixth annual report to Congress on the costs and benefits of federal regulation.¹ The law requires that OMB submit a report to Congress that provides estimates of the costs and benefits of federal regulation. The report is also supposed to make recommendations for reform, provide guidelines for agencies to standardize cost-benefit estimates, and assess the impact of federal regulation on State and local government, small business, wages and economic growth.²

The 2003 OMB draft report improves upon earlier reports in two ways.³ It aggregates costs and benefits for regulatory programs and expands the time frame of analysis to ten years. Unlike last year's report, however, this year's report neither lists antiterrorism regulations by agency nor provides useful summary information on OMB's regulatory oversight activities, such as return letters and prompt letters.

Our analysis of earlier reports suggested ways that OMB could improve its annual report. OMB has yet to implement some of these recommendations, so we have included them in this year's analysis.

¹ OMB (2003).

² The FY2001 Treasury and General Government Appropriations Act, § 624 (a) requires OMB to submit an "accounting statement and associated report" containing: "(1) an estimate of the total annual costs and benefits (including quantifiable and nonquantifiable effects) of Federal rules and paperwork, to the extent feasible: (A) in the aggregate; (B) by agency and agency program; and (C) by major rule; (2) an analysis of impacts of Federal regulation on State, local, and tribal government, small business, wages, and economic growth; and (3) recommendations for reform." Unlike reports from the past three years, this year's report does not address impacts of federal regulation on state, local, and tribal governments, small business, wages, and economic growth. The FY2001 Treasury and General Government Appropriations Act, § 624 (c) requires OMB to "issue guidelines to agencies to standardize: (1) measures of costs and benefits; and (2) the format of accounting statements."

³ Although the report is published in the Federal Register by OMB, the particular office within the Office of Management that is responsible for reviewing rules submitted by agencies, issuing information quality guidelines, issuing prompt letters, and enforcing Executive Order 12,866 is the Office of Information and Regulatory Affairs (OIRA). See Office of Management and Budget, OIRA Q&As. Available: http://www.whitehouse.gov/omb/info/q&a_2-25-02.pdf (last visited March 31, 2003).

We recommend that OMB include a scorecard on the extent to which regulatory analyses comply with OMB's guidelines for regulatory analysis; provide information on regulations addressing terrorist threats; summarize useful information about its regulatory oversight activities, including return letters, prompt letters, turnaround time, and regulations and programs recommended for improvement or reform; and ask independent agencies to provide annual assessments of the costs and benefits of their economically significant regulations. We also suggest that Congress require agencies to comply with OMB's information quality guidelines and guidelines for regulatory analysis.⁴

Section 2 identifies improvements in the report. Section 3 offers recommendations for improving OMB's report and regulatory oversight function. Section 4 presents our conclusions.

2. Improvements in the Report

There are two significant improvements in this year's report: new information on aggregate benefits and costs for select agency programs and an expansion of the number of years covered by OMB's cost-benefit estimates to ten years from the six and a half years presented in last year's report.

First, OMB estimates annual costs and benefits of select agency programs, such as "Energy Efficiency and Renewable Energy", "Food and Drug Administration", "Occupational Safety and Health Administration", "National Highway Traffic Safety Administration", "Coast Guard", "Office of Air", and "Office of Water."⁵ Aggregation of costs and benefits by program is a welcome improvement and can provide valuable information about a program's effectiveness.⁶

⁴ For OMB's Draft Guidelines for Conducting Regulatory Analysis, see OMB (2003). For a review of OMB's Draft Guidelines for Conducting Regulatory Analysis, see Hahn and Litan (2003). For OMB's Information Quality Guidelines, see OMB (2002b).

⁵ OMB (2003).

⁶ There are, however, some limitations to estimates of total costs and benefits by agency and program. OMB states, "More research is necessary to provide a stronger analytic foundation for comprehensive estimates of total costs and benefits by agency and program. OMB's examination of the benefits and costs of Federal regulation supports the need for a common-sense approach to modernizing Federal regulation that involves the expansion, modification, and rescission of regulatory programs as appropriate." OMB (2003, 5494).

Second, OMB has expanded the presentation of cost-benefit estimates from six and a half years to ten years. While there are many factors that should go into the choice of a reasonable time frame, we are in favor of this expansion. Cost-benefit estimation of a larger sample of regulations can not only yield a more credible conclusion about the effectiveness of regulation in general, but also can provide insights into the effectiveness of several major regulations.⁷

Although this progress is important, OMB can make further improvements. The following five recommendations aim to help improve OMB's annual report and the regulatory process.

3. Recommendations

We offer five recommendations: four apply to OMB and one applies to Congress.

Recommendation 1: OMB should publish cost-benefit estimates from independent agencies and request that those agencies provide assessments of the costs and benefits of their regulations.

In this year's report, OMB provides a table showing whether independent agencies monetized costs and benefits for economically significant regulations issued between October, 2001 and September, 2002.⁸ OMB, however, does not provide any monetized estimates of these regulations. In cases where the agencies have monetized benefits or costs, OMB should publish these monetized estimates and explain any uncertainties.⁹ In cases where independent agencies have not supplied benefit or cost information, OMB should ask them to estimate benefits and costs in the same format that

⁷ OMB, however, cautions that, "In order for comparisons or aggregation to be meaningful, benefit and cost estimates should correctly account for all substantial effects of regulatory actions, including potentially offsetting effects, which may or may not be reflected in the available data...Any comparison or aggregation across rules should also consider a number of factors which our presentation does not address." OMB (2003, 5494).

⁸ OMB (2003).

⁹ See Table 6, OMB (2003, 5498). The table, based on GAO reports, shows that the Securities and Exchange Commission (SEC) monetized benefits and costs for one economically significant regulation: "Books and Records Requirements for Brokers and Dealers under the Securities Exchange Act of 1934." The table also shows that the SEC monetized costs but not benefits for two economically significant regulations: "Certification of Disclosure in Companies' Quarterly and Annual Reports" and "Acceleration of Periodic Report Filing Dates and Disclosure Concerning Web Site Access to Reports." The table shows that no other independent agencies monetized benefits or costs for economically significant regulations.

executive agencies estimate them.¹⁰ Independent agencies, such as the Securities and Exchange Commission (SEC) and the Federal Communications Commission (FCC) recently issued significant regulations that could have benefited from benefit-cost analyses.¹¹

Recommendation 2: OMB should issue a scorecard assessing the extent to which agency regulatory analyses comply with its guidelines for conducting regulatory analysis.

Last year, we recommended that OMB issue a scorecard identifying the extent to which regulatory analyses comply with its economic guidelines.¹² OMB, however, has not yet implemented our recommendation.¹³ We encourage it to issue a scorecard for two reasons. First, a standardized evaluation will help the public to compare regulatory analyses. Second, a scorecard will give agencies the incentive to conduct higher quality regulatory analyses. We propose that OMB request the agencies to score their own regulatory analyses on a few criteria: whether the agency monetized or quantified costs and benefits, used the discount rates prescribed by OMB, and considered alternatives.¹⁴

¹⁰ Under Executive Order 12866, OMB can require independent agencies to summarize alternatives and preliminary estimates of anticipated costs and benefits for economically significant regulations. See Clinton (1993) for Executive Order 12866, § 4(c), which outlines “The Regulatory Plan”: “For purposes of this subsection, the term “agency” or “agencies” shall also include those considered to be independent regulatory agencies, as defined in 44 U.S.C. 3502(10). (1) As part of the Unified Regulatory Agenda, beginning in 1994, each agency shall prepare a Regulatory Plan (Plan)...The Plan shall be approved personally by the agency head and shall contain at a minimum:...A summary of each planned significant regulatory action including, to the extent possible, alternatives to be considered and preliminary estimates of the anticipated costs and benefits.”

¹¹ The recent Federal Communications Commission decision regulating the four regional Bell operating companies could have benefited from a regulatory impact analysis. The FCC issued a decision (3-2) relieving the Bell operating companies from giving rivals low-cost access to crucial elements of their high-speed Internet networks, but requiring them to continue leasing their local phone networks to rivals at low prices set by state regulators. See “Local Phone Rules to Stay in Place,” *New York Times*, Friday, February 21, 2003.

¹² For OMB’s Draft Guidelines for Conducting Regulatory Analysis, see OMB (2003). For a review of OMB’s Draft Guidelines for Conducting Regulatory Analysis, see Hahn and Litan (2003). For an example of a scorecard, see Table 4, Hahn and Sunstein (2002, 1519).

¹³ Hahn and Litan (2002, 11).

¹⁴ For a discussion of alternatives, see Hahn et. al. (2000, 874-875): “Unfortunately, the agencies generally did not provide a significant analysis of alternatives in RIAs, even when the agencies conducted a quantitative analysis of the preferred option...This incomplete assessment of alternatives makes it difficult to assess whether the alternatives would actually be superior to an agency’s preferred policy, even when using an agency’s own assessment.”

OMB should confirm the accuracy of the completed scorecard and summarize the results in its report.¹⁵

Recommendation 3: OMB should provide information on regulations addressing terrorist threats.

In last year's report, OMB provided a table with information on regulations addressing terrorist threats.¹⁶ We encourage OMB to add a table similar to last year's table of all antiterrorism regulations issued since September 11, 2001.

We are pleased to see that OMB has requested public comments on how to analyze the costs and benefits of future rulemaking in general.¹⁷ We think, however, that OMB should go further and request the agencies to analyze the costs and benefits of current antiterrorism regulations.¹⁸ Moreover, OMB could develop ways to measure the regulations' effectiveness. While determining precise quantitative estimates of benefits is often difficult, some quantitative or qualitative description is possible. An attempt at measuring the net benefits of terrorism-related regulations will help policy makers and the public to compare the merits of different regulatory options and assess whether these regulations are meeting expectations.¹⁹

Recommendation 4: OMB should provide useful summary information on its regulatory oversight activities, including return letters, prompt letters, turnaround time, and regulations and programs recommended for improvement or reform.

In last year's report, OMB included information on the number of return letters issued by OMB between 1981 and 2001, number of prompt letters, turnaround time, and regulations publicly nominated for improvement or reform.²⁰ In this year's report, OMB does not mention the return letter, prompt letter, or turnaround time. Although return letters, prompt letters, and turnaround time are posted on the OMB website, a welcome

¹⁵ OMB should go further and offer its in-house expertise to assess the quality of agency regulatory analyses. See Hahn and Litan (2002, 11) for a discussion of OMB's in-house expertise: "The major advantage that OMB analysts have over other potential authors of this report, such as academics, is that they are more familiar with the details of particular regulations and regulatory analyses."

¹⁶ See Table 1, OMB (2002, 7-9). The table includes information on the issuing agency, sub agency, and rulemaking stage.

¹⁷ OMB (2003).

¹⁸ Hahn and Litan (2002).

¹⁹ For a discussion of how the government can effectively deal with the risk of terrorism, see O'Hanlon et. al. (2002).

development, OMB does not summarize their status in a table.²¹ OMB should summarize turnaround time, return letters, and prompt letters in the report, highlighting important concerns that it has raised in the letters. OMB ought to note, for example, when it returns a rule because of insufficient analysis and when it returns a rule because costs exceed benefits. It should also note how an agency responds to specific letters.²² This summary would provide the public with useful information on the nature of OMB's concerns and the responsiveness of the agencies to those concerns.

In addition, we suggest that OMB list regulations and programs recommended for improvement or reform. Although OMB has tabulated estimates of costs and benefits for regulations and programs in this year's report, it has not listed the regulations or programs that should be targeted for reform.²³

Recommendation 5: Congress should pass a law requiring that all regulatory agencies comply with OMB's guidelines for regulatory analysis and information quality guidelines when analyzing the impact of economically significant regulations.

There are three sets of guidelines issued by OMB with which the agencies should comply when they issue regulations.²⁴ Unless the President decides that a regulation addresses an emergency, Congress should require that the proposed regulations not move forward if the agencies' Regulatory Impact Analyses fail to meet the guidelines. OMB's guidelines provide a set of principles for improving regulatory analysis and making the

²⁰ See OMB (2002, 14-23) for information on turnaround time and the status of prompt letters and return letters. Last year's report also contains a table describing the status of draft rules returned.

²¹ See OMB website at http://www.whitehouse.gov/omb/inforeg/return_letter.html (last visited Mar. 31, 2003) for return letters, http://www.whitehouse.gov/omb/inforeg/prompt_letter.html (last visited Mar. 31, 2003) for prompt letters, and <http://www.whitehouse.gov/omb/library/OMBARYTD-2002.html> (last visited Apr. 2, 2003) for turnaround time on individual regulations.

²² Hahn and Litan (2002).

²³ See Appendix A and Appendix B, OMB (2003) for OMB's and agencies' estimates of the costs and benefits of individual regulations. OMB not only can rely on public nominations for regulations and programs needing reform, but also can also apply its own in-house expertise to suggest possible regulations and programs in need of reform.

²⁴ The guidelines are: OMB Draft Guidelines for the Conduct of Regulatory Analysis and the Format of Accounting Statements, which will be finalized this fall and will replace the Guidelines to Standardize Measures of Costs and Benefits and the Format of Accounting Statements; Guidelines for Ensuring and Maximizing the Quality, Objectivity, Utility, and Integrity of Information Disseminated by Federal Agencies, which were republished on February 22, 2002; and M-00-02, Guidance for Implementing E.O. 13132, "Federalism", which was published on October 28, 1999. See OMB (2003), OMB (2002b), OMB (1999b).

regulatory process more transparent. They should be required for all economically significant regulations from both independent and executive agencies.

Currently, OMB has no mechanism for enforcing its guidelines. Previous efforts to enforce similar guidelines have been unsuccessful.²⁵ Moreover, agencies often fail to clearly communicate their findings.²⁶

If Congress does not pass the law that we recommend, enforcement authority for implementing the guidelines should be included in a new Executive Order.

4. Conclusion

This analysis critically reviews the draft of the Office of Management and Budget's sixth report on the benefits and costs of federal regulation. The draft report is an improvement over previous reports. We think that the changes that OMB has made to increase and improve coverage of regulations and programs are significant. These include expanding the time frame to analyze major regulations from six and a half years to ten years and estimating costs and benefits for programs within agencies.

There is room for substantial improvement, however. We offer five recommendations—four for OMB and one for Congress—that would help hold regulators and lawmakers more accountable for the regulations they produce. Our recommendations focus on getting the regulatory agencies to produce better analysis, making that analysis more transparent and readily available, and making the regulatory process itself more transparent.

²⁵ See, for example, Figure 5 in Hahn et. al. (2000, 875), suggesting that agencies often do not quantify the impacts of alternatives in RIAs.

²⁶ See Hahn and Litan (1997) and Arrow et. al. (1996). See also Hahn (1999) for a specific suggestion for summarizing results in a "Regulatory Impact Summary" and using the *Federal Register* to communicate findings of the regulatory analysis in a clear, concise fashion.

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